

Sergey VASILIEV

**Regional energy cooperation in Northeast Asia  
and its impact on world energy security**

Dear Professor Sang-Yon Lee,

Ladies and Gentlemen,

I would like to express my gratitude to Korea Energy Economic Institute and International Energy Agency for providing me opportunity to take part in this very important Conference and deliver a report on the theme: "Regional energy cooperation in Northeast Asia and its impact on world energy security".

For me it is a great honor and a big challenge. From 1997 till 2002 I was engaged in Moscow with the problems of Russian participation in APEC, including two years in capacity of a Senior Official, and for the last two years I am working in Russian Embassy in Tokyo in charge of bilateral Russian-Japanese economic relations. And my activities in these two directions have brought me to a conclusion of necessity of more deep and profound study of the perspectives and potential of the participation of Russia in economic cooperation on the intermediate level - on the Northeast Asia's level.

What is very important for me - I began to feel it in connection with the upgrading process and positive qualitative and quantitative changes in Russian-Japanese economic and trade relations. This developments can be seen first of all in the field of energy, but is not limited to it, and they are going into other related industries and spheres.

At the same time, given the big economic and political powers located in Northeast Asia, and their role in the world, and growing importance of energy issues in general, it seems to me, that we should consider energy cooperation in Northeast Asia in context of the overall situation in the region as well as in context of the global energy situation.

Frankly speaking, when I was preparing this report, thousands of figures went through my head, leaving only a severe headache and today I intended to speak without using them, but could not stand the temptation and will give you some data demonstrating the role and importance of Northeast Asia in world economy and energy.

Just for illustration. China, Russia and Japan are, after the US, the leading consumers of primary energy in the world. Russia and China are among the 6 biggest producers of oil in the world (in 2003 Russia became number 1), and Japan and Republic of Korea are on the second and 3<sup>rd</sup> places in the volume of its import, China is on the 8<sup>th</sup> place, and China's import of oil has grown last year by 19%. Russia is on the first place in production and export of natural gas, Japan and Republic of Korea - 3<sup>rd</sup> and 8<sup>th</sup> in import. China has the biggest coal producing country and second exporting, Russia - 6<sup>th</sup> and 5<sup>th</sup>. Japan, Republic of Korea and Chinese Taipei take all three medals in competition for the coal import.

In production of nuclear electricity Japan is on the 3<sup>rd</sup>, Russia - 5<sup>th</sup>, Republic of Korea - 6<sup>th</sup> place. In production of Hydro electricity 2<sup>nd</sup> place belongs to China, 5<sup>th</sup> - to Russia, 7<sup>th</sup> - to Japan. In production of electricity in general China, Japan and Russia are placed directly after the world leader - the USA. (IEA, for 2001). At the same time, statistical data also show that Japan has the highest prices in the world on electricity and natural gas - 1,5-2 times higher than other countries.

When we are speaking about potential of economy, I prefer using parity of purchasing power indexes - first of all because they are more favorable for Russia. So on PPP basis China is Number 2 in the world, Japan - 3, Russia - 10, Republic of Korea - 14. It is well known that the level of economic development of Chinese Taipei is rather high, but to my regret, Mongolia and especially DPR of Korea have not yet caught up.

What is especially important, main economies of the region, first of all China, Republic of Korea and Russia have recently rather high rates of growth, and

Japan, Republic of Korea and Chinese Taipei have already high level of economic development and income per capita in comparison with world level. Their success is based first of all on development and wide introduction of modern technologies and highly effective economic policy, including energy. For example, Japan leads the major industrialized nations in comparison of energy consumption by GDP, excelling the US almost by 3 times.

So, we have a rather rosy picture in the region of Northeast Asia... Not in every economy, at in every industry, not always, may be not forever. During the last years and now countries of Northeast Asia have to deal with new changers and challenges under the terms of globalization of economic and political life, at the same time many old problems remaining on board, sometimes in "secret" places, hiding for some time from us. Nevertheless one of most vulnerable and important spheres is, to my understanding, energy situation and closely connected to it, ecology.

Challenges have here a very complex and complicated character, taking into consideration already high and growing dependency on external, not regional sources of energy and fuel (with the only exception of Russia). At the same time, very far from ideal is so called "energy mix" almost in every economy of the region. For example, China has already a very challenging urban air pollution problem. It relies heavily on coal as an energy source, and its economy is now the world's largest emitter of sulphur (20 million tons in 2000).

In short term perspective there is a well-known danger of terrorist acts on main sea lines for oil and gas transportation, especially on the region of Southeast Asia, what can endanger the smooth and timely supply of fuel to the Northeast Asian countries and cause severe fluctuation of prices. Emergency stocks are not in all countries of the region, and creation and supporting them is not free of charge.

Even more difficult, to my understanding, is the task of guarantying long-term stable supplies of energy for world economy, first of all Northeast Asia, taking into consideration growing demand of this market, especially in China, and the fact that current consumption is here already at a very high level, including Japan and Republic of Korea.

Studying different prognosis and scenarios of the development of energy situation in the world, including prepared by very respected IEA, I have run across the fact that all of them are based on a very optimistic and ideal preposition that supply every time in future will meet demand. And what shall me do, of not?

By the way, any quantitative predictions are really a very risky business. For Example, only in August 2003 has Russian Government approved "The Strategy of Russian Energy till 2020", but it does not already comply with the reality on some very basic parameters. In case of Russia, this time the real situation has turned to be much better than the predictions.

One of the most critical issues, influencing economic and energy situation - the level of prices on energy resources. It seems to me, that conservative estimations are also rather far from reality. At least the prices for leading energy sources, including oil and coal, are today much higher than it was predicted only half a year ago by rather reliable research centers. May be, it is not yet the upper limit. We should not forget that fossil fuels are limited resources by their nature, and it is quite possible that the deficit of them will only grow in future.

To mitigate and eliminate pending problems of secure energy resources supply on the global scale and, especially, in Northeast Asia, where the biggest consumers of energy are concentrated, there is an optimal, best way - development of international, including regional cooperation.

Obviously, the countries of the region have already recognized main problems they have to deal with, but up to now they prefer to solve them by

themselves, on individual basis, or in the best cases - relying on bilateral cooperation.

Some examples of the projects, which are implemented on a multilateral commercial basis, like PSA Sakhalin 1,2 have local character, do not solve strategic problems. Of course, we should not underestimate them - their participants, and the Government of Russia, and local authorities are accumulating very serious experience of cooperation and solution of difficult current problems on a mutually beneficial bases. At the same time Asia Pacific countries get an additional and rather perspective source of oil and gas supply. Nevertheless it is only the first step.

Recently we have in Northeast Asia a rather active discussion related to oil and gas pipelines based on utilization of energy resources of Russia. Mainly, nevertheless, these discussions concentrate on the level of academicians and experts, and sometimes they are conducted on the level of general ideas and concepts, without calculating and taking into consideration real economic technical and natural aspects. At the same time, periodically we have problems, related to financing feasibility study (FS) of concrete projects. We have such situation, for example with FS of construction of electric power station in the southern part of Sakhalin island for delivering electricity to Japan. Not so much real progress have we seen yet in such a projects as modernization of electric power stations in Far East region and other part of Russia aimed at reducing the production of CO<sub>2</sub> and other greenhouse gases.

I have given only several examples, related mainly to Russia. It is clear, that all the economies of Northeast Asia have their own serious problems in spheres, related to energy. In case of China pollution of the environment, lack of electric energy; anxiety in Japan, Republic of Korea, Chinese Taipei concerning stable supply for a long perspective, high inner prices for energy, political risks; DPR of Korea - severe lack on energy even nowadays; Russia and Mongolia - wearing-out

of energy equipment, low efficiency, lack of financial and technical capabilities for modernization of energy infrastructure and development of energy resources.

To my understanding all these factors show the necessity and are objectively and naturally working in favor of establishing long-term strategic cooperation in the field of energy in the Northeast Asian Region, they are pushing the countries in this direction. It seems to me that it is much better not to wait till the problems will get a character of urgency, but to begin to establish structures and mechanisms for solving these problems beforehand just now.

We have already here a very big and rich pool of ideas, thanks to activities of IEA, KEEI, EEI of Japan, ERINA and many others. So it is necessary to formalize and separate them, prepare concrete structured proposals - we need very clear products but not something in a form of an "intellectual cloud".

As a next step may be it would be useful and of practical importance to create a joint detailed inventory of pending, perspective big-scale multilateral projects in every possible field related to energy and provide it to concerned governments. This inventory could be supported by concrete information on energy situation and its perspectives in relevant countries including availability of financial resources.

It will be also necessary to provide governments with a distinct agenda, make some proposals on the format, level and composition of participants. In any case, to my opinion, "the fruit is already ripe" - I mean the idea of energy cooperation in Northeast Asia and should go to the next level.

Naturally, somebody has to take the initiative, there could be several initiating parties as well. But nevertheless here I am relying first of all on the representatives of the Republic of Korea. May be, because it is in the epicentre of these pending international problems.

Of course, we can use some existing institutions, including APEC and its Energy Working Group and Meetings of energy ministers to begin the process.

Maybe we could start from the very beginning and create a new Forum. The first strategic step could be establishing Northeast Asia Energy Community, and in more distant perspective - Northeast Asia Economic Community. Such development would correspond not only to the interests of the region, but to the needs of the world economy.

Speaking about energy cooperation in the region I mean not only provision of necessary fuels, but facilitation of the international flows of modern technologies, capital, know-how, improving the quality of the environment. It is important that we can use the experience of establishing institutions and legal foundations in Europe, and other parts of the world the cooperation in Northeast Asia can be based on a new technological base, using new materials and information technologies, higher standards, including related to the protection of Environment.

Deepening of cooperation in energy will provide a stimulus for higher international competitiveness of the regional economies, improvement of the global energy and ecological situation, promotion of transparency, predictability on the regional and world energy markets.

I would like to give just one example of possible effects of cooperation. According to calculations of IEE of Japan, import of oil by three main oil consuming countries of Northeast Asia (China, Japan, Republic of Korea) will reach by 2020 770 mln.t per year, level of consumption - 980 mln.t. Dependency on import will be about 80%. Dependency on Middle East producers in case of Japan - 89%, Republic of Korea - 79%, China - 51%. As a whole it will be as high as 65% (now - 58%). The only real way - import of oil from Siberia, what can help to downscale on Middle East to 54%, and at the same time, to my understanding limit the pressure of so called "Asian premium".

In any case, the economics of Northeast Asia should develop their cooperation in energy on the principles of nondiscrimination and openness, market

mechanism and gradual liberalization of regulations. It is very important to develop direct exchanges of basic information between regional governments, opening the way to policy dialog, and promotion of concrete cooperation projects. Of course, private sector should play the leading role, but the importance of governments and state also should be not underestimated, especially in such strategic, big-scale and long-term cooperation field as energy, where due consideration should also be given, do we like it or not, not only to macroeconomic factor, but to political as well.

By joining the efforts of the countries of the region we can get the effect of "synergy" and mutually use strong sides of each other. May be in several years time the governments of our countries will not rely on separate "Energy Strategies" but will act on a basis of a joint, united document, based on interests, ideas, knowledge, approaches.

Nevertheless, now it is too early to speak about more or less developed Northeast Asia energy market or broad regional cooperation, a great impact of them on world energy security. We do have still to many "ifs" and "whens". At the same time it is clear, that future development of Northeast Asia Energy Cooperation will have a very big and positive influence on global energy situation. The scope will be of great scale, because of the size of energy sector of the region. According to Investment Outlook 2003 of IEA, cumulative energy investment of this countries 2001-2030, will account for about 25% of the global volume (more than \$ 4 trillion) and will increase most rapidly. Positive effect can be foreseen thanks to stabilizing balance between demand and supply, lower transportation cost, using fuel of higher quality, developing competition and technological exchanges, fully utilizing financial potential of the region. The global energy situation will become more stable and predictable, what shall also provide better circumstances for development of the economy of Northeast Asia. Russia is also ready to support

this process by awakening its dreaming energy treasures and by participation in other forms of energy cooperation.

Making this report in my private capacity, nevertheless I would like to conclude quoting President Vladimir Putin at the APEC summit in Bangkok in October 2003: "Russia is also prepared to make its contribution in the Asian and Pacific Region. This will allow consumers of energy resources, which are widely represented in the APEC, also fearing in mind the economic growth of these countries, to diverse deliveries of energy resources, and, which is especially important, to ensure their security".

I fully agree with this idea of my President and think that these words should first of all be related to Northeast Asia which, I hope, in the framework of APEC and other international fora well as on the global level, will more and more often act as a united region, including, of course Russia. In such capacity Northeast Asia will be in a better position to make its own individual positive input into the global development, including world energy security.

March 12, 2004