

The Strategy Research on Chinese Direct Investments in Russia under the Belt and Road Initiative

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Abstract: The purpose of this study is to examine the characteristics and problems of Chinese direct investment in Russia. This paper first demonstrates the background of proposing of Belt and Road Initiative and its meaning and importance to facilitate both Chinese and Russia economic development. Then the study summarises the characteristics of the past Chinese direct investments in Russia and the current problems that Chinese enterprises have been encountered when they operating in Russia. In the end, this study brings forward the related countermeasures and strategy suggestions accordingly, hoping to further strength the economic links between China and Russia and further facilitating Chinese direct investment in Russia.

1. Introduction

Russia, the largest country in the world, owns abundant resources of land, oil and natural gas. China, who has the largest population, with its rapid economic development, also plays an increasingly important role in the world economy, as well as in the region economy. Because of close geographic links and rich natural resources, Chinese direct investment has been attracted to Russia for the past decades, and the investment cooperation has been further strengthened after the emergence of Belt and Road Initiative.

“One Belt, One Road” Initiative was proposed in 2013, when Chinese President Xi Jinping paid a visit in Kazakhstan. It consists of two perspectives, one is Silk Road Economic Belt and other one is 21st-Century Maritime Silk Road. The initiative attracted considerable attention from the international community and won a positive response from the countries involved. It integrates the historical symbolism of the ancient Silk Road with the new requirements of today. The initiative is a Chinese program whose goal is to maintain an open world economic system, and achieve diversified, independent, balanced, and sustainable development, and also a Chinese proposal intended to advance regional cooperation, strengthen communications between civilizations, and safeguard world peace and stability.

Russia has taken a crucial position in Belt and Road Initiative due to its prominent geographical location. Moreover, Russia is the founder of Asian Infrastructure Investment Bank. It is without doubt that the construction of Belt and Road Initiative will provide new vitality and opportunities for China-Russia cooperation and economic development.

It has been five years since the proposition of Belt and Road Initiative, and the China-Russia investment cooperation has achieved unprecedented results through the joint efforts of both countries' governments. This paper will make a research of current investment cooperation between China and Russia, conclude the achievements and find out the major existed problems. Based on the analysis, this paper will bring forward practical policy suggestions for the future investment cooperation between China and Russia.

2. Analysis of Current Chinese Direct Investments in Russia

It has been more than 60 years since the establishment of diplomatic relationship between China and Russia. The strategic partnership of coordination between China and Russia has become increasingly mature and steady. With the proposition of Belt and Road Initiative in 2013, the relationship between China and Russia shows a historic breakthrough and development.

2.1. Historical Review of Chinese Investment in Russia

During the past twenty years, the relationship between China and Russia has been warming up rapidly, and both political and economic aspects have achieved great development and progress. China and Russia formally established their cooperative partnership in 1996, which promoted Chinese direct investment in Russia greatly. In 1997, China's direct investment in Russia reached \$1.19 million, achieving an increase of 1390% compared with 1996.

The demand for energy in the world has been growing rapidly since 2000, and China is one of them that desire resources badly due to its large population and shortage of energy resources. Russia is rich in energy resources. Therefore, Russia has fully seized this opportunity and made use of energy advantages to achieve rapid economic development. China increased its direct investment in Russia, especially in the energy industry. In 2000, China's direct investment in Russia reached 14 million US dollars.

When it comes to 2005, China's direct investment in Russia exceeded 100 million US dollars for the first time, reaching \$203 million. During 2005-2007, China's direct investment in Russia increased rapidly and the Chinese government has strongly encouraged domestic companies to invest in Russia and has set a target of \$12 billion by 2020.

Because of Financial Crisis in 2008, however, China's direct investment in Russia was only \$395 million, showing a negative trend for the first time. In 2009, the investment in Russia fell further to \$348 million. Since 2010, the global economy began to recover slowly and the international oil price began to rise, which brought good opportunities for the recovery of Russian economy. China has further strengthened its strategic cooperation with Russia, promoting the level of China's direct investment in Russia. China's direct investment in Russia reached a new high of \$568 million in 2010.

By the end of August, 2013, 4th Investment cooperation between China and Russia was held in Moscow. "Memorandum of Understanding about the Implementation of 'Sino-Russia Investment Cooperation Plan'" has been signed on the meeting, indicating a new form of cooperation will be seen in the future, rather than the old forms of economic cooperation that has been used for the past 20 years.

In October, 2013, after the proposition of Belt and Road Initiative, China and Russia signed a joint statement on how to link and cooperate with the construction of the Silk Road Economic Belt and the construction of the Eurasian economic union. It is stated that Russia is willing to carry out more in-depth cooperation with China to jointly build the Silk Road Economic Belt, and China will also support Russia's integration process within the framework of the Eurasian economic union (EEU) and immediately start relevant consultations with the EEU. Based on the in-depth

cooperation in both economic and political area for the past decades, Chinese direct investment in Russia has experienced dramatic development. In 2013, China’s direct investment in Russia reached a record high of \$1.022 billion, with a year-on-year increase of \$237 million.

Due to Russia's interference in Ukraine in 2014, however, the group led by the United States and European powers began to impose economic sanctions against Russia, which put Russia's economy at risk. The first sanction was to freeze the bank accounts of Russians in relevant countries overseas and refuse their entry. A second wave of sanctions were triggered by the deterioration of the situation in the east of Ukraine, due the beliefs of some western countries that Russia was the main causes of such situation. The scope of the sanctions imposed against Russia has been further expanded, not only limited in the area of economic, but also covered the usage of Russian energy such as natural gas, and so on. The third wave of sanctions covered an even large scope of Russian economy, including Russian Banks, oil and gas companies. It has been banned to provide any loans or bonds to Russia, sell the advanced drilling equipment to energy companies, or purchase Russian technology. These things led to the falling of the stock market because of the instability of the roubles. As a result, the sharp depreciation of the Russian economy and rouble has deterred Chinese direct investments, joint ventures and trade with Russia.

2.2. Analysis of Current Chinese Direct Investment in Russia

2.2.1. Chinese Direct Investment Scale in Russia

In 2017, Chinese investments in Russia were 1548 million US dollars, ranked number 4 among all the Europeans destinations of Chinese outward FDI and number 12 of all destinations. At the end of 2017, China’s investment stock in Russia was 13.872 billion US dollars, accounting for 0.8% of China’s OFDI stock and 12.5% of China’s investment stock in Europe.

Table 1 and Table 2 indicate China’s direct investments in Russia from 2007 to 2017. Chinese investment in Russia shows a continuous growing trend, although experienced some fluctuation, and reaches its highest record in 2015.

Table 1: China’s direct investment in Russia, flow.

Millions of US dollar

2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
478	395	348	568	716	785	1022	634	2961	1293	1548

Data resource: National Bureau of Statistics of China

Table 2: China’s direct investment in Russia, stock.

Millions of US dollar

2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
1838	2220	2788	3764	4888	7582	8695	14020	12980	13872

Data resource: National Bureau of Statistics of China

2.2.2. Chinese Direct Investment Industry Distribution in Russia

In terms of industry distribution, Chinese investment flows to Russia mainly concentrated in mining (38.7%), agriculture/forestry/animal husbandry/fishery (18.7%), finance (10.4%), manufacturing (8.5%), wholesale and retail (6.5%), scientific research and technical services (6.5%) in 2017, as demonstrated in Table 3.

By the end of 2017, a total of nearly 1,000 overseas enterprises have been set up by Chinese companies in Russia, employing 20,000 foreign employees. From the distribution of main industries,

mining industry is 6.592 billion US dollars, accounting for 47.5%; agriculture/forestry/animal husbandry/fishery is US \$2.702 billion, accounting for 19.5%; manufacturing is \$1.574 billion, taking up to 11.3%; leasing and business services is \$924 million, approximately 6.7% of the total.

Table 3: Major sectors of Chinese direct investment in Russia in 2017.

Industry	Millions of US Dollars			
	Flow	Share (%)	Stock	Share (%)
Mining	599.46	38.7	6591.51	47.5
Agriculture, Forestry, Animal Husbandry, Fishery	289.90	18.7	2701.66	19.5
Manufacturing	130.98	8.5	1574.08	11.3
Leasing and Business Services	36.88	2.4	923.97	6.7
Financial Services	160.87	10.4	495.13	3.6
Wholesale and Retail Trade	101.13	6.5	483.68	3.5
Real Estate	51.09	3.3	403.50	2.9
Construction	48.84	3.2	297.68	2.1
Scientific Research and Technical Services	100.21	6.5	151.48	1.1
Information Transmission, Software and IT Services	0.44	0.0	111.39	0.8
Transportation, Storage and Postal Services	22.48	1.5	79.10	0.6
Resident Services, Repairs and Other Services	0.12	0.0	27.97	0.2
Other	6.02	0.3	30.45	0.2
Total	1548.42	100.0	13871.60	100.0

Data resource: National Bureau of Statistics of China

2.2.3. Regional Distribution of Chinese Investment in Russia

From the regional distribution of Chinese investment in Russia, it is found that most enterprises are located in Moscow or near a large city, such as St. Petersburg. These regions are preferred mainly because of their relatively good economic development, well-constructed infrastructure, and relatively high consumption level. Therefore, there are hundreds of Chinese companies investing in Moscow, including many powerful Chinese companies, such as Huawei Group, China Construction Corporation and Shanghai Industrial Group.

With the deepening of economic and trade cooperation between China and Russia, as well as the relaxation of Russia's energy development and utilization regulations, the Far East and Siberia regions have become the hot destinations for Chinese direct investment. These places not only have very rich energy resources, such as oil, but also are rich in gold mining and many other kinds of precious metal mining. Moreover, these regions are close to China geographically, and are relatively convenient for transportation.

3. Problems in China's Direct Investment in Russia

Although China's direct investment has experienced a rapid development during the past years, there are some problems that need to be addressed.

3.1. Chinese Investment Concentrate on Energy Resources

With the rapid development of economy, China's demand for resource products is increasing day by day, while Russia is rich in natural resources and is a major country in the world. Therefore, energy and resources account for a large proportion of China's investment in Russia, which leads to the spread of "China's energy aggression" and other remarks in Russia society. This "China energy aggression" concept is particularly serious in Russia's Far East region, which has a negative impact on the development of both Chinese investment and Russia economy.

In addition, some Chinese enterprises lack investment experience, pay no attention to understand the Russian national culture, legal system and customs, and fail to timely and efficient communication, which may create further misunderstanding between Russian people and Chinese enterprises and cause certain obstacles to investment. These aspects that the two sides failed to reach trust may increase the transaction cost of China's investment in Russia, and also incur unnecessary risks, making a lot of originally promising investment not viable.

3.2. Unstable of Russia's Policies and Regulations

Russia is a country that at its economic transition period, which means laws and regulations are not that perfect and executive of regulations and laws are sometimes not well performed. In terms of investment environment, the poor legal environment has always been a serious problem in Russia, especially in the eastern region. In recent years, although the laws of Russia have been constantly improved, they are still not perfect in general, and there are some non-transparent and non-standard situations in the law enforcement, especially the frequent changes of laws and regulations, which often make Russian enterprises and foreign investors at a loss.

In the judicial field, corruption often occurs due to the existence of various interest groups, which results in some administrative and law enforcement personnel asking for bribes, accepting bribes and consulting for perverting the law, which makes foreign enterprises stop investing in Russia.

3.3. Lack of Labour in Russia

Table 4: Population of Labour in Russia from 2011-2015.

Year	2011	2012	2013	2014	2015
Population of labour (million)	77.0	76.9	76.6	76.3	76.2
Share of total population (%)	53.8	53.7	53.4	53.1	52.8

Data resource: National Bureau of Statistics of China

Table 4 describes the population of labour changes from 2011 to 2015. It is obvious that from 2011 the number of people of working age has been decreasing sharply, the percentage of labour in total population also shows a great drop. The huge labour gap will pose some obstacles for Russia to attract Chinese direct investment.

3.4. Chinese Enterprises Lack an Understanding of the Russian Market

Compared with the Chinese market, the Russian market environment is more complex. Chinese enterprises often do not acquaint with the Russian market conditions, do not understand the Russian culture, and their knowledge about Russia's investment environment, consumer habits, consumer psychology, policies and regulations is limited, which makes the initial stage of investment in Russia is difficult. In addition, the Russian product inspection standards are stricter than the Chinese local inspection standard, which requires our enterprises to improve product quality.

4. Policy and Suggestions

Under “One Belt One Road” initiative, it is of great practical significance to strengthen the cooperation between China and Russia, and promote the economic development of the two countries in view of the current situation and problems of China's direct investment in Russia.

4.1. Explore New Models of China-Russia Cooperation

Although the cooperation between China and Russia has a long history, China is still not familiar with the Russian market and has encountered many problems in the process of its direct investment in Russia. Therefore, in the process of cooperation, Chinese enterprises should give full consideration to the specific conditions in Russia and explore a new type of China-Russia cooperation model in combination with the specific conditions of the local market, so as to develop a cooperation model more in line with the development of the two countries.

At the same time, in order to improve the business reputation and product quality of Chinese enterprises, China should actively encourage those Chinese enterprises with sufficient strength to invest in Russia, ensure the smooth completion of cooperation projects, and upgrade the level of Chinese investment in Russia.

4.2. Prevent Risks in Investment Cooperation

In the process of investment cooperation, we should pay attention to the analysis and evaluation of investment risks, take risk prevention measures and protect the interests of both Chinese and Russian enterprises. First of all, relevant laws and regulations should be formulated to clearly determine the liability for possible risks. Both China and Russia must comply with the requirements of laws and regulations, and at the same time, ensure the enforceability of laws and regulations. Secondly, in the process of bilateral cooperation, the risks before and after project investment should be evaluated and prevented in detail to minimize the risks. Finally, China and Russia can also establish relevant third-party guarantee institutions, such as insurance, guarantee institutions and risk management institutions, to minimize risks and losses.

4.3. Carry out In-depth Cooperation in Various Fields

Considering the advantages of natural resources in Russia and differences in industrial structure of China and Russia, Chinese enterprises should be encouraged to enter into various fields of industry, including agriculture, forestry, infrastructure and constructions, finance and insurance, tourism, high-tech industry, as well as mining

4.4. Promote Cultural Exchanges and Mutual Understanding

When Chinese investors come to Russia, they must do as the Romans do, be a high-quality spokesperson of the Chinese image, and win the recognition of the Russian people. Chinese government, together with Chinese enterprises, can carry out some expo negotiation activities, called on Russian citizens to actively participate in, let them fully understand China, understand China's outstanding enterprises and investment projects, to inform the Russian people that Chinese investments are on both sides of the favourable.

Both China and Russia should strengthen economic and cultural exchanges, to undertake such as cultural festival, friendly city meeting, film week, joint art performances, and all kinds of forums, to

ensure a high degree of cultural compatibility between the two sides and the efficient and long-term development of investment cooperation between China and Russia.

5. Conclusions

There are both opportunities and risks in China-Russia investment cooperation, but on the whole, it still has great potential and leaves much room for further development and cooperation. In the future, China's investment in Russia should carry out risk assessment and field visits in advance, which is of great significance for protecting the vital rights and interests of Chinese investors. Both governments should strength their cooperation in various fields and give top priority to the establishment and improvement of laws and regulations related to investment attraction. A harmonious atmosphere that welcomes investment should be fostered. Chinese investors are encouraged to fully integrate into the local conditions and customs and local policies of Russia, constantly optimize their own management system, and future strengthen the relationship and links between China and Russia.

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