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THE INVESTMENT OF THE RUSSIAN FEDERATION INTO THE NEW SILK  
ROAD

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## VENÄJÄN FEDERAATION INVESTOINTI UUTEEN SILKKITIEHEN

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Tämän opinnäytetyön tarkoitus oli antaa tietoa silkkitiestä ja keskittyä Venäjän osuuteen ja investointiin uudessa silkkitiessä. Tarkoituksena oli kerätä tietoa eri lähteistä kuten artikkeleista ja kirjoitelmista miten Venäjä on investoinut uuteen silkkitiehen ja mitä mahdollisuuksia ja haasteita uuden silkkitien yhteydessä on.

Tämä opinnäytetyö oli rajattu vain Venäjän osuuteen ja miten Venäjä kehittyi ja kehittää omia osuuksiaan silkkitien kehityksen edetessä. Tietoa kerättiin enimmäkseen Venäjän investoinneista, poliittisista suhteista ja Venäjän kiinnostuksista, englannin ja venäjän kielisistä lähteistä. Opinnäytetyö antaa laajemman kuvan Venäjän käyttäytymisestä poliittisessa ja rahallisessa mielessä. Opinnäytetyö antaa käsityksen silkkitien muodostumiseen Venäjän puolelta.

Kerättyjä artikkeleita ja muita lähteitä käytettiin teoriaosuudessa kirjoitettuun tietoon. Samalla nämä tiedot myös auttavat haastattelu osuudessa kysymysten muodostamiseen joilla saadaan parempi kuva ja parempi pohja tutkimustyölle joka antaa tarkemmin tietoa aiheesta. Haastattelut kohdistettiin kolmelle henkilölle ja he olivat Aleksanteri Instituutista, Cursor Oy:stä ja Kymenlaakson liitosta jotta investointiin liittyvät kysymykset saisivat mahdollisimman laajan vastauksen.

Opinnäytteen tutkimus tavoite saavutettiin etsimällä mahdollisimman uusia ja ajankohtaisia artikkeleita. Samoin saavutettiin ymmärrys siitä mitä Venäjä on valmis tekemään investoinneilla uuteen silkkitiehen. Siihen vaaditaan huomattavasti investointeja Venäjän sisällä kuin myös yhteisillä projekteilla Venäjän rajojen ulkopuolella, suurimmaksi osaksi Kiinan kanssa ja myös naapurivaltioiden kanssa. Tutkimus paljasti myös mahdollisia ongelmia joita infrastruktuuriin liittyvät projektit ja investoinnit vaativat, mutta myös todistaa paljon mahdollisuuksia joita uuden silkkitien rakentaminen ja investoiminen tuo.

Opinnäytetyön perusteella esitellään mahdollisimman laajasti Venäjän osuus uudessa silkkitiessä ja mitä kaikkea siihen on vaadittu ja tulevaisuudessa vaaditaan investoinneilla. Samoin naapurimaiden ja muiden maiden poliittisia asioita tutkitaan jotta saadaan mahdollisimman selvä kuva.

## THE INVESTMENT OF THE RUSSIAN FEDERATION INTO THE NEW SILK ROAD

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The purpose of this thesis was to provide information about the Silk Road and focus on the Russian contribution and investments in the new Silk Road. The purpose was to gather information from different sources such as articles and texts on how Russian Federation has invested in the new Silk Road, and what opportunities and challenges is there.

The study was limited only to Russian portion and how Russia evolves and develops its own shares in the development of the new Silk Road and its progress. The information was focused mostly on Russian investment, political relations and Russia's interests from English and Russian sources. The thesis gives a broader picture of Russia's political and monetary behaviour. The thesis gives an insight into the formation of the Silk Road from Russia's point of view.

The collected articles and other sources were used in the theoretical part of the collected data. At the same time the data also helps to form the interview questions, that will be part of the research methodology part of the thesis in order to get a better picture and better base for research work that will give further information on the subject. The interviews are focused to the Aleksanteri Institute, Cursor Oy and The Regional Council of Kymenlaakso in order to get the broadest possible response and understanding in the issues.

The thesis research objective was achieved by finding new and topical articles as possible. Similarly, an understanding was achieved on what investments Russia is ready to make in the new Silk Road. It requires quite a lot of investments within Russia as well as joint projects outside Russia's borders, mainly with China and also with neighbouring countries. The study also revealed potential problems that are related to infrastructure projects and what investments demand, but also prove a lot of opportunities that the construction of the new Silk Road and investments will bring.

On the basis of the thesis it presents as broad as possibly Russia's share in the new Silk Road and all that it has required and will continue to require with investments. Similarly, neighbouring countries' and other countries' political issues are examined in order to obtain the clearest possible picture.

## CONTENTS

1	INTRODUCTION.....	5
1.1	Purpose of the thesis.....	5
1.2	Research questions and problem.....	6
1.3	Conceptual framework.....	7
1.4	The structure of the thesis.....	8
2	LITERATURE REVIEW.....	10
2.1	The new Silk Road.....	10
2.2	Russia's investment to the new Silk Road.....	15
2.2.1	EAEU and China.....	18
2.3	Problem and opportunity in Russia's investment to the new Silk Road.....	19
2.4	Russia's benefits and challenges when investing to the new Silk Road.....	21
2.5	Pay-Back.....	24
2.6	Political support.....	25
2.7	Finance.....	27
2.8	Russia's interests.....	30
3	RESEARCH METHODOLOGY.....	31
3.1	Validity and reliability.....	31
3.2	Research methods.....	32
3.3	Collection of data.....	32
3.4	Analysis of data.....	33
3.5	Scope and delimitation.....	33
4	EMPIRICAL RESULTS.....	34
4.1	Conduction of the interviews.....	34
4.2	Interview results.....	35
5	SUMMARY AND CONCLUSIONS.....	38
6	FINAL WORDS.....	39
	APPENDICES	

## 1 INTRODUCTION

The focus and purpose of the thesis is the research that is gathered from various sources from the internet. The topic is chosen from the authors own interest towards the topic. There is no case company but there are interviews that will give the empirical data in order to get more detailed picture of Russian Federation's investments and political presence. The thesis is thus only a research of the topic. There is no personal opinions in the research. The topic focuses to the investments that are made to the new Silk Road and also highlighting the Russian Federation's contribution with investments, politics and joint projects within the new Silk Road.

The beginning part of the thesis is the introduction, purpose and conceptual framework. All of that will be discussed first before moving on to the theory part of the thesis. The literature review is the topic of the thesis. It describes the investments, infrastructure, politics and the development of the new Silk Road and also focuses to Russian Federation.

The thesis results from the research and empirical part are analyzed in the end. The last part of the thesis gives a summary and conclusion of the results that are researched in the thesis and gives a potential continuation of the subject. Also the success of the whole research will be discussed in the end.

### 1.1 Purpose of the thesis

The research is done to give an understanding of the investment parts and understanding what the new Silk Road project is. The information that is gathered from various sources from the internet gives a current picture of the project and how Russian Federation is participating to it. The investments, opportunities and challenges and political affairs of Russian Federation is the focus for the research. The research also introduces the other projects that take place in the development of the new Silk Road. The research information is not an opinion but a combined knowledge of this moment. The aim is to build an understandable picture of the new Silk Road's investment as a whole.

The research will give an information of the Russian Federation's contribution to the new Silk Road with its participation, investments and politics. Russia's interests are also described towards the new Silk Road and towards joint projects. The basic information of the new Silk Road is also researched highlighting the investments.

## 1.2 Research questions and problem

The research problem is about the financial area and also what it consists of when investing to the new Silk Road. The political support is taken into consideration in order to get a more full view of the situations that take place in the new Silk Road. The thesis and the subject is mostly viewed from Russia's point of view and on Russia's financials and on investments parts.

The research questions will give as broad as possible view of what it takes from Russian Federation to invest to the new Silk Road and what is needed in order to be part of the new Silk Road. Five questions were done in order to get an overview.

RQ1: How much and how is Russian Federation investing to the new Silk Road?

RQ2: Why is Russian Federation investing to the new Silk Road?

RQ3: What challenges can Russian Federation face when investing to the new Silk Road?

RQ4: What are Russian Federation's infrastructural opportunities when investing to the development of the new Silk Road?

RQ5: How does politics affect to the initiative?

The first question aims to give an answer and explanation to the financial matters that Russian Federation needs to do to be part of the new Silk Road. The second questions answers to the matter of why is Russia investing and wanting to be part of the initiative. The aim of the third question is to give as broad answer and understanding as possible of the challenges that lie in the new Silk Road when investing to it. The fourth question is about the infrastructural opportunities that Russian Federation has when it invests to the initiative's development. The fifth question aims on answering about the political matters, situations and also political

support that Russian Federation faces in the initiative with other countries. Also how it affects when being part of the new Silk Road, which is developing.

The research questions will be answered in the theory part of the thesis. It gives as current answer to the present situations in the new Silk Road. The empirical data will give a better and more detailed information about the Russian Federation's investments to the new Silk Road.

### 1.3 Conceptual framework

The conceptual framework of the thesis is presented in figure 1. The purpose of figure 1 is to show the thesis and its topics and what has been researched in the theory part of the thesis. Also the topics on the conceptual framework will be also used in the empirical part of the thesis. This is in order to get as fulfilling finish to the thesis as possible. The conceptual framework consists of the Silk Road and Russia and what opportunities and challenges is there for Russian Federation with investments. Also the investment in infrastructure is an important part of the conceptual framework, as it is for the thesis. Political support and all that happens with the political situations and matters with other countries and Russia will be present in the thesis. All the topics in the conceptual framework will form an overview of the thesis as clear and as current as possible.

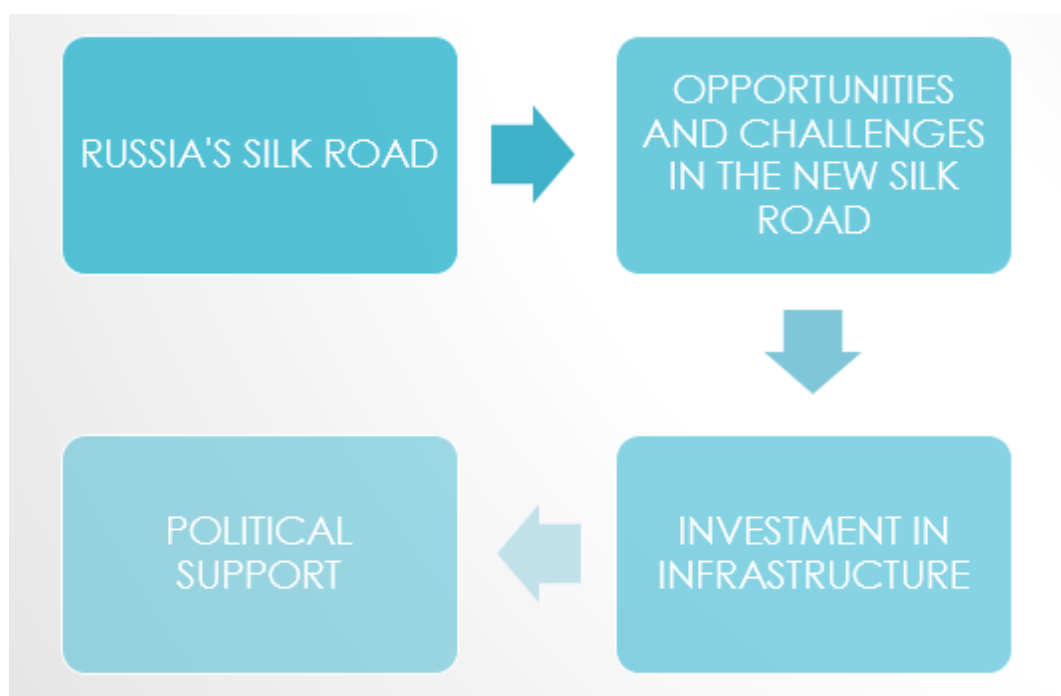


Figure 1. Conceptual Framework (Made by the author 2017)

#### 1.4 The structure of the thesis

The thesis has two main parts. There is a theoretical part that explains the Russian Federation's investments, opportunities and challenges and politics in the formation and development of the new Silk Road and what is needed to be part of it. The research questions will also be answered in the theoretical part to give an understanding of the topic of the thesis. The empirical part will consist of the interviews to Aleksanteri Institute, Cursor Oy and The Regional Council of Kymenlaakso. The interviews will give a more detailed information about the investments and political matters and affairs that Russian Federation has in the new Silk Road.

The thesis is in six parts. The first chapter introduces the thesis and the topic in order to give a full overview of the topic's literature review's theoretical part and also the empirical part that consists of the interviews from Aleksanteri Institute, Cursor Oy and The Regional Council of Kymenlaakso. The topic is as clearly as possibly introduced in the matter of the new Silk Road and Russia and also the opportunities



and challenges that Russia faces in the development of the new Silk Road and also the investments in infrastructure and political support and political affairs.

The second chapter consists of the theory from various sources. It explains in detail the current situation that Russia has with the new Silk Road's development. Also the new Silk Road project with China and other countries in Central Asia and Europe will be described as broadly as possible. Russian Federation's investments financially and also infrastructurally are described in more detail in the second chapter of the thesis. The focus is also in the Russian Federation's challenges and opportunities and in political affairs, which are part of the new Silk Road. The third chapter is research methodology. It explains the collection of data, analysis of data and scope and limitations of the thesis. The fourth chapter is the empirical results which are the results from the interviews. The answers will give a more detailed information and understanding on Russia's investments and political situations and affairs. The fifth chapter concludes and summarises the thesis, when finished, it gives an abstract of the thesis towards the end. The sixth and last chapter is the final words and opinions of the author to conclude the whole thesis.

## 2 LITERATURE REVIEW

### 2.1 The new Silk Road

The new Silk Road initiative started in the year of 2013 in September. Before that, the Foundation Silk Road was formed in China in February. \$40 billion is meant to finance the infrastructure projects. They are meant in Eurasia and Asia, Pacific region. The willingness to finance and joint projects with Russia was introduced in Beijing. A year and a half later, when the initiative was officially stated in September 2013, China's president Xi Jinping spoke in Kazakhstan's capital Astana at Nazarbayev University about the concept of building Economic Belt Silk Road. It is a huge and vast economic cooperation zone. It will stretch from China to Europe and it covers approximately 3 billion inhabitants. Initially, China's leader's initiative caused contradictory interpretations from politicians and experts. It has since developed a clearer outlines and contours.

One Belt One Road's objective is to create better relationships between Asia, Europe and also Africa. The trade routes are going to expand China's ties with European Union (EU). In order to have a working results, it is important to fix the development of infrastructure. Also political coordination and financial intergration are going to help with trade, when the infrastructure is fixed. (Website of NG 2015)

China's State Administration of foreign exchange earning, China Investment Corporation, Export-Import Bank of China and China Development Bank are the main sources of finance and the beginning capital was \$10 billion. (Website of Financial Times 2016)

The high-speed highway, the idea of it, was already developed in the mid-2000's. The idea was developed in order to link the European countries and China. The fast increase in the trade volume, between European Union and China, is something that it was developed for in the first place. In 2014, the turnover was €467 billion and

according to the European Conference of Ministers of Transport, the trade between European countries and Asian countries has grown six-fold in 20 years.

The idea of economic intergration is a component thread of the Chinese concept. It does not mean the creation of gigantic structure with stiff and rigid rules and obligation from the participants. It has free trade zones and intensive economic convergence of almost all the conceivable areas. These are the transport construction, trade, investment, trade liberalization, the calculations in national currencies, the laying of pipelines, development of telecommunications and even the use of “soft power”. Soft power is an attraction to China for thousand of students. The process naturally includes all the existing international structures or bodies. They are the Shanghai Cooperation Organization (SCO), the Eurasian Economic Union (EAEU), the European Union (EU). Also the future structures will be a part of it, if there will be any.

The countries that are part of the Economic Belt are the possible members of the Eurasian Economic Union (EAEU). Russia and China have many partnerships in different bodies.

Geographical outlines of the Economic Belt are: One of its branches extends from China to Europe via Kazakhstan and Russia. The other extends through Central Asia and the Middle East. The “Economic corridor”, which is considered, is the third and also planned part from China to India, Bangladesh and Myanmar, as well as China-Pakistan corridor.

Along with the Economic Belt project, Beijing has offered an idea. The idea is Maritime Silk Road of 21<sup>st</sup> century. The meaning of the Belt and the Road is to create favourable conditions. It means to raise a new level of economic activity of China in the Eastern Hemisphere. By doing so, it would strengthen its role in world politics. The necessity and need for such a breakthrough comes from the current extended generation of Chinese leadership. The strategic goal is the rejuvenation of the Chinese nation and of the ambitious goals of building moderately prosperous society by 2021. By 2049, the goal is to build a wealthy and powerful modern socialist state. (Website of NG 2015)

The Economic Belt Silk Road and the Maritime Silk Road are included in the Silk Road initiative. Both littoral countries and continental countries are the target for the initiative. Russia is a significant power in this field.

The new Silk Road aims to cooperate between different countries. The countries are going to be the ones that are in the transit corridor. It will go from Europe to Asia. The plan is to build the ground roads and also the Maritime Silk Road. This would promote economies and exports.

The Maritime Silk Road will be built in two channels. The first is Nicaragua. It is an alternative to the Panama Canal. The second goes through Thailand's Kra Isthmus. This is an alternative to the Malacca Strait. (Website of CFTS)

Economic power in Beijing provides Economic Belt's building and construction position for informal leaders. They then perform the most important function. These are the allocation of funds, for what the Fund was created in China with capital of \$40 billion.

Leaders of China highlight that the concept is based on “win-win” principle. This principle is China's and its partners' and the principle is more or less true. The fact is that the interests of China and other countries are at the same stage in development of the world economy. At least, they largely and substantially coincide or are equal. Economic development is where the focus will be in the future. The business circles of other countries accepted, embraced and approved the Chinese concept. Central Asian countries are the most enthusiastic. The cooperation with China means to them that they would receive the access to international markets. It does not only mean economic recovery of the economy. Central Asian countries have to understand clearly that the convergence with China has downsides. The downsides are a one-sided development of the primary industries and tensions in the emergence of economic dependence from a powerful partner. The Central Asian countries do not have any alternative options of development.

The new Silk Road, the region, consists of the countries in Central Asia, West Asia, the Middle East and Europe. It is going to help the development of the region. Infrastructure and the expansion of cultural and economic ties will also be positively affected by the new Silk Road.

For Russia, it contains both chances and challenges. For Russia, it is the perspective of participation in the construction of the Silk Road. The performance of Russian transit function of Chinese goods to Europe, which is a natural chance, is already in use. Russia is able to transform its site or lot into a modern and powerful transport corridor. That would be the transcontinental highway. This can be done by modernizing the material resources and logistics. Intensive use of modernized track could give Russia a push to develop the surrounding areas. In addition to that it would give growth of direct revenues from transit.

For China, this corridor is the only land route into Europe. There has not been laid and routed an alternative route, as a whole, which would go through Central Asia and the Middle East. To turn that into a full-fledged highway, it would require multibillion investments. In addition to that there is a need to address the complex political and customs problems that are associated with crossing of many borders.

China is ready to connect the routing through Russia and to lay tracks through Russia and route it with high bandwidth and capacity. The parties have agreed already on studying the construction that is needed for the project. The construction needs a number of sections of high-speed transport corridor between Europe and Asia. Above all, the parties have agreed on cooperation in the construction of the the road from Moscow to Kazan. A memorandum on cooperation is signed in the field of high-speed highway. Chinese press has noted that Russia is one of the main participants of the Economic Belt Silk Road. According to estimates of China's experts, the cost of construction of Beijing-Moscow highway could reach \$350 billion. But the travel time will be reduced from six to two days. China's general principle of partnership in the infrastructure construction should be taken into consideration. This means that Chinese party provides capital, technology and equipment. But this is only when involved long-term in the operation of the constructed object.

A consortium that is lead by China has a contract of building a high-dpeed railway line. It will be 770km and it goes between Moscow and Kazan. The investments are \$16,7 billion (Website of Financial Times 2016). The journey from Moscow to Kazan will be 3,5 hours instead of 12 hours. The main disadvantage of the modernization of the transcontinental route, that goes through Kazakhstan, is that it

will decrease the interest of carriers in the Trans-Siberian transit channel. It is already losing points in the competition with the transcontinental route. It suffers a variety of long-standing vices, such as bottlenecks, low freight rate and inflated prices. To revive Siberia and the Far East, such developments would negatively affect the plans.

The construction of railway lines has already begun, in the province of Heilongjiang, from Harbin to the Trans-Siberian and BAM (Baikal – Amur Mainline) through Manchuria, Tongjiang and Suifenhe. Suifenhe served as the realization of the Silk Road concept with the expectation of trade, commodity flows from the various provinces of China. The fundamental status and situation does not change, as it remains the same. (Website of NG 2015)

A negative result or consequence of initiation of Russia to the Silk Road will express the fact that the new Chinese investments will decrease the interest of Central Asian countries to participate to the SCO (Shanghai Cooperation Organization). For China, the decline of attractiveness of the SCO will be offset by growth of its own economic presence in Central Asia. For Russia it will not.

There are concerns that the new Chinese investments to Kazakhstan's economy could cause a contradictory situation due to the fact that it is a member of Eurasian Economic Union (EAEU). Also Kyrgyzstan has the same situation. A maturing conflict of interests especially is that the Central Asian countries and China, as experts, are not considered strong enough.

Russia simply has no alternatives in embedding to the new Silk Road. However, it is important in the present circumstances since the country's position has deteriorated due to the Ukrainian crisis and from the confrontation with the West. Russia's conversation with China on business issues are not to be conducted from a position of weakness. Interaction with China should not be forced to answer to sanctions but the realization of the fundamental principles of Russian-Chinese strategic partnership. (Website of NG 2015)

«Шелковый ветер» позволит грузам из Китая попадать в страны ЕС в обход России



Figure 2. The Silk Road and Maritime Silk Road (Website of RBC 2015)

## 2.2 Russia's investment to the new Silk Road

In 2016, the shareholders of Sibur and the representatives of the Chinese Investment Fund (Silk Road Fund) signed the final documents on the acquisition of 10% from Sibur, a petrochemical company. Sibur's Chairman of the board of directors Leonid Michelson, CEO Dmitry Konov and president of the foundations “Silk Road” Van Yanchji attended to the signing ceremony. Silk Road foundation has already invested in the Russian oil and gas industry. In march 2016, the Fund acquires 9,9% from “Yamal LNG”. (Website of Tass 2016)

The emergence of such a large financial institution, as the Silk Road Foundations, and the shareholders in Sibur confirm the investment attractiveness of the company. It strengthens its position in the international market. They are confident that the cooperation between Russia and China will contribute to further development of economic relations.

For any country, the key is the factors of maintaining long-term economic growth, whereas the search and diversification of infrastructure are challenging. Forecasts of the Organization for Economic Cooperation Development with an average annual growth rate 3,3% of worlds gross domestic product will double by 2035. It can be expected to amount to \$145 trillion. In the measure of GDP, China has become the leader according to purchasing power parity (PPP) and has become the largest economy in the world. China's GDP will grow 2,5 times by 2030, compared with India's GDP in 2014. Third world economy GDP will triple by 2030. Russia's GDP will double over this period. It will then be among the five largest economies of the world. OECD experts estimate that the global GDP will double by 2035 and that the passenger traffic increases 2,5 times during that period. Air cargo will triple and containers will increase four times. The existing transport corridors between Asia and Europe will increase the turnover more than 50%, on average. It will require several years to design, construct and to expand the large infrastructure projects. There is a necessity to decide the use of mechanisms and to finance all stages of such a project's lifecycle. Russian Federation's economy, as well as economies of many countries in the world are going through difficult times. In an unstable and increasingly difficult geopolitical situation, the associated restrictions of the national economy should raise the inefficient economic models. (Ivanov & Bochkareva 2016)

Investment in transport infrastructure in Russian context, characterized by large multiplier (in macroeconomics), gives 3 – 4 rouble growth of value added in economy for every invested rouble.

For all types of goods, the decrease of freight costs by 10% gives additional 0,12% to GDP. It gives an additional 1% of GDP investment in infrastructure and creates 3,4 million new jobs places in India, 1,5 million places in the United States or 1,3 million places in Brazil. Brazil and Russia have similarities in the economic performance. Taking that into account, the number of work places created in Russia is probably going to be the same.

In Russian Federation, the level of investment in transport infrastructure is close to the level of investment in countries with infrastructure being approximately 3% of GDP. This is already enough for progressive development but not for a qualitative



leap. Russia's contemporary socio-political conditions are necessary to implement anticipated infrastructure development plans in comparison with other sectors of economy to remove most of the traffic restrictions on manufacturing, retail as well as in the social sphere.

For the project's successful implementation and operation, the investors hold shares. They use the put option. This mechanism is necessary to accurately assess the value of the right to withdraw from the project. This is a substitute for direct investment budget to be effective. The financial mechanism of state prefers that it buys preferred shares of SPV. This, in turn, would pay dividends to the state, as a shareholder. It is done as long as the SPV itself or private investor buys shares. This financing method places fixed dividend payment obligations for the company while giving the right to buy back part or all of the issues as they become available funds. These sort of arrangements stimulate the finance of equity companies. The state can encourage the flow of funds to companies. It would not be through equity but through loan capital. The government can do the following as a first thing, in this area, to stimulate lending. 1. The state can give an indication for any state of the banking structure to give guarantees to foreign partners. 2. The structure ensures the foreign partner of the project execution and payment of obligations. 3. Project issues credit which is usually up to 80% of the necessary investment. 4. SPV generates cash flow, returning interest to the loan. (Ivanov & Bochkareva 2016)

In the case of project financing source, it is crucial that the financial resources to repay the funding becomes free cash flow generated by all its projects. The cash flow generated only by the project financing in general are only those assets that have been acquired for its implementation. Increase in tax revenues, to the budgets of different levels, will be established with government and leading companies of neighbouring countries. It will also include local and regional authorities. This is because the project interests other sides as well. It should be noted that the mechanism of project financing is more flexible than the traditional method of implementation of investment projects. It is suitable for the implementation of huge capital-intensive projects. Those are necessary for the integration of Russia in Economic Belt Silk Road.

The mechanism used in the financing of the “Yamal LNG” project, which plans the construction of a liquefied natural gas plant which has the capacity of 16,5 million tons per year to resource. It is based in South-Tambeyskoye field that is located in north-east of the Yamal Peninsula, in Russia. This mechanism has been implemented by Novatec. They have 9,9% stake in the Silk Road fund. The cost of the project is estimated at \$27 billion. The investment that is already been made is \$10 billion. Sberbank, Gazprombank, Vnesheconombank, China Eximbank and China Development Bank are part of it.

Kazakh and Chinese lines are the first ones that were connected. In 2013, the freight that was transported was 2,2 million tons. The annual freight will increase. By 2020 it can be expected that the freight is approximately 15 million tons. The lines that are, and those that will be connected, will multiply the connections with central part of China.

#### 2.2.1 EAEU and China

EAEU countries are the ones that are the most interested in the “New Eurasian Land-Bridge”. The Land-Bridge will improve transportation for Russia, Kazakhstan and Belarus. The investments are directed to those countries. The Land-Bridge then can be used to transport goods inside EAEU.

It will connect themselves and Poland and Germany and also China to Western Europe. China has cooperation with EAEU but China has increased the application of capital in Russia. China increased the direct investment to Russia. It increased from \$125,9 million to \$1,270 million. Also the FDI, that Russia received, increased from 0,2% to 5,6%.

For EAEU, China is the most important partner in foreign trade. The exports have grown significantly since 2007 to 2012. It grew from \$26,9 billion to \$59,6 billion. Russia imports machinery and equipment, metal products, textiles, transport equipment, plastic and rubber and different goods from China.

The percentages of the imports from China to Russia are: Machinery and equipment 29.5%, Metal products 11,3%, Textiles 10,4%, Transport equipment 7,8%, Plastic and rubber 7,5% and different goods 6,6%.

With trade, China is important for EAEU. This goes also to Kazakhstan and Kyrgystan.

EAEU and its member states are the best option for the development of transport corridor that goes from China to Europe. There are problems that need to be fixed. For example Russia has too low bandwidth in its highways. EAEU should fix the problems in order to stay in the infrastructure network of Economic Belt Silk Road. (Website of Vesti Finance 2016)

### 2.3 Problem and opportunity in Russia's investment to the new Silk Road

The opportunity with investing to the Silk Road lies in many fields. These are the tourism, transportation and logistics. There are opportunities with energy, mining, chemicals and machinery. The oil and gas sector has expanded in recent years. Chinese and Russian investors have been active in that field.

There is a joint project between Russia and China. It is about the production of FAW truck plant. The joint project has begun in the spring of 2017 in the Primorye Territory in Russia. (Website of Transinfo.News 2017)

The problems may occur with the fact that there are many Western countries also present in the development and investment of the Silk Road. Especially in the Central Asian region where Russia is also present. The whole area, where the Silk Road is developing, attracts FDI (Foreign Direct Investment). This shows that the Silk Road interests investors also to increase their investments. The attraction also lies in the strong economic growth, improving productivity and in low labour costs.

One Belt One Road opens new opportunities in the transportation and logistics for both Europe and Asia. The cooperation, that is between China and Europe, is going to be in distribution of goods and logistics.

Tourism, for the region of Silk Road, is important. The Silk Road attracts international tourists to Central Asia. For the region, Russian Federation is an important source of tourists.

The problems, with investments, are also in the investment environment. This means that there are differences in the improvement of the business environment. For example Kazakhstan is in tenth place as Uzbekistan is fourth. In the attempt of creating better investment conditions, the body of law is still developing in Central Asia.

The Central Asia's oil and gas pipelines were put in when there still was Soviet Union. The oil and gas pipelines in Russia and Central Asia are vast. The problems that occur with the pipelines are for example between Tajikistan and Uzbekistan. There are political issues, as well as bilateral issues that can cause interruptions. Also what causes difficulties is the fact that the vast territory makes infrastructure difficult.

Russia's opportunity in the Silk Road is to have Russian companies included in the initiative. Russia should not have only companies outside of Russia to take part in the Silk Road. The opportunities are also in the creation of jobs in Russia by Russians. Russian Federation has the opportunity to join to the Asian economy and promote its private sector. (Website of Rethinking Russia 2016)

The Silk Road project connects East and West. It is an attraction to investors, to both strategic asset seeking and resource. The opportunities, in the region, lie in economic growth. The regional market in the Russian Federation and China are promising to the investors.

Russia has become self sufficient due to the sanctions. The depressed oil prices are the reason for the figures in Russia's economy. The natural resources in Siberia alone are substantial. Due to the vast natural commodities, Russia is an important investment partner and trade partner in the future.

The sanctions have pushed Russian people to invest more. Also entrepreneurial actions are encouraged. The sanctions have not stopped Russia, in fact the economy of Russian Federation grew faster in 2017 compared to European Union (EU). Russia's re-emergence has been a positive thing. The re-engagement of the infrastructure of Eurasia is going to develop a positive results in Central Asia. The involvement of Russia in the new Silk Road promotes European business. The new Silk Road and the fact that Russia and China are part of it would interconnect

markets. These would be the Eurasian and Asian markets. This way Russia and China are able to participate without trade arguments with West. (Website of Russia Briefing 2017)

If the route would not go through Russian Federation, it would most likely not be competitive. The reason is because there are inconsistencies between Ukraine, Kazakhstan and Azerbaijan. The inconsistencies are in the tariff policies between the countries. To make the route more competitive, the countries' representatives have met in 2016 to discuss the flaws and also try to develop a common tariff. By this way the route would be possibly competitive. To coordinate the tariffs between the countries, they would have a route where there is possibility to transport goods such as Kazakh coal and dairy products. The new Silk Road has created competition between the countries. (Website of Transinfo.News 2016)

There is an agreement between Russia, China and Mongolia to a transport corridor. It will start a transport of regular road freight. The agreement between the three countries affect to the development. The development affects to positively to the economic potential of the three countries. There will be possibly a reduce in the transportation time between the countries and also between China and Europe. The volume of foreign trade cargo flows and also international trade would be more present in the countries. (Website of Transinfo.News 2016)

#### 2.4 Russia's benefits and challenges when investing to the new Silk Road

Russia's integration into the project is the most effective way to accelerate the modernization of its transport infrastructure. This would form the real foundation of the economy and modernization would allow Russia to ensure a reduction of the specific transaction and transportation costs of businesses. It is also to intensify the clustering of the regional economy. This would not just contribute to the growth of national wealth.

Russia is not the only one that is committed to the inter-regional integration. Kazakhstan participates also in the Economic Belt Silk Road. There are considered several options in the direction of Kazakhstan. To Western Europe, a total length of

10900km that goes from Lianyungang through Kazakhstan and Russia. According to experts this will form an economic zone that implements up to 23% of world exports. The project is a “challenge” for Russian economy. This is because it can reduce the flow of goods, freight of the Trans-Siberian Railway. If the pace of the modernization of the international transport corridor in Russia does not increase, as a consequence the value of the transit potential will plummet. The reduced development of the effective mechanisms to attract Chinese capital, that is aimed at implementing the Economic Belt Silk Road, will allow the Russian Federation to fill the gap between the possible amount of funding that is necessary for intensive development which is 11,4 trillion rubles. 5.5 trillion rubles comes from the state budget. The limited capacity of state budget requires to consider regarded budget not as a source of funding. It is only as a factor to stimulate the influx of foreign investment in transportation sector. The trend is observed in the analysis of investment infrastructure projects of the federal target program of the Transport Strategy of the Russian Federation for the period until 2030. This provides for the involvement of 62,1% of foreign investment.

Russia benefits not only investing itself to the Silk Road but investments that go to Russian Federation as well. China has invested to Russia with the Economic Belt Silk Road. The infrastructure that exists is the focus point. The existing roads are repaired and what is absent needs to be developed.

With potential and opportunities, there are weaknesses in the region. The weaknesses are for example barriers. Also the market size issues limits. Because there are individual economies, a regional approach is used in the area of economic development.

Russia will have unity to the new Silk Road more with railroad projects. Those projects will link Russia to Central Asia and China with roads and railroads. Modernization and transportation programs are the main ways to invest to the Economic Belt Silk Road. There are and will be a number of investments done. The objective and purpose is to connect China and the neighbouring countries to the global economy.

In Russia, transportation from China and to China grew 83,8%. China is most active in the Trans-Siberian transportation. This has resulted growth in indicators. The traffic volume rose by 19,8%. This means that it grew from 205,8 to 246,5 thousand TEU (Twenty foot equivalent unit). (Website of Transinfo.News 2016)

The influence Russia has in the region is significant. That comes with the Trans-Siberian routes, that go from East Asia through Europe. In addition to the route, Russia has a political presence in Central Asia and also in the Middle East.



Figure 3. Map of Russia's railway lines (Website of Wikipedia 2012)

Central Asian countries have to think the cooperation with China in the new Silk Road. They have to think that is it going to be beneficial economically. Even though these countries are pro cooperation it is important to recognize if it is supportive. For them it is more about the individual projects that take part in the new Silk Road. Foreign investments are most likely not going to be refused.

China is the most important partner and investor in the Central Asia. China is a big part of the region and it benefits with gas imports. The gas import to China is going to increase in the future. Oil from Kazakhstan is also something that benefits both Kazakhstan and China. The trade between Kazakhstan and Kyrgystan and China is

significant. The foreign trade of China is around \$3860 billion. (Website of Russian International Affairs Council 2013)

China has invested a lot of money to the new Silk Road initiative. There has been \$40 billion invested to the new Silk Road Fund. There is also Asian Infrastructure Investment Bank worth of \$100 billion. Private investors, with £3,2 million, have created Green Silk Road Fund. China invests substantially to the new Silk Road and to the development that it needs. There is a possibility for low-interest and long-term loans for countries that go along the new Silk Road. China is looking for investment partners for the infrastructure projects. China does not want to invest alone. For solo investment, the sector would need to be very important for China. Even though China does seem to invest alone substantial amounts, they do prefer a shared risk. This way it is more sustainable. There are undoubtedly geopolitical interests there. China is interested in the idea of new international order. With politics, China does want its Western region to develop economically since it is behind when comparing it to the Eastern region. Gateway to Europe, Asia and the Middle East helps in that. The economic transformation that is going on in China slows the economic growth. New markets to export their products would help with the development. The Silk Road initiative and the potential “boom” of infrastructure would benefit Chinese companies. (Website of The Telegraph 2015)

For Europe, the access to Eurasian trading area that is intergrated would benefit them only. The free trade agreements are atleast one benefit. Also the access to consumer market in China is an advantage. With China, the joint projects are something they relate positively to.

The estimation of investments to the new Silk Road are \$890 billion. China is planning to invest \$10 billion in 2018. The investment is planned by Asia Infrastructure Investment Bank (AIIB). China also has opportunities in the bilateral agreements. (Website of Financial Times 2016)



## 2.5 Pay-Back

The region where the new Silk Road is being constructed carries a busy traffic. There are numerous highways and railways that transport goods between countries. Russia alone has several roads to transport goods. With Pay-Back, the shorter the period the better it is. For the Silk Road, it has many investments in different areas. The Pay-Back can be calculated: cost of investment divided by annual cash flows.

The investments that the Silk Road and Belt require have long Pay-Back periods, since some of the investments are large. The need for different financing models are needed. It has been thought that PPP model is a potential way to give a push to the countries along the Silk Road. The deputy head of National Development and Reform Commission He Lifeng has suggested the potential that is in the PPP model. This model would help the financing companies to provide more channels and would provide progress in the projects. It is an innovative way to boost this since Pay-Back periods are mostly long-term.

It has also been stated that there is different ways to invest. It is possible to solicit money from the capital market, directly. There is also allowed social security funds and insurance premiums to invest. (Website of The Indian Express 2017)

The Pay-Back of railroad “Turkmenistan - Afganistan – Tajikistan” of the section of Turkmenistan – Afganistan is estimated to be 12 years. This gives a view of the possible Pay-Back period to all of the roads along the Silk Road. The Pay-Back period naturally varies with the amount of investment that is put to different sections. (Website of Silk Road Reporters 2014)

The visible sign of the new Silk Road is the cargo that arrived to Iran, Tehran by rail. It took 30 days to get to Tehran. Before the railroad, the cargo would have been shipped there through waterway. (Website of PBS Newshour 2016)

## 2.6 Political support

With the political situation not being stable, Russia has still a good opportunity with the neighbouring countries that once were part of the Soviet Union. The countries

that neighbour Russia and also that are in the region that participate in the Silk Road are Uzbekistan, Tajikistan, Turkmenistan, Kyrgystan and Kazakhstan. These are the Central Asian countries to participate in the Silk Road with China and its provinces Xinjiang, Shaanxi, Ningxia and Gansu.

The region with its diversities has a common language. Russian language has a strong place with communication in international commerce. In many of the countries in the region have Russian language as the second language and the language is also used in “government and business communication” (Investment guide to the Silk Road 2014). The Central Asian countries all have trade with Russian Federation with both export and/or import. (Investment guide to the Silk Road 2014)

There are different trade arrangements between the countries. The countries that are part of the Silk Road do not have regional free trade agreement (FTA). With some of the Central Asian countries, they have bilateral trade agreements (BTA's). They also have agreements with CIS countries (Commonwealth of Independent States). With Central Asian countries, China pursues BTA's strongly. With all the trade agreements there is also one development, the Customs Union (CU). It is an important development in arrangements in the regional trade. The Customs Union is between Kazakhstan, Belarus and the Russian Federation. There is a free flow of goods, capital and labour among Kazakhstan, Belarus and the Russian Federation. There is common tariffs, customs procedures, that are harmonized, and eliminated customs control.

Due to the recent politic situations, Russia has received sanctions from Europe and United States. The military tensions are tightened due to Crimea and Ukraine.

The sanctions that were placed on Russia, mainly by United States, are more of a problem to Europe than to United States. The trade between Russia and United States was/is very low compared to what it is with Europe. The sanctions have intensified Russia's relations with Asia. Russia will eventually “decrease” the trade with European Union and focus more on trade with Asia.

Russia and Vietnam form a bilateral trade. The trade with Russian Federation and China will be done by 2020. There are interest with other countries also to have trade

with Russian Federation. India is also going to form a bilateral trade with Russia. It will be boosted with \$30 billion by 2025. (Website of Russia Briefing 2016)

China is moving to the direction where it will be the world's largest trading nation. Russia and China have signed an agreement where Russia is to deliver oil and gas to China. It will be a 30 year long contract. The currency used for payments will be in local currencies. By that, Russia will not need to buy US dollar Treasury bonds for the reserves since it will not use dollars as a currency for payments. (Website of Global Research 2015)

The cooperation between different countries enhances cooperation in customs and exchange of information. The regulations and laws would improve and the bilateral cooperation would be easier.

The political stability in the region is itself an attraction. Also including to that, the improving investment environment, better infrastructure and also social stability are attractive to the investors. The effort that is given to intraregional and interregional economic intergration stabilize the region.

Belarus and Lithuania will take part in the new Silk Road. Together with Ukraine they want to bypass Russian Federation. A memorandum has been signed between Ukraine and Lithuania. The aim is to have the Silk Road go from Ukraine to China. It is a “Viking” project. The project has been launched already in 2003. The train would contain machinery, tractors, polyethylene and also ferrous metal products would go to Ukraine. Rubber, rental and ferrous metals would go to Belarus and Lithuania. Ferroalloys would go to Latvia and Estonia. The road, that is 1734km, would take the time of 52 hours. The container train that was shipped from Ukraine to China in 2016 took 16 days to arrive to the destination. The container train is called the new “Silk Road”. There has been a report that the lack of goods for transportation has resulted in a way that the transportation is stopped. (Website of Gazeta 2016)



Figure 4. The Silk Road bypassing Russian Federation (Website of Transinfo.News 2016)

## 2.7 Finance

The Silk Road as an infrastructural investment is one of the biggest investments in the world. The new Silk Road will create land routes that in turn will "free" a number of countries from the routes that go through sea trades. For Eurasian economy, the Silk Road is an element of intergration.

The collaboration of financial institutions and international companies will have a positive reaction towards trade and economic cooperation. It is important to have investments in order to promote that.

The Silk Road will go through a number of countries. It will go through countries in Central Asia, the Middle East, Europe and Russia.

The first investments from Beijing has helped to invest to Russia's liquified natural gas project.

The finance that is needed in the new Silk Road has risks in infrastructure that is happening in cross border infrastructure. The risks that are present in that are firstly political risks that happen inside the country and also risks that come outside. The situation affects to the neighbouring countries and to the region where the construction and project takes place. The finance also has risks with the construction

itself. The delay and time of the completion does not always stay within the budget. If the delays occur the finances increase which in turn causes potential tensions. The structural risks and the obligation towards the payments from third parties to the lenders also presents risks. The finance of the Silk Road and the finance on the construction of roads in general is a difficult area due to the events that can happen between the countries. The currency risk and the loss that occurs in the fluctuation from foreign rates is also a potential risk. This also includes restrictions in currency that are in countries with less development. The legal risk happens in area where the local law and norms that are in international law are not consistent. Also corruption, weak institutions and political influence are part of it.

In order to have a successful financing in infrastructure, the experienced, trustworthy professionals should be used to sponsor, contract and operate. It is important to attract investors and financing from the market. That is why the project's commercial viability is important to have an attractive project. In order to gain investors, the legal framework should be in check. (Silk Road Finance Corporation 2016)

China's low-value and high-value goods need market opportunities. China has to secure the energy supply routes. By doing that, new market opportunities for China's goods will be opened. The One Belt One Road (OBOR) has the means to do so. The trade that potentially comes from the trade lines connects over 65 countries. The trade that comes from the countries that participate potentially reaches to \$2,5 trillion in ten years. The new Silk Road is able to have energy exports with Central Asia, the Middle East and Africa.

With finance, the BRICS financial organization with the member countries (Brazil, Russia, India, China, South Africa) contribute \$100 billion initial capital evenly. By this, their objective is to support the construction of infrastructure among other objectives. (Silk Road Finance Corporation 2016)

There are variation of taxes in the countries that participate in Silk Road. The economies also have variations in the wages. Since the wages are lower in China, Kazakhstan, Kyrgystan, Tajikistan, Turkmenistan, and Uzbekistan, it makes them competitive when compared to Russian Federation, which is a CIS country. The

wages vary from 81 – 614 dollars compared to Russia's wage of 806 dollars. (Investment guide to the Silk Road 2014)

China has invested significant amounts to the countries that are part of the new Silk Road. To Kazakhstan, China has invested \$30 billion. Uzbekistan has received an investment worth of \$15 billion. Kyrgystan has \$3 billion. On top of the investments made to different countries, China has invested to repair the port of Colombo in Sri Lanka worth of \$1,4 billion. (Website of Combined Transport 2017)

China has done significant investments to the infrastructure. Its aim is to support the economic growth. The Silk Road project is about the logistic security. The transit corridor will strengthen China's position and influence in the region.

It is estimated that the strategy and the implementation are going to be trillions of dollars. The Nicaraguan Canal will cost \$50 billion and the Malacca Strait will cost \$28 billion. In one year, the Asia-Pacific region will have investments of \$750 billion. Kazakhstan leads, with Russia, actively the negotiations concerning fundraising. With Kazakh Invest, the negotiations have determined the agreement of framework. It is for the formation of industrial cooperation. The industrial joint projects, in the long-term, could be financed by China. (Website of CFTS)

In order to cut down time in delivery and lower the costs, the combination of transport models is ideal. Optimization of container transport routes is one of the benefits from combining the modes.

The route that is developed begins from Eastern China and ends to Russia and to the Baltic Sea. It would go through European countries and Central Asian countries. There are also other routes that can be thought that would include the Baltic countries.

## 2.8 Russia's interests

Russia has many interests in the new Silk Road. Russia is interested in the business matches with China's objectives in the new Silk Road. Also the development of modern transport corridors in Russia is something that they are interested in. This

means also across the EAEU. Russia allocated 302 billion rubles to develop the railway infrastructure. It will go on from 2013 to 2018. The estimated cost as a whole is going to be 562 billion rubles. This will promote the Russian railways. The railways are important in the central regions of Russia. The project includes on building high-speed rail lines.

Russia's interests are also in the oil and gas infrastructure. There is a development in Far East. Those developments' objective is to diversify the supplies of energy. This means to Asia and the Asia-Pacific region. There are contracts for delivering oil. Rosneft is working with China's National Petroleum Corporation. Russia has been able to increase the share in Mongolian market. The share of Rosneft's petroleum product supply to Mongolia is 80%. On top of this, Rosneft obtains assets in Asian markets.

Russia has also interested in joint projects. One of these is mobile operating systems and software development. Also optical cable that would be cross-border is something that Russia is interested in constructing. The joint projects would also include on building data centers to Siberia.

Research and development and China and India are an opportunity for Russian companies in terms of joint projects. These countries have a scientific and technological potential that is positive opportunity to Russia. Roskosmos has a cooperation with China and India. They operate in the field of satellite navigation systems and development of devices. (Website of Vesti Finance 2016)

### 3 RESEARCH METHODOLOGY

#### 3.1 Validity and reliability

The sources that were used in the literature review are vast. The literature review is valid and reliable due to the fact that the sources that were used were current and the information came from several sources. The sources were reliable from well known

websites. The sources included articles, news, and study papers by other authors. The information was always consistent in the various sources both from Russian and English. The information is valid and reliable based on the consistency and how current the sources were.

The idea for the thesis topic came from a visiting teacher from Poland. She presented thoroughly and in interesting way the new Silk Road. The new Silk Road as a thesis topic is current. The topic includes also Russia which is the author's own subject of interest. The author of this thesis had no previous knowledge of the new Silk Road. All the knowledge that are in the literature review are gained from researching the international articles and studies from other authors.

The author started the thesis with the literature review in order to gain information that can be used as a base in the interviews and interview questions. The literature review also gave material for the empirical data, which are the interviews. The interviews give more detailed information to the literature review. By this way the topic becomes more reliable and valid, as it is already from the researched sources.

For the interviews, three interviewees were chosen. They were Aleksanteri Institute, Cursor Oy and The Regional Council of Kymenlaakso. Together, as a source of information, they produce more extensive picture of the new Silk Road and provide more details for the topic. Aleksanteri Institute, Cursor Oy and The Regional Council of Kymenlaakso, as sources of information, were chosen by the author due to the fact that they are convenient sources of information to get reliable and valid answers. The three combined give more specialized information concerning what happens in Russia. These three sources were the best options for this thesis to gain more broad data. The interview results go together with the literature review.

### 3.2 Research methods

The research method for this thesis is qualitative method. Qualitative method was chosen due to the fact that the thesis is a research and only qualitative method was proper to use. Quantitative method was not necessary nor even possible for this



thesis. The information was gathered from various internet sources that were reliable. The sources includes articles, studies and news articles in English and Russian.

The qualitative method was used to conduct the research for the topic. The aim was to have in the end a clear picture of the investments made to the new Silk Road. The literature review concentrates to investments, opportunities and challenges of Russian Federation. The articles and other sources were as current as possible and thus give a current information that is happening during the time the thesis was done.

### 3.3 Collection of data

The method of collecting data in the thesis are research and interviews. The information for the research is gathered from various sources, both Russian and English. This is the secondary data that is used in the literature review. The author spent 5 hours a day to produce the literature review. The sources give information which is repeated in the various sources making it valid and reliable to use for the thesis. The interviews are a source of primary data. The interviews, the results from the interviews bring the whole thesis together with the gathered information. The primary data, interviews, and the secondary data, literature review, support each other. The interviews give qualitative data for the topic of this thesis, no quantitative data is used. The qualitative data supports the researched data in the literature review.

The empirical data consists of data only from interviews. The interviews present a purpose for this sort of research. The aim is to provide and research as valid and reliable information for thesis. The interviews support the finding that are researched from the secondary data.

The interviews are unstructured. The interviewees give open-end answers to the questions. There are no themes in the interview. This way they are able to give as broad answers as possible to the topics chosen to the interviews. The author also gains more knowledge from the interviews and is more informed about the topic. The answers that are gained contribute conclusions to the thesis.

### 3.4 Analysis of data

The research problem was already decided before the actual writing of the thesis even began. This helped when the research from the internet sources was done. The researching of the data was easier and more logic. The literature part came together easier with all the headings and sub-headings.

The research questions were not independently described in the literature review as such. The answers to the questions come together with the whole secondary data as such.

### 3.5 Scope and delimitation

The research for the thesis focused on the Russian Federation's investments to the new Silk Road. The thesis discusses also the opportunities and challenges that Russian Federation has in the development of the new Silk Road. The aim is to get a basic understanding on what goes on in the new Silk Road and with the investments and highlighting Russia's contribution towards it. The international characteristics are also topic of discussion with politics and with their contribution.

The limit to the thesis comes with the focus of the topic. The main limiting factor is Russian Federation. Although other countries are also discussed in the thesis, the focus is Russian Federation. The choice of choosing Russia as a part of the topic is due to the author's personal interest towards the country.

The limiting factor also is the topic itself. The new Silk Road focuses on specific regions and areas on the planet. Focusing to Russian Federation narrows the topic and makes it more compact. Russian Federation is a big contributor in the new Silk Road and thus makes it a convenient country to focus.

The investments section also limits the topic. On top of that the opportunities and challenges that Russian Federation has in the new Silk Road narrows the topic. The thesis and literature review provides needed information but not being too wide.

Due to the limitations that are in the thesis, it makes it more convenient to produce questions to the interviews that are relevant and focus solely to the topic of the thesis. This way the empirical data completes the literature review.

## 4 EMPIRICAL RESULTS

### 4.1 Conduction of the interviews

The interviews consisted of open-end questions and were held in April – May 2017. The questions focused on the investment parts from Russia's point of view. Also couple of questions were also there to get a view on how Finland fits in the new Silk Road. The interviews gave information that complete and complement the theory that was gathered from different sources in the theory part. Also it gives more broader picture when there is focus on Finland also. Together the interviews and theory provide as broad as possible situation that is as current as possible.

The interviews were conducted to three persons. The majority of the interviewees wanted to remain anonymous. The author decided to keep all of them anonymous. The interviewees were from Cursor Oy, Aleksanteri Institute and The Regional Council of Kymenlaakso. The topic of the thesis is not as current in Finland as it is in other countries which is why there were limitations to get interviews from many people. Fortunately there were couple of people who have some sort of knowledge of the new Silk Road and willingness to take part in the interviews. The interview questions focused solely on the topics of the thesis. There were no separate themes in the questions. The only extra addition were the couple of questions that focused on Finland. The interview questions can be found in the appendix part of the thesis.

The author conducted the interviews after the theory and methodology part were finished. This was the natural way of conducting and producing the thesis in order it to be logical and productive. The empirical data complements the theory findings.

## 4.2 Interview results

The interview answers are combined to give a clearer understanding. The answers are collected from three interviewees and together they support the theory.

Russian Federation has several reasons why it invests to the new Silk Road. The sanctions after Ukraine have forced Russian Federation towards the East, mainly towards China. Also because it expects some benefits from being a transit country between China and Europe – it is a natural point of geography. If Russia abstains from participating, it will lose the role of transition route from China to Europe to Turkey + South Caucasus and/or Iran. Also Russian Federation feels that it will gain economic benefits, for example with tariffs and with direct jobs.

The reason Russian Federation participates to the new Silk Road is that after sanctions Russia focuses more towards China and East in general. Also the reason that there are expected benefits with participating to the new Silk Road. It is important to be a part of transition route between China and Europe and between other countries in the region. Also the economic benefits are a factor with the participation. Russian Federation has good reasons to participate to the new Silk Road as with other participating countries.

Russian Federation has both problems and opportunities when it invests to the new Silk Road. The most obvious problem is that there are huge costs with infrastructure etc. Also the major problems are two-fold. The first set of problems are technical, given the differences in track gauge between Russia and China and also between most of Europe. The other set of problems are political ones, given Russia's increasing economic dependency from China. The most obvious opportunity Russian Federation has when investing to the new Silk Road is that the Asian market will open more to Russian Federation.

The benefits and challenges that Russian Federation has when investing to the new Silk Road are physical and political. Exports to China will facilitate both physically and politically. Also the benefits are typical for transit states elsewhere. This is that Russia will get revenues for transit of cargo from China to Europe. The challenges Russian Federation faces are also typical for transit country – related to Russia's

possible dependency from China, especially given the fact that Russia is not the only transit route from China to Europe, and the southern route via Turkey may become an alternative in the future. The challenge for Russian Federation is China's strengthening at the same time.

Russian Federation's political support towards the neighbouring countries is financial as well as political. Russian Federation offers certain support to political leaders in Mongolia, Kazakhstan and Central Asia as well as some financial support to countries like Kyrgystan. Over time they will be more and more dependent from China rather than from Russia given the economic weight of China.

Russian Federation has interests in the future. These are expanding trade relations and also increase of own production (based on own raw materials). The interests are also aimed towards economic development and increasing budget revenues and also to be an indispensable part of global commodity flows.

Russian Federation's investments into the new Silk Road proposes a possible opportunity for Finland also. Finland is able to benefit on Russia's investments into the new Silk Road since the passage to Asia will open. In a way Finland will benefit probably mostly indirectly, and this impact is supposed to be rather minor. Possible increase of Russia's GDP will contribute to Finland's economic growth. Also, Chinese cargo will reach Finland more quickly than now thus reducing transportation costs. If Russian Federation invests for example in improving the railroad tracks on a route that ultimately leads to Finland, it is clear that Finland will benefit, for example shorter transport times.

Finland has potentially a strategic opportunity as a part of the new Silk Road or as a target for investments. This opportunity can be possible through the Karelian silk track. The magnitude of expected profits are hard to declare and whether or not the investments are worth for Finland. Also there is required a good cooperation with China in order for Finland to have strategic opportunity.

The infrastructure needs additional construction and it requires also investments. The container terminals of the railways should be strengthened. Also the infrastructure definitely needs additional construction. This means the railroads etc. are not in as good shape, to put it mildly. For Finland, it is difficult to declare how much

investments it actually requires and what are the expected profits, if there is any. The need for a national level will ultimately depend on how much traffic volumes will eventually grow. For example, the design work at Kouvola Rail-Road Terminal is currently in progress. There is a need for increased axle loads. The handling capacity are required for 1100 metre long trains. Also the ports should be invested in.

Other countries who are interested in the new Silk Road can contribute by taxation and also with investment support. China has declared that it will help with the needed funding and financing of the projects and infrastructure.

The Karelian silk track project proceeds fast. It is estimated that exports from Finland are 1300 containers a year and imports are 14000 containers a year. Working container train connection raises demand for freight transportation. Finland and Russian Federation customs are promoting the project. Sweden is also positive about the project and the logistical and industrial aspects of it.

Innovation Oy has done the needed agreements with railway operators with China, Kazakhstan and Russia. The first test train will go during spring from China to Kouvola, Finland. The logistics operator is operated by kazakhstan's railways. The aim is to schedule the train connection and also to price container transport/shipment. The aim is to operate the train once a week.

The northern transport corridor for the flow of goods is being sorted out. Niirala's railway border station is thought for the logistic operators. The railway traffic from Niirala border crossing seems positive. Stora Enso started in fall of 2015 a container transport of dissolving pulp through Niirala to Russia and through Kazakhstan to Central China.

Sea transportation takes about a month but railway transportation takes only 8 – 10 days. The Silk Road initiative has Finland's and Russian Federation's customs' management's strong support.

The progress of the technological and development in the Far East can not be achieved only by governmental measures. It also requires a significant amount of foreign capital. Attractive investment climate is needed in order to convince and attract domestic and foreign investors.

Advanced Special Economic Zones (ASEZ) and free port system of Vladivostik have been set up in order to attract investments. The Far East Development Corporation (FEDC) manages both of them. It is a jointly owned by the Russian State and the Vnjeshekonombank State Bank for development and foreign affairs.

The managements structure of ASEZ area's support network is: on top is Deputy prime minister of commission on the implementation of investment projects (Yuri Trutnev). Below is Ministry for the development of the Russian Far east ( Alexander Galushka) who then governs the investments, development, funds and labour development.

Finland's inclusion in the target audience as a potential investors is a significant factor. It is significant in mapping potential new business opportunities on the Russian market.

From Finland and North Karelia – Trans-Siberia and Baikal – Amur routes connect via China to the main ports of the Far East. Which also have sea connections to Japan, South Korea and other parts of Asia.

The development of the Far East has a potential to increase the volume of Russian transit traffic between Asia and Europe. This can reflect in Finland and through Finland to other Nordic countries.

## 5 SUMMARY AND CONCLUSIONS

The purpose of this thesis was to gain and to give understanding about the new Silk Road, how Russian Federation participates with investments to it and also to get understanding about the political support that happens in the region where the new Silk Road is forming. The thesis emphasizes Russian Federation throughout the thesis. Russian Federations opportunities and challenges when investing to the new Silk Road are a focus. The topic of the thesis was chosen for it's current occurrence. The author does not include own opinions of the subject at any point. Empirical part supports and compliments the theory findings.

Empirical part was conducted with interviews from three interviewees. All the participants were from different fields of business and were not dealing with each other. They were from Aleksanteri Institute, Cursor Oy, The Regional Council of Kymenlaakso.

The author of the thesis had no previous knowledge of the new Silk Road and how Russian Federation participates to it with investments, infrastructure and politics. The author was positively surprised of the magnitude of the new Silk Road. It is obvious that Russian Federation participates extensively to the formation of the routes in Russia.

## 6 FINAL WORDS

The thesis subject was chosen when a visiting lecturer from Poland was presenting the new Silk Road. The topic seemed right for the thesis right away and the aspect of Russian Federation was chosen due to the authors own personal interest towards the country. The author was interested to gain knowledge on what sort of different projects does Russian Federation participate in.

The thesis helped the author to gain a better understanding of the whole subject of the new Silk Road. The knowledge that was gained gave a basic knowledge for the author.

The author worked with the thesis for 3 – 4 months. For the thesis, the author researched throughly the right sources to use as current information in the theory part as possible. All the free time that was left in a day was used to conduct the thesis. Since the beginning, the thesis topic, and the aspect of Russian Federation, did not cause any problems to the author.

The thesis, in some days, was very time consuming. This was especially when the research of the sources was taking place, both English and Russian sources. Best effort was used and in the end it was very interesting to learn and to write thesis about this topic.



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## APPENDIX 1

1. Why is Russian Federation investing to the new Silk Road?/ Miksi Venäjän Federaatio investoi uuteen Silkkitie hankkeeseen?
2. Why is Russian Federation participating to the new Silk Road?/ Miksi Venäjän Federaatio osallistuu uuteen Silkkitie hankkeeseen?
3. What are Russian Federation's problems and opportunities when investing to the new Silk Road?/ Millaisia ongelmia ja mahdollisuuksia Venäjän Federaation investoinneilla on uuteen Silkkitie hankkeeseen?
4. What are Russian Federation's benefits and challenges when investing to the new Silk Road?/ Mitä hyötyjä ja haasteita Venäjän Federaation investoinneilla on uuteen Silkkitiehen?
5. How does Russian Federation support politically the neighbouring countries?/ Miten Venäjän Federaation tukee poliittisesti naapurimaita?
6. What are Russian Federation's interests in the future?/ Mitkä ovat Venäjän Federaation kiinnostukset tulevaisuudelle?
7. Does Finland benefit somehow from Russian Federation's investments into the new Silk Road?/ Hyötyykö Suomi jollain tavoin Venäjän Federaation investoinneista uuteen Silkkitiehen?
8. Is there a strategic opportunity for Finland as a part of the new Silk Road or as a target for investments?/ Onko Suomella strategista mahdollisuutta olla osa uutta Silkkitietä tai ollakseen kohde investoinneille?

9. Does the infrastructure need additional construction and if yes then how much investments does it require?/ Tarvitseeko infrastruktuuri lisärakentamista, jos kyllä kuinka paljon investointeja se vaatii?