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**Research Report**

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## Russia: Turn to China?

*Margarete Klein and Kirsten Westphal*

After its relations with the West deteriorated massively in the course of the Ukraine crisis, Russia has been aligning itself increasingly towards China. This shift is most obvious in the strategic spheres of military and energy cooperation. Even if the immediate impacts on Germany and the European Union – caused by the dynamics in the relationship between these two major neighbours in the East – are limited, the development is of great relevance for international relations and the global order. It would therefore be wrong to underestimate the long-term ramifications. Germany and the European Union should counterbalance these nascent tectonic shifts with inclusive and multi-lateral cooperation and dialogue initiatives in the Euro-Asian region. Regional and global cooperation should be shaped by economic exchange, infrastructure expansion and the search for solutions to global problems.

Moscow has been successively expanding its relations with Beijing since the end of the Cold War – from the “constructive partnership” (1994) and the “strategic partnership of cooperation” (1996) through to the “comprehensive, deepening strategic partnership” (2010). Whereas overcoming bilateral tensions was uppermost from the 1960s to the 1980s, since the mid-1990s the pair have been cooperating wherever shared interests exist. These extend from rejection of what is felt to be a US-dominated world order and associated “colour revolutions” through the wish for political stability in the shared Central Asian neighbourhood to the expansion of bilateral economic relations. The growing importance of Asia is also reflected in Russia’s foreign trade. Since 2008 Russia has been importing more

goods from China than from Germany, while the two alternate as first and second destination for its exports. Military and energy cooperation are especially strategic. China’s rise, the American “pivot to Asia” and Moscow’s desire to play a greater role again in East Asia have further boosted the Russian “povorot na vostok” (turn to the East) and its China policy since the end of the 2000s. But it is only since relations with the West collapsed in the course of the Ukraine crisis that Russian political discourse has begun presenting convergence with Beijing not just as a supplement to its relations with the West, but as a long-term reorientation and rejection of the West.

## Security and Military Policy

In the area of security Moscow has been pursuing a dual strategy towards Beijing. Its *first pillar* is formed by engagement such as military/political dialogue, joint exercises and armaments cooperation designed to improve mutual trust and transparency and facilitate a joint threat response. Both countries feel threatened by spillover effects from the Central Asian neighbourhood, including Islamist extremism, terrorism and drug trafficking, but also by the United States's superior military capabilities. Domestically Beijing and Moscow share concerns about "colour revolutions", which they both regard as Western-inspired insurrection seeking regime change. Above all, the Kremlin uses joint military exercises as a show of strength towards NATO and the United States.

Moscow also worries about China's rise and long-term intentions, even if this has never appeared in any official document out of political consideration for the "strategic partner". Since the end of the Cold War the power relationship between China and Russia has reversed, to the latter's detriment. For example, today China's GDP is more than four times Russia's. In the military sphere, while Russia can continue to rely on its lead in nuclear weaponry, China's conventional forces are already in many respects quantitatively and qualitatively superior. In 2014 the Chinese People's Liberation Army possessed more than three times as many soldiers than the Russian armed forces, as well as a clear numerical advantage in tanks and warplanes. Beijing's \$129 billion defence budget for 2014 was almost double Russia's (\$70 billion).

The Kremlin is aware that China's military expansion is directed primarily against the United States rather than Russia, and intended to back up its claim to leadership in East Asia. But the growing military imbalance contains the danger of Beijing acting more assertively towards Moscow in future conflicts, for example over access to resources in Russia's Far East. For this reason, the *second pillar* of Moscow's dual

strategy is to foster indirect balancing against China. This includes preserving its defensive capability towards China by modernising its nuclear arsenal and expanding its strategic air defences in the East. Russia is also working to contain China in two respects: On the one hand, it supplies modern weapons systems to countries that are China's rivals or involved in territorial conflicts, such as India and Vietnam. On the other, it avoids supplying China with the very latest Russian weapons systems.

Since the outbreak of the crisis over Ukraine, Moscow has concentrated one-sidedly on expanding the cooperation pillar of its dual strategy, as reflected above all in an increase in the frequency, scope and intensity of joint manoeuvres. After a long period where Sino-Russian military exercises were restricted to the border region and the shared Central Asian neighbourhood, in 2015 the two navies exercised jointly for the first time in the Mediterranean (May) and the Sea of Japan (August). The spectrum of operations has also been broadened from fighting terrorism, insurgency and piracy to repelling enemy attack and even offensive operations. In August 2015, for example, Russian and Chinese marines together practised an amphibious landing for the first time. The degree of interoperability is also increasing. Whereas previous Sino-Russian exercises tended to proceed as parallel manoeuvres by the two forces, since 2014 some Russian and Chinese soldiers have been training in mixed groups under joint command. Moscow and Beijing are naturally still a long way from being able to conduct a major integrated operation. But they are expanding their ability to conduct joint military operations in local and regional conflicts, especially in the Central Asian neighbourhood.

The two sides have expanded cooperation in other spheres of security, too. The framework agreement on cooperation on questions of international information security, signed by Moscow and Beijing on 30 April 2015, is especially significant. In it the two sides promise to refrain from cyber-

attacks on one another and to take joint action against “technologies” that endanger the “security and stability” of the state or seek to “destabilise the socio-economic situation” internally. As such both sides are enhancing their coordination, both in cyber-defence against third states and with respect to state control of the internet and thus the prevention of “colour revolutions”.

While substantially expanding its security cooperation with Beijing, Moscow is finding it increasingly difficult to maintain the countervailing force pillar of its dual strategy at the existing level. Although the Kremlin can continue to rely on its nuclear deterrent and is continuing defence cooperation with Vietnam and India, it has had to abandon its previous caution over arms exports to China. Although Russia has been China’s largest arms supplier since the 1990s, it has in the past refrained from exporting the latest developments to China out of security concerns, and to some extent fear of product piracy. But in April 2015, according to press reports, Moscow signed a deal to supply S-400 anti-aircraft systems, even if many details – including the delivery date and precise type of missile – remain unclear. Talks are still ongoing over the sale of the latest warplane, the Su-35.

Exporting such weapons systems is not only militarily sensitive, but also politically. If the S-400 version with a range of four hundred kilometres is supplied, this would enable China not only to penetrate Taiwanese airspace, but also to operate over the Senkaku/Diaoyu Islands, which are contested between Japan and China. In strengthening China’s ability to project power, Moscow is undermining its own hitherto neutral position in territorial conflicts in the South and East China Seas. Another sign of Moscow quietly abandoning its neutrality and supporting Chinese hegemonic strivings was the Russian navy’s first joint manoeuvre with China in the Sea of Japan in August 2015. Previously consideration for Japan would have precluded such a move. These latest arms sales and

manoeuvres narrow Moscow’s options in East Asia.

## Energy

Europe has traditionally been the most important market for Russian oil and gas. Almost two-thirds of Russia’s oil and nearly half of Gazprom’s gas production are exported to the European Union. The complementarity between a resource-poor consumer region and an energy-rich producer, as well as their geographical proximity, have promoted expansion of infrastructure and trade over many decades. In the coming decade too, Europe will remain Russia’s largest export market.

When relations with the European Union deteriorated in the wake of the Russian-Ukrainian gas crises of 2006 and 2009 and the implementation of the EU’s third internal energy market package in 2009, Moscow repeatedly threatened to redirect gas exports eastwards. Since 2014 geopolitical considerations have accelerated energy cooperation with China.

In fact, geoeconomic shifts alone would be reason enough for Russia to diversify towards Asia, as the international energy markets are presently characterised by deep and rapid change. Demand for oil and gas is growing above all in the Asia-Pacific region, whereas consumption in Europe is stagnating or falling. As a traditional pipeline exporter, Russia has largely missed out on an increase of more than one quarter in trade in liquefied natural gas (LNG) over the past decade. Only since 2010 has Russia – the world’s largest gas exporter – been exporting LNG from its Sakhalin II Terminal, and even then this amounts to just 4 per cent of the total global LNG supply. Fracking in the United States has also considerably increased the global oil and gas supply. Russia finds itself exposed to growing competition not only in the global markets, but also in its traditional pipeline market in Europe.

Russia therefore needs to diversify its exports and flexibilise its transport options

and contract structures if it is to defend its export markets. In 2010 Russia's "Energy Strategy 2030" set a goal of expanding sales to Asia, further concretised at the beginning of 2014: by 2025 oil and gas exports to Asia are to be doubled. Late, but energetically, Moscow is working to advance the "povorot na vostok" in the sphere of energy, for example via repeated alterations to the tax system since 2013. This is of great importance to the Kremlin not only in terms of foreign trade, but also for the economy as a whole, because its "Gas Programme for the East" adopted in 2007 proposes developing the gas sector in Eastern Siberia and the Far East. Thus from an economic perspective it makes sense to expand the gas fields and infrastructure both for domestic demand and for export.

The turn to Asia in fact follows a similar logic to the close energy partnership between Russia and Western Europe in the second half of the twentieth century: energy-rich Russia cooperates with energy-hungry China. However, manifestations of crisis in the Russian economy, low oil prices and sanctions are producing unwanted effects and hampering both infrastructure expansion and the development of new fields. Western sanctions target the neuralgic technologies required to rapidly expand market share in Asia: the exploitation of shale oil and tight oil formations and deep-sea projects in the Arctic and off Sakhalin Island. Financing through the international capital markets is also restricted. With access to Western financial markets subject to sanctions, Russia all the more urgently needs hard currency revenues. The situation of Russian energy giants like Rosneft and Gazprom also depends on their hard currency revenues and the ratio of rouble to hard currency expenditure.

Although the crisis over Ukraine has acted as a catalyst to intensify and accelerate Sino-Russian cooperation, Russia's means for implementing the turn to China while guarding its strategic interests are shrinking. The Power of Siberia gas pipeline agreed in May 2014 was supposed to come

on stream at the end of 2017, supplying China with 38 billion cubic metres of natural gas annually for thirty years. Even at the time the deal was signed, it was regarded as unlikely that the project would turn a profit for Gazprom until the 2020s. But now high development and construction costs and the unfavourable turn in gas prices are burdening the operator even more strongly than expected and the project is suffering delays. This is in fact not unwelcome for China, which is experiencing structural adaptation processes in the economy as a whole that will slow growth in demand and reform its gas market and gas pricing mechanisms. Under these circumstances the "West route", the so-called Altai Pipeline with a projected initial annual capacity of 30 billion cubic metres, can be regarded as a remote prospect at best. This situation presents Gazprom with a dilemma: Its gas fields in the East are still in the development phase and lack treatment facilities to supply gas in the required dry quality via the Power of Siberia pipeline. At the same time the company finds itself confronted with a potential gas surplus in Western Siberia, where it has developed fields for the European market whose gas is now no longer required. From that perspective, the West route would make more sense for Gazprom, as it would permit a flexibilisation of exports. But it would end in the province of Xinjiang, far from the centres of consumption – just where the pipeline from Central Asia ends too. Russian and Chinese interests are thus only partially compatible and characterised by asymmetry.

In the Russian oil sector, on the other hand, growing Chinese long-term investment is already flowing and the Siberian fields have been connected to the Chinese market. In 2002 oligarch Mikhail Khodorkovsky's energy company YUKOS (since broken up) raised hackles in the Moscow establishment with its plan to build a pipeline to China. But by 2008 Russian state-owned companies Rosneft and Transneft had reached agreement with China on joint funding of the Eastern Siberia Pacific Ocean

(ESPO) pipeline in return for 15 million tonnes of crude annually for twenty years. The first deliveries to Daqing in China occurred in 2011. ESPO is now the world's longest oil pipeline, with a capacity of one million barrels per day. It branches near the Russian town of Skovorodino, with one spur going to China, a second to the Russian export port of Kozmino. Between 2010 and 2014 Russian crude oil exports to China more than doubled to almost 30 million tonnes. China now accounts for a good 13 percent of Russia's crude oil exports.

The sanctions against Russia open up new possibilities for China, because approval processes have made importing technology from the West slower and more complicated, and above all refinancing of projects has become more laborious. The difficult situation has led Russia to open up resources that had previously been earmarked as strategic and relevant for the national interest to Chinese investors and to rely on importing crucial technologies from China. Thus Rosneft is negotiating with the state-owned China National Petroleum Corporation (CNPC) to sell a 10 percent stake in the Vankor oilfield – the main source of oil transported through the ESPO pipeline. Rosneft is already cooperating with the Chinese oil and gas company Sinopec to develop tight oil fields in Eastern Siberia, and CNPC is a partner in the project to liquefy natural gas on Russia's Yamal Peninsula. And Russia and China are intensifying their cooperation in other parts of the energy sector too, the strategically most important being civil nuclear technology. The two countries are competitors here, but can also profit from cooperation.

### **Symbolic Politics with Substance**

Russia's turn to China represents more than mere symbolism. In recent years it has significantly gained in substance in almost all areas.

China has become the country outside the post-Soviet space with which Russia maintains its closest military relations.

Intensified exercise activities will make it easier for them to take joint action in future, especially in Central Asia. In cybersecurity, too, Beijing and Moscow are significantly expanding their coordination. Yet Western worries about a formal Russian-Chinese military alliance are exaggerated. Neither side is seriously interested in such a move, which would restrict their own freedom of action.

Cooperation in the field of energy is also currently being expanded. This allows both sides to diversify their trade relations and Russia to gain market share in China.

Nonetheless Russia's turn to China should not be overrated. Cooperation has its limits, and despite cooperation arenas of conflict that could burden the relationship in future still remain. Moreover, since the end of the Cold War the bilateral balance of power has altered to Moscow's detriment in almost all aspects. Russian hopes of playing China and the West against each other as a sought-after "swing state" had already proven over-optimistic before the crisis over Ukraine. Now Russia is even losing the ability to assert its interests on equal terms. So the costs of the turn to China are considerable for Russia. Short-term interests in political symbolism and tangible economic necessities override long-term strategic considerations. As a consequence Moscow's leeway shrinks.

Moscow has pursued a strategy of expanding political and economic relations with all countries in the Asia-Pacific region. But the "povorot na vostok" – actually conceived as a turn to East Asia as a whole – now threatens to shrink to a turn to China. Although Russia is still making overtures to Japan on security and energy, Japanese sanctions and intensified Sino-Russian military cooperation have noticeably darkened the relationship with Tokyo. Moreover, growing financial constraints are narrowing Russia's possibilities to expand infrastructure for exports to other Asian markets.

Russia's strategy of flexibilising its exports with the help of natural gas liquefaction and new pipelines encounters its

limits in the partnership with China. Being so closely tied to a single purchaser now impinges on its role as a global exporter. For example, expanding Russian ESPO exports to Daqing undermines the goal of establishing ESPO blend crude as a new price reference by withdrawing volume from the spot market in Kozmino. China has not only secured specific volumes for twenty years, but also a particular quality of crude.

As Russia gradually exhausts the financial resources it needs to respond adequately to the geoeconomic shifts, the Kremlin increasingly turns to symbolic politics and demonstrations that the country is not isolated internationally. The focus here is on the Eurasian Economic Union (EEU) and cooperation with China. Cooperation with other emerging economies, like the BRICS summit hosted in the Russian city of Ufa in June 2015, and the Shanghai Cooperation Organisation (SCO), also gains in importance in this context. But in these formats it is China that is increasingly setting the agenda, as reflected in Russia's agreement at the SCO in Ufa to seek integration of the EEU with the Chinese Silk Road Initiative ("one belt, one road", OBOR). Both these projects were concretised during the Beijing International Economic Forum in September 2015 in a cooperation agreement and various other arrangements in the context of the Silk Road economic alliance.

### **Repercussions for Germany and the European Union**

Russia is seeking to play the China card in its conflicts with the European Union, NATO and the United States. But the threat scenario this generates is not terribly credible, because Moscow and Beijing ultimately remain a long way from forming any kind of formal anti-Western alliance. Nonetheless, long-term consequences are becoming visible for global and regional order(s) and governance in important policy fields.

Moscow and Beijing share important criticisms of Western-dominated governance

structures and principles, and are joining forces to either modify these to their satisfaction or to weaken them through alternative forums like BRICS. This could reduce the West's ability to set the global agenda and determine the framing of international politics.

This also touches on the attractiveness and legitimacy of political systems. Russia and China are keen to establish a narrow interpretation of the humanitarian responsibility to protect and to popularise their interpretation of the "colour revolutions" as new form of Western warfare. Above and beyond the normative level, both countries are expanding their ability to defend against "colour revolutions", as demonstrated by their cyber-cooperation. A situation of closer relations between Russia and China also possesses the potential to bolster authoritarian systems and undermine the Western model of liberal democracy and rule of law.

This alliance also possesses the potential to change the existing liberal economic order, which is heavily based on free trade, investment and access to resources – although not to completely supplant it. After all, Russia and China also profit from functioning markets. But situations of scarcity could lead both to cease relying entirely on market forces, instrumentalising instead the close ties between state-owned companies along the value chain. Both are also united by their wish to break the dominance of Western currencies and structures in international financial transactions (such as the Society for Worldwide Interbank Financial Telecommunication, SWIFT). Both are dissatisfied with the international architecture of Bretton Woods and the institutions dominated by the OECD. That is behind their participation in founding new institutions such as the Asian Infrastructure Investment Bank and the New Development Bank (BRICS).

At the same time Russia and China are working on a restructuring of economic spaces. This can be observed in their talks about reducing barriers to trade, and above

all in infrastructure expansion. Joining OBOR with the Eurasian Economic Union and expanding the Shanghai Organisation by admitting observers such as Mongolia and Iran creates new realities for Western influence and presents the EU's Central Asia Strategy, for example, with new challenges. It also hampers Europe's efforts to diversify its energy sources.

Closer relations between Russia and China also have repercussions for bilateral energy relations between Russia and the European Union. Although in the short and medium term the EU remains the most important market for Russia – which urgently needs the revenues to fund projects orientated towards Asia – in the longer term its importance for Russian energy exports is likely to shrink (in relative terms). Firstly, consequences for quality and quantity are to be expected, as Russia diverts increasing amounts of eastern Siberian high-quality light crude from towards Asia to meet its pledges on volume and quality. Secondly, structural shifts may occur. If European companies lose out to Chinese rivals over access to the Russian market, this will narrow their market access and capitalisation. In the longer term this could seriously disrupt the functioning of the free market, above all if supply is further constricted. It is also Western firms that possess the production-boosting technologies required to maintain Russia's oil production at a high level.

There is also a risk of the international governance of energy relations becoming drawn in sooner or later in. To date it has been shaped by the organisations and mechanisms initiated by the OECD states after 1973 and the G8 states after 2007. These include the International Energy Agency (IEA) with its collective crisis mechanisms, and transparency initiatives like the Joint Organisation Data Initiative (JODI) at the International Energy Forum (IEF). Geopolitical distractions have also held up the IEA's association process, which had been advancing steadily since 2007 and also included Russia and China.

## Conclusion and Recommendations

Closer relations between Russia and China represent a challenge for Germany and Europe. Their cooperation has grown more substantial and could in the longer perspective restrict European options and fundamentally alter the global framework. Germany and Europe should devote greater attention to this development and include it in their strategic considerations.

It is not in the German or European interest for Russia to become a junior partner one-sidedly strengthening China's position, nor for the global and regional convergence between Beijing and Moscow to proceed at the expense of Europe's policy options. It would therefore be advisable to resume pragmatic cooperation with Russia in fields of shared interest. In a "compartmentalised" form this would mean restricting the negative spillover effects of the crisis over Ukraine on other regions and the global level. But any watering down of the Minsk II agreement should be avoided. Shared interests exist, for example, in stabilising Afghanistan and the Middle East, in non-proliferation policy and in fighting terrorism and Islamist extremism. As far as East Asia is concerned, it would be in the interests of both Russia and the European Union to find peaceful resolutions to the North Korean nuclear issue and the territorial disputes in the East and South China Seas. The European Union should therefore step up its political dialogue with Russia on East Asia.

States in the Euro-Asian region that find themselves being sucked into the Sino-Russian spheres of influence should be offered alternative courses of action. The Organisation for Security and Cooperation in Europe (OSCE) should place a connectivity initiative of its own alongside China's Silk Road Initiative.

Energy and economic relations in the Euro-Asian region should not be further securitised. The guiding principles should instead be trade, interdependency and infrastructure expansion.

To date the European Commission has prioritised bilateral dialogues and the Euro-



pean Energy Community in the immediate neighbourhood. This approach is geographically and substantively short-sighted. It needs to be backed up with inclusive regional governance initiatives (such as the OSCE, the Energy Charter process and the UN Economic Commission for Europe, UNECE), to develop agreed sets of rules. At the global level, finally, the inclusion of influential states in the IEA needs to be pushed more energetically, because the establishment of parallel institutions runs counter to Western interests.

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