

Will the boom in Japan-Russia economic relations continue?

By Shinichiro Tabata

In the first decade of this century, especially since the mid-2000s, trade between Japan and Russia has increased at an unprecedented rate. While in 2006 the volume of that trade exceeded \$10 billion for the first time in the history of the two countries' bilateral trade, in the following year, it reached \$20 billion, and in 2011, it surpassed \$30 billion. It is safe to say that at present Japan-Russia economic relations have reached their most developed stage ever, despite the limited progress in political relations, marred by the unresolved disagreement over the so-called northern territorial issue.

There are two factors supporting the immense increase in Japan-Russia bilateral trade in the 2000s: automobile exports from Japan to Russia and oil and gas imports to Japan from Russia. During the period from 2002 to 2008, Japanese car exports to Russia skyrocketed. This was due to the oil-fueled economic boom in Russia, characterized by increasing household expenditure, almost half of which is traced to imports. Russia's imports in passenger cars increased from \$1.3 billion in 2002 to \$30.3 billion in 2008, of which those from Japan grew from \$0.3 billion to \$11.5 billion over the same period. Japan's share of Russia's passenger car imports increased from 20.3 percent in 2002 to 37.9 percent in 2008. While the automobile industry is the most important and competitive sector in Japanese manufacturing, the significance of Russia as a market for Japanese cars is growing. As Russia became the second-largest market for new passenger cars in Europe, Russia ranked second (its share was 9.0 percent) behind only the United States as a passenger car importer from Japan in 2012.

The rapid increase in Japan's imports from Russia is mainly due to imports of oil and gas. While the share of oil, petroleum products, and liquefied natural gas (LNG) in Japan's imports from Russia was only 5.2 percent in 2004, it reached 68.7 percent in 2012. It should be noted that Russian oil and gas development has shifted further toward the east. The Russian government embarked on development of Sakhalin's oil and gas, construction of the East Siberia-Pacific Ocean (ESPO) pipeline, and exploitation of oil fields in East Siberia. As a result, the share of East Siberia and the Far East in Russian oil production grew from 1.2 percent (3.9 million tons) in 2000 to 9.6 percent (49.4 million tons) in 2012. With respect to oil exports, the sum of those to Japan, China, and South Korea rose from 1.5 million tons in 2000 to 39.0 million tons in 2012. Their share in Russia's oil exports rose from 1.1 percent to 16.2 percent over the same period.

The share of Russia in Japan's oil imports grew from 0.7 percent in 2005 to 7.2 percent in 2010. This share was 4.6 percent in 2012, of which 63.4 percent was imported from Koz'mino, an export terminal on the ESPO pipeline near Vladivostok, and 34.8 percent was transported from Sakhalin. With respect to LNG imports from Russia, they only

started in 2009 after the opening of Russia's first LNG plant in Prigorodnoye, located at the southern end of Sakhalin Island. In 2012, Japan imported 8.3 million tons of LNG from this plant and the share of Russia in Japan's imports of LNG amounted to 9.5 percent. Russia already ranked fourth in Japan's LNG imports after Australia, Qatar, and Malaysia.

Given the March 2011 earthquake, tsunami, and closure of the Fukushima nuclear power plant, Japanese demand for Russia's oil and gas is forecasted to increase, since as a consequence of the disaster Japan will inevitably reduce its dependence on atomic energy. In 2010, the share of atomic power in Japan's production of electricity was 30.8 percent, followed by LNG (27.2 percent), coal (23.8 percent), hydropower (8.7 percent), and oil (8.3 percent). In addition, considering the increasing risk entailed in reliance on oil and gas imports from the Middle East (its share in Japan's oil imports was 83.4 percent in 2012), imports from the adjacent Russian Far East will increase in importance in light of Japan's energy security.

While Japan's imports from Russia are certain to increase further at least in the near future, the prospect of Japan's exports, i.e., Japanese car exports, to Russia depends on several factors. Among others, it depends on the continued expansion of household consumption in Russia. In 2013, for example, although relatively high income growth continues, high interest rates of consumer loans, caused by a high inflation rate (about 6 percent), may restrict the growth of passenger car imports. Another factor is that Toyota, Nissan, and other Japanese companies are increasing their production in Russia, as is the case for the automobile companies of other countries. This, together with imports of Japanese cars produced in third countries, may decrease their imports directly from Japan. Nonetheless, the sum of bilateral trade, or we should say overall economic relations, between Japan and Russia, including the activities of Japanese companies in Russia, will undoubtedly expand further in the decade to come.

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