

Competition Between Japanese and Chinese Infrastructure Projects in Mongolia

P. V. Kulneva

Abstract

Mongolia is a landlocked country in East Asia, which has a number of advantages related to its geographical location, abundance of natural resources, openness to foreign capital, and dynamic development due to the market reforms carried out in the 1990s. This determines the interest in the country from China and Japan and the inclusion of Mongolia among the platforms of global competition between these largest Asian economies.

Development of Japan-Mongolia and China-Mongolia political and economic relations in the second half of the 20th century and Mongolia's economic progress in recent decades have coincided with increasing competition between Japan and China in the world stage. At present, both countries are important trading partners for Mongolia and sources of capital needed to build its infrastructure and integrate it into global supply and production chains. The study of Sino-Japanese interaction in Mongolia may help us understand how Japan and China compete with each other in the world stage and to specify their areas of specialization and rivalry.

The objective of this research is to show, taking infrastructure projects as an example, how the global competition between Japan and China unfolds in Mongolia. In order to evaluate the current state of economic relations between Mongolia and each of the countries, in the first part, the author traces the history of Japan-Mongolia and China-Mongolia relations from the establishment of diplomatic relations to the present time, focusing on infrastructure projects.

The second part analyzes the interaction between Japan and China in Mongolia in the context of their growing economic competition. The study sheds light on particular areas of rivalry, while demonstrating that Japanese and Chinese projects not only compete but also complement each other.

Keywords: Japan-Mongolia relations, China-Mongolia relations, infrastructure investment, Japan's ODA, ADB and AIIB, competition between Japan and China, Belt and Road Initiative, Mongolia in transport and logistics chains.

Introduction

China and Japan are the world's most influential economies located in the vicinity of Mongolia. Both states have their own history of interaction with Mongolia and play a certain role in its foreign economic and foreign policy relations.

During the 20th century, due to the state borders problem that both countries had at different times with Mongolia (primarily in connection with wars, including the Sino-Chinese war of 1937–1945), Sino-Mongolian and Japanese-Mongolian economic relations were not very active. Positive trends in this area appeared only towards the end of the last century. The increased global competition between China and Japan at that time made Mongolia one of the venues where the interests of the two countries collided.

Despite the low population density and relatively modest economic indicators of this steppe state of East Asia, a number of advantages of Mongolia make it an attractive place for investment by China and Japan and determine the potential of its economic cooperation with these countries. Mongolia has no access to the sea, but one of the sections of the Great Silk Road that once connected East and Central Asia passes through its territory. Taking into account the recently announced ambitious plans of the People's Republic of China to revive the Great Silk Road, Mongolia gets the opportunity

to regain its historical function and become a transit point for goods and energy resources, also expanding its own trade with neighbouring countries. Mongolia's long land border with China and Russia opens up possibilities for transporting goods through numerous border posts. Another important advantage of Mongolia is the variety of mineral resources. The country has large deposits of coal and fluorite, copper, gold, silver and other metal ores. There are also rare earth metals that are used in radio electronics, instrument-making, and nuclear engineering. At the same time, Mongolia's mineral deposits have not been fully studied, and the country continues exploration work. Although Mongolia's economic development is still based on the extractive industry, since the market reforms of the 1990s (not least thanks to Japan's assistance), the country has made a major stride towards economic diversification and openness to international cooperation. As is the case in the world stage, Chinese and Japanese economic projects in Mongolia complement each other in many ways. At the same time, the competition between them makes it possible, using the example of Mongolia, to better understand how the global roles of the two strongest Asian economies are divided. The chosen theme is also important in regard to Mongolia, for which this rivalry is a favorable factor. Thanks to their investments in the infrastructure of Mongolia and of the surrounding region, China and Japan make a significant contribution to the development of Mongolia and help integrate it in global logistics and production chains.

The objective of this study is to use the example of infrastructure projects to show how the global rivalry between China and Japan unfolds in Mongolia. To achieve this objective, the author aims to accomplish the following tasks:

- 1) to trace the history of the development of Mongolia's economic relations with Japan and China in the 20th and 21st centuries and to describe their current state in a comparative way, focusing on infrastructure projects;
- 2) to illustrate the interaction of Japanese and Chinese infrastructure projects in the context of global competition.

In the Conclusion, based on the results of the study, a conclusion will be drawn about the problems and prospects for continued cooperation between the countries in the area under review.

Development of Economic Relations of Japan and China with Mongolia

Japan and China established diplomatic relations with Mongolia at different times, and their economic ties with this country have advanced at different rates. Although the indicators of Japanese cooperation with Mongolia are quantitatively inferior to those of China, they are characterized by relative durability¹, steady growth and clear goals. For instance, Japan provided significant support to Mongolia in the course of the market reforms in the 1990s. Targeted support for specific projects plays an important role in the development of the Mongolian economy, both through Japanese financing channels and through international financial organizations, primarily the Asian Development Bank (ADB).

China's economic relations with Mongolia in the 20th century showed positive dynamics a little later, but they are characterized by a steep increase in indicators and a larger scale. Among other features, it can be noted that the advantages of the territorial and historical proximity of the two countries are clearly shown in the Sino-Mongolian cooperation. Whereas China, along with Russia, has always been among Mongolia's nearest neighbours, cooperation with Japan is carried out in the framework of the "third neighbour" concept.²

¹ Being a country that recovered fairly quickly after the war and embarked on the path of capitalist development, Japan had the opportunity to implement large-scale projects abroad earlier than China. In 1954–1973, the Japanese economy showed phenomenal growth rates, at times exceeding 10 percent, which made it possible to speak about the Japanese "economic miracle."

² Mongolia's foreign policy doctrine aimed at building relations with countries outside the circle of its nearest neighbours (which are China and Russia).

Japan

The mutual claims of Japan and Mongolia related to the war were settled during the period of 1956–1972. It is believed that the decision to establish diplomatic relations was made by the two countries' leaders after the participation of the Mongolian government delegation in the World Expo-70 in Japan (1970). Then, the parties agreed not to raise the issue of reparations anymore and to move on to negotiations on economic cooperation. Diplomatic relations between the two countries were established as soon as 1972, after an intensive negotiation process [Nyamtseren 2001, p. 19]. In 1977, Japan and Mongolia signed the Agreement on Economic Cooperation, which made it possible to begin the implementation of the first major joint project – the construction of a factory for the manufacture of “Gobi” cashmere products with financial, personnel, and technological support from Japan. In March 1990, a trade agreement was signed to secure the commitment to increase trade turnover to the highest possible level and facilitate the issuance of necessary permits for the import and export of goods. In February 2001, the two countries signed an agreement on investment promotion and protection, which provided favorable conditions for Japanese businesses in Mongolia. An important event in recent years has been the signing of the Economic Partnership Agreement (EPA) between Mongolia and Japan (February 2015), which stipulates, in addition to a phased reduction of customs tariffs, the liberalization of labor and capital movement, the creation of favorable conditions for the protection of intellectual property and other important measures for the development and strengthening of economic ties. Japan was the first country to sign an agreement of this format with Mongolia.

The Ministry of Foreign Affairs of Mongolia considers Japan to be one of its “third neighbours” with the “strategic partnership” level of relations: Third Neighbours. *Ministry of Foreign Affairs of Mongolia*. 2021. <https://mfa.gov.mn/en/diplomatic/56715/>.

The steps taken contributed to the growth of indicators of Japanese-Mongolian economic cooperation. By 2022, Japan's trade turnover with Mongolia had approached \$5 billion (Japan's imports from Mongolia – \$4.2 billion, exports – \$0.7 billion).³ The amount of accumulated Japanese direct investments in Mongolia currently stands at about \$1 billion. Japan ranks sixth by this indicator,⁴ and, in terms of the number of companies with Japanese capital (680 companies), it comes in fourth after China, the Republic of Korea and Russia [Mongoru keizai gaikyō 2023, p. 19].

Japanese investments are concentrated in telecommunications, banking, industrial production, mining, sales of mining and construction equipment, construction and energy. All enterprises with Japanese capital, working in different industries, provide conditions for improving the Mongolian infrastructure.

Japanese companies have made a significant contribution to the development of the extractive industry, whose products are the main export item of Mongolia. Sumitomo Metal Mining and Mitsui & Co. participated in the development of copper and gold mines in the country. Mitsubishi Corporation owns a 34-percent stake in Areva Minez together with the Mongolian state-owned enterprise Man-Atom and the Mongolian branch of the French industrial company Ogapo S. A., which is engaged in uranium exploration and production. At the same time, Japanese capital has interest not only in the extractive sector, but also in high-tech industries that create added value in the Mongolian industrial sector. In 2010, plans were announced to build, with the participation of the Japanese companies Toyo Engineering Corporation and Marubeni Corporation, an oil refinery in Darkhan near the border with Russia (estimated investment was

³ Gadaad khudaldaany güitsetgel ornoor [Foreign Trade Performance by Country]. *Mongolian Customs Service*. 2023. <https://gaali.mn/statistic/detail/03> (In Mongolian).

⁴ Mongolbank Statistics data. *Mongolbank*. 2023. <https://stat.mongolbank.mn>

\$600 million).⁵ There are also joint projects aimed at optimizing coal extraction and processing.⁶

While Japan occupies a modest position in terms of trade with Mongolia and direct investment and is inferior to its other partners, it is the undisputed leader in providing official development assistance (ODA) to that country.⁷ The projects implemented with ODA include the above-mentioned construction of the Gobi factory, which actually contributed to the creation of a new branch of Mongolian industry and had impact on the structure of Mongolia's exports. In the 1990s, thanks to the Mongolian market reforms, the scale of Japanese ODA expanded, and concessional yen loans were added to its forms such as gratuitous assistance and technical cooperation. In addition to supporting cattle breeding, financing the construction of schools, the supply of medical equipment, assistance to the country in preventing natural disasters, etc., ODA began to include large-scale infrastructure projects.⁸

In the 1990s, Japanese funds were used to modernize railway communications (loan years: 1993, 1994), upgrade the capacity

⁵ Marubeni: Tōyō enji to kyōdō de Mongoru no daruhan seiyusho kensetsu ni sankaku [Marubeni: Participating in Construction of Darhan Refinery in Mongolia Jointly with Toyo Engineering]. *Bloomberg*. 29.09.2010. <https://www.bloomberg.co.jp/news/articles/2010-09-29/L9HPoT6JIJUO01> (in Japanese).

⁶ Mongoru no tabantorugoi tankō de Nichi Mongoru kyōdō jigyō o jisshi e [Japan-Mongolia Joint Project to be implemented at Tavan Tolgoi Coal Mine in Mongolia]. *NEDO*. 17.02.2016. https://www.nedo.go.jp/news/press/AA5_100526.html (in Japanese).

⁷ Official development assistance (ODA) is provided by Japan to developing countries in the post-war period in order to promote economic growth and support modernization. It includes grant aid, yen loans, and technological cooperation. One of the ODA functions is also to compensate for the damage caused to recipient countries during the war [Kovrigin 2012, p. 10].

⁸ Activities in Mongolia. *Japan International Cooperation Agency (JICA)*. https://www.jica.go.jp/mongolia/english/activities/activity_02.html

of CHP-4 in Ulaanbaatar (1995, 2000), and develop the Shivee-Ovoo coal mine (1996, 1997).⁹ In the 2000s, efforts were focused on transport links. The most ambitious project was the construction of an international airport in Ulaanbaatar. An agreement on the allocation of a concessional loan by Japan for this purpose was signed in 2008, and the construction of the airport began in 2013. Its official inauguration took place in 2021. It is expected that the airport will receive 2–3 million passengers per year. A significant part of investments in transport links (roads, viaducts, interchanges) in recent decades has been aimed at improving access to the airport, this main transport hub of Mongolia.

In recent years, ODA has helped implement a large number of projects which are in line with the latest trends in socio-economic development. They are related to the construction of environmentally friendly cities (air pollution control in Ulaanbaatar, reduction of heating needs, etc.) and the creation of an inclusive society (which implies improving health standards and the quality of other basic social services). Japan continues to provide assistance in promoting market reforms, which is aimed at creating a fair competitive environment and developing capital markets.

By 2001, Japan's ODA had amounted to about 80 percent of all such assistance provided to Mongolia by OECD member countries, and although Japan's share declined slightly in the 2000s, it still ranks 1st among the donor countries providing ODA for Mongolia, overtaking not only the United States and the major economies of Europe and Asia, but also international organizations (Table 1).

It is also important to mention Japan's leading position in the Asian Development Bank (ADB), which is one of the largest ODA donors (see Table 1). The bank was established in 1966 with the direct participation of Japan, which has always been one of its leading shareholders (along with the United States). Until now, only Japanese citizens have held the position of president of the bank.

⁹ Japan's Assistance to Mongolia. *Embassy of Japan in Mongolia*. <https://www.mn.embjapan.go.jp/news/ODAenglish.PDF>

Table 1

The Largest ODA Donors in Mongolia

Ranking	ODA Source	Million US Dollars*
1	Japan	176
2	International Development Association	113
3	Asian Development Bank	87
4	USA	36
5	EU organizations	33
6	Republic of Korea	33
7	Germany	26
8	France	25
9	Switzerland	15
10	Hungary	8

* Mean value for 2020–2021

Source: Aid at a glance charts. Interactive summary charts by aid (ODA) recipients. Mongolia. *OECD – DAC*. 2023. https://public.tableau.com/views/OECDDACAidataglancebyrecipient_new/Recipients?:embed=y&:display_count=yes&:showTabs=y&:toolbar=no&:showVizHome=no

Mongolia became a regional member of the ADB in 1991, when it needed financial support for market reforms. The first aid was provided to Mongolia through the bank in the form of quick loans for basic needs such as purchases of wheat, medicines, fuel, materials and raw products for the construction and manufacturing industries. This was followed by loans to finance the budget deficit and the balance of payments. Throughout the period of Mongolian reforms, the ADB played a leading role in political transformations, the formation of a modern banking sector, infrastructure modernization, environmental improvement, the development of agricultural production and, on the whole, the integration of the country into the economy of the region. The development of minerals and energy has been an important source of financing

in line with Japan's interests. Telecommunications have become particularly important at the present stage. Thanks to ADB funding, mobile network and Internet coverage have significantly expanded, and most Mongolian residents now have access to information and services [Moving Forward Together... 2021, p. 18–27].

In terms of its structure, financing through ADB largely complements Japanese ODA, and the same goals can be achieved through different financing channels. This is clearly seen through the example of the Ulaanbaatar airport. The first major infrastructure loan was given by the ADB in the 1990s specifically for the modernization of the airport. Later, as early as in the 2010s, the airport was rebuilt with the use of ODA – a preferential yen loan from Japan – already in accordance with new needs.

By April 2023, Mongolia's accumulated financial obligations to ADB had reached \$4.14 billion, and 477 projects have been implemented or are in the process of being implemented. 80 of them relate to public sector management (total investments of \$877 million), 57 are related to transport (\$695 million), 44 – to energy (\$460 million), 46 – to water supply and other urban infrastructure (\$431 million). Less expensive, but numerous projects are being implemented in healthcare, the financial sector, agriculture, and education. A number of major projects pertain to the development of industry and trade and to currently relevant information and communication technologies. Over the past few years (2017–2022), ADB provided Mongolia with an average of \$308 million annually.¹⁰

The Central Asian Regional Economic Cooperation (CAREC) program, proposed by ADB in 1997 and aimed at the sustainable development and prosperity of the participating countries, including Mongolia and China, is of great importance for the development of infrastructure in the region. In 2001 to 2022, investments made under the program amounted to \$45.7 billion for 246 projects, of which \$16.9

¹⁰ Mongolia Facts. ADB's Work in Mongolia. *Asian Development Bank*. 2023. <https://www.adb.org/where-we-work/mongolia>

billion were provided by ADB, \$19.4 billion were given by the program's partners, and more than \$9 billion came from the governments of the member countries. Most of the investments go to transport (about 71 percent, or more than \$32 billion), energy (22 percent, or more than \$10 billion) and trade (3 percent, or \$1.4 billion).¹¹

Directly related to Mongolia are 36 projects, including expanding the transport network and improving its safety, modernizing the customs system and training the personnel, solving environmental problems (reducing air pollution from coal-fired power plants, introducing energy-efficient construction technologies), as well as consultations on the country's economic development strategies, assistance in developing trade policies, and assistance in Mongolia's inclusion in the WTO system. The total volume of investments as of 2021 was \$714 million.¹²

It is important to note that the ADB's financial assistance includes promotion of cooperation between Mongolia and China. A number of transport projects, in particular, are aimed at facilitating the transportation of goods between Mongolia and the People's Republic of China and between the People's Republic of China and Russia through the territory of Mongolia. Several projects implemented in the 2000s were targeted at developing Mongolia's regional cooperation with China. In 2006, funds amounting to \$0.8 million were allocated for the development of transport links, ensuring Mongolia's access to Chinese seaports, coordinating the work of customs authorities, energy cooperation, improving the political environment, and joint development of large border cities (the project was completed in 2010). In 2007, \$0.9 million (of which \$0.75 million came from the ADB and \$0.15 million from the governments of China and Mongolia) were allocated for technical aid and assistance in coordinating regional cooperation programs, including consultations and training of senior and middle-

¹¹ CAREC Project Portfolio. *Central Asia Regional Economic Cooperation (CAREC)*. 2022. https://www.carecprogram.org/?page_id=13630

¹² CAREC Countries: *Mongolia*. *Central Asia Regional Economic Cooperation (CAREC)*. 2022. https://www.carecprogram.org/?page_id=8

level government officials of both countries (the project was completed in 2011). In 2009, \$1.5 million was allocated by the ADB for technical assistance in liberalizing and improving the efficiency of trade between small and medium-sized enterprises of China and Vietnam and of China and Mongolia.¹³

China

The People's Republic of China (PRC) established diplomatic relations with Mongolia in 1949, but the Sino-Soviet split that began in the late 1950s caused Mongolia to have concerns about its security and sovereignty. It was not until the 1980s that the two countries resolved the issue of border demarcation, and their leaders realized the need to develop trade and transport links. The approaching end of the Cold War also helped to reduce the degree of tension.

In 1985, the countries signed an agreement on civil aviation and soon resumed direct flights from Beijing to Ulaanbaatar. In 1986, they concluded a five-year bilateral trade agreement. In fact, trade on credit has been conducted since 1951, and agreements signed in the 1980s, 1990s, and 2000s were aimed at simplifying and expanding it. In 1991, the sides signed agreements on investment protection and on the avoidance of double taxation. Exchange of delegations between the countries became more frequent, as did consultations on various issues and areas of bilateral cooperation. In 1994, during the visit of Chinese Prime Minister Li Peng to Mongolia, the Agreement on Friendship and Cooperation was signed, which consolidated positive trends in the development of bilateral relations.

The natural result of the efforts made was an increase in the indices of Chinese-Mongolian cooperation. By the early 2000s, the trade turnover

¹³ Project List. Mongolia. *Central Asia Regional Economic Cooperation (CAREC)*. 2022. [https://www.carecprogram.org/projects/?page_id=1&paged=1&country\[\]=mongolia](https://www.carecprogram.org/projects/?page_id=1&paged=1&country[]=mongolia)

had reached \$1 billion and continued to grow in the following decades, primarily due to exports from Mongolia to China. This, in particular, was facilitated by China's permission to use the port of Tianjin for Mongolia's access to the Asia-Pacific markets. Currently, China is Mongolia's main trading partner: about 70 percent of Mongolian exports go there. In 2022, Mongolia's exports to China exceeded \$10 billion, and its imports from China amounted to more than \$3 billion.¹⁴

In addition, China is one of the main sources of direct investment for Mongolia: to date, the country has accumulated 5.3 billion dollars' worth of Chinese capital, and, according to the Bank of Mongolia, China is the second largest investor in the country after the Netherlands.¹⁵ As for the number of companies, China ranks first: about 7.5 thousand companies with Chinese capital are registered in Mongolia [Mongoru keizai gaikyō 2023, p. 19]. Chinese investments mostly go to mining, energy, construction, finance, livestock processing, catering, and other industries. Mongolia is an important source of resources for China. After successful exploration work, Chinese oil companies are working in Mongolian oil fields. Since 2001, Dong Sheng Petroleum Mongolia has been producing oil in the Dornogov aimag in the south-east of the country. In 2013, Petro China Daqing Tamsag was given a 20-year license to produce oil in the Tamsag basin, the second largest oil field in Mongolia. The extracted oil is shipped to China, where it is processed, and part of the final product is transported back to Mongolia under a production sharing agreement. Oil production in Mongolia requires transportation infrastructure, which continues to improve. At the same time, there appear opportunities to increase the added value produced in the country. In 2021, the Chinese state-owned enterprise NORINCO concluded an agreement with Mongolia on the construction

¹⁴ Gadaad khudaldaany güitsetgel ornoor [Foreign Trade Performance by Country]. *Mongolian Customs Service*. 2023. <https://gaali.mn/statistic/detail/o3> (In Mongolian).

¹⁵ Mongolbank Statistics data. *Mongolbank*. 2023. <https://stat.mongolbank.mn>

of a 530 km-long pipeline for the transportation of crude oil from the Tamsag basin to the Dornogov oil refinery currently under construction with the participation of Indian capital.¹⁶

Of great interest to China are metals, which are widely found among the minerals of Mongolia. In the framework of the Chinese-Mongolian joint venture Xindu Mining Co., Ltd., located in the east of the country (Sukhbaatar), the parties cooperate in the development of the Tumertiyn Ovoo zinc mine under the “engineering in return for resources” model. The agreement was signed in 1997, and the development of the field began in 2005. To date, the total investment volume is \$50 million. The mine’s capacity is estimated at 300 thousand tons of zinc ore per year with a production period of 25 years [Duiwai touzi hezuo... 2022, p. 27].

Just as Japanese investments, Chinese capital is used not only in the extractive industry, but also in related industries. At the same time, various forms of cooperation create conditions for the exchange of technologies and personnel, increasing the employment of the local population, obtaining resources for the industrialization of Mongolia, and developing transport links.

In addition to the above-mentioned form of cooperation, “engineering in return for resources,” China provides personnel for contract work. In 2021, Chinese enterprises signed 68 contracts worth \$3.8 billion with Mongolian partners, which is 60 percent more than a year earlier. In total, over the entire period of cooperation, about one and a half thousand Chinese workers and specialists of various categories have been sent to Mongolia [Duiwai touzi hezuo... 2022, p. 28].

In 2007, China United Cement Group made investments in the construction of a production line with a capacity of 750 thousand tons of clinker and 1 million tons of cement per year. Currently, the plant employs

¹⁶ Qianshu jianshe cong dongfangsheng zhi donggebisheng 530 gongli shuyou guanda o xiangmu xieyi [Signing of the Agreement on the Construction of a 530-kilometer Oil Pipeline Project from Dornod Province to Dornogovi Province]. *Mongolian National News Agency*. 19.04.2022. <https://montsame.mn/cn/read/295051> (in Chinese).

125 people, including 30 Chinese citizens and 95 Mongolian citizens. Since the launch of production, the company has diligently fulfilled its social obligations, also making efforts to improve the professional and technical skills of the Mongolian personnel [Duiwai touzi hezuo... 2022, p. 28].

In 2014, the Chinese company China Longjian Road and Bridge Co., Ltd. entered the construction market of Mongolia, and it has already completed the construction of several large sections of roadway in the western part of Mongolia with a length of 165.98 and 167 km. Construction work is currently underway on other sites [Duiwai touzi hezuo... 2022, p. 28].

In 2014, Chinese President Xi Jinping, during his visit to Mongolia, made a proposal to explore the issue of bringing cross-border cooperation to a new level. After a long period of joint work, in late 2021, the parties signed an agreement on the establishment of the Eren-Hoto–Zamyn-Uud economic cooperation zone [Duiwai touzi hezuo... 2022, p. 28]. It was timed to coincide with the opening of a 900-hectare free economic zone (FEZ) on the territory of Zamyn-Uud in the same year. By 2021, a new highway, a sewerage system, water and electricity supply stations, and a thermal power plant had been built there due to a Chinese soft loan of \$58.8 million.¹⁷ Assistance in the development of the FEZ was also provided by the ADB: in 2020, the bank approved a loan for expenses related to the commissioning of the zone in the amount of USD 30 million. For the ADB, this is part of the previously mentioned broader CAREC regional economic cooperation project.¹⁸

Zamyn-Uud is the largest city on the Mongolian-Chinese border, with a border crossing to China. This is the busiest border crossing, which serves both road and rail transportation, not only between the

¹⁷ A New Free Economic Zone Starts Working. *Voice of Mongolia*. 25.08.2021. <http://www.vom.mn/ru/p/46769>

¹⁸ ADB to Support Economic Cooperation Zone for Mongolia. News Release. *Asian Development Bank*. 19.06.2020. <https://www.adb.org/news/adb-support-economic-cooperationzonemongolia>

two countries, but also between China and Russia, and, in some cases, also transit traffic going further to Europe. This makes the interests of both China and Japan in this area obvious. It is expected that, thanks to the financial support of the two countries, the Zamyn-Uud FEZ will make better use of the potential of the border crossing and will contribute to the development of industry, as well as the transport, logistics, and tourism sectors in Mongolia.

Mongolia is an integral part of the global projects and initiatives being implemented in the region under the leadership and with the participation of the People's Republic of China. The Belt and Road Initiative, proposed by Xi Jinping in 2013, provides for expanding China's global influence through investments in transport, logistics, and economic corridors covering the territories of more than 150 countries around the world. Mongolia, which has always been in the sphere of China's geopolitical, strategic, and economic interests and plans, is among the countries included in the initiative and has signed a corresponding agreement with the PRC. In 2014, Xi Jinping delivered a major keynote speech in Mongolia, where he outlined the prospects for bilateral cooperation and invited the country to participate in the Silk Road Economic Belt project (the overland part of the initiative aimed at creating trans-Eurasian economic corridors). It is important that the concept of the "Silk Road Economic Belt" echoes the "Steppe Way" infrastructure project, which was initiated almost simultaneously by the Mongolian side [Graivoronsky 2018, p. 55].¹⁹ According to the memorandum signed in 2014 in Beijing, Mongolia is among the "potential founders" of the Asian Infrastructure Investment Bank (AIIB), created at the proposal of China to finance infrastructure projects in Asia, and is its regional member.

The route map of the Belt and Road Initiative includes the China, Mongolia, and Russia economic corridor. The possibility of creating

¹⁹ The Mongolian "Steppe Way" initiative appeared in early 2014. Its idea is to use the cooperation of Russia and China to create a modern transport, energy, and other infrastructure in the country, which will be used for transit traffic.

such a corridor was first announced at the summit of the Shanghai Cooperation Organization (SCO) in Dushanbe in 2014. The idea was put forward by the President of Mongolia and supported by Chinese leader Xi Jinping [Ulagpan 2021, p. 2]. The program with the stages of the project was signed two years later, in 2016, in Tashkent. Like other programs of this kind, it aims to create modern transport, energy and other infrastructures necessary to take advantage of the geographical location of countries in international economic relations. Although each of the participating countries has its own interests (for Mongolia, this is the activation of its own trade flows with Russia and the use of its territory for the transit of goods during cargo transportation between China and Russia, and for China, the convenience of cargo transportation between Europe and the Asia-Pacific countries), the benefits of the project should ultimately be global and multilateral.

Mongolia is also being considered as a territory for the transit of Russian gas to western China through the Power of Siberia-2 pipeline, which is to connect to the Chinese West-East gas pipeline. In July 2022, Prime Minister of Mongolia Luvsannamsrain Oyun-Erdene announced the completion of the feasibility study of the project and the planned start of construction of the pipeline in 2024.²⁰ The project has been discussed for a long time; its implementation has been postponed several times, including due to Beijing's delay in concluding an agreement. This delay, however, is not related to the loss of interest in Mongolia as a convenient territory for the transit of energy resources. According to some assumptions, China's wait-and-see attitude is caused by its desire to get more favorable terms.²¹

²⁰ Power of Siberia 2 to divert Europe-bound gas to China. *Asia Times*. 20.06.2022. <https://asiatimes.com/2022/07/power-of-siberia-2-to-divert-europe-bound-gas-to-china/>

²¹ Gazprom responded to FT data on China's delay in the construction of the Power of Siberia-2. *RBC*. 25.05.2023. <https://www.rbc.ru/business/25/05/2023/646f78319a7947daefb08375>

The trends in the development of cooperation between China and Mongolia remain generally favorable. This is evidenced by China's patronage of Mongolia in many issues of foreign policy and international economic relations. For instance, in 2014, Chinese leader Xi Jinping expressed approval of Mongolia's entry into the Asia-Pacific Economic Cooperation (APEC) and welcomed its membership in the AIIB.²² The Chinese leader has repeatedly expressed support for Mongolia's participation in the SCO activities.²³

In 2020, Mongolia, with the support of China, became a full-fledged member of the Asia-Pacific Trade Agreement (known as the Bangkok Agreement until 2005).

Interaction of Japanese and Chinese Projects in the Context of Global Competition

Until the early 1990s, it was believed that Japan had every chance to become the first economy in the world, but after the collapse of the “bubble economy” in Japan's stock market and real estate market, a prolonged depression began in the Japanese economy. This period coincided with the rise of the Chinese economy due to the policy of “reform and openness” initiated by Deng Xiaoping in 1978. In the 1990s, the Chinese economy grew at a rapid pace, sometimes with double-digit figures, and there were signs that China would overtake Japan in GDP and become the second largest economy in the world after the United States. As expected, this happened in the 2000s: in 2001, China overtook Japan in GDP calculated according to the purchasing power parity of currencies, and in 2010 – in nominal GDP.

²² China Supports Mongolia to Join APEC. *Global Times*. 09.11.2014. <https://www.globaltimes.cn/content/890775.shtml>

²³ China, Mongolia pledge more cooperation. *Xinhua*. 11.06.2018. http://www.xinhuanet.com/english/2018-06/11/c_137245018.htm

As the reforms progressed, China became the most important direct investment area for world economic leaders such as the United States and Japan. Having accumulated enough capital and experience of interaction with the largest economic players, having become a full participant in the globalization process (which was manifested, among other things, in the successful completion of the negotiation process for its WTO accession by 2001), China moved on to the implementation of the “going out into the world” program (Chinese *zou chu qu* 走出去). The “going out into the world” program initiated by the country’s leadership is a well-thought-out policy aimed at increasing direct investment from mainland China, diversifying Chinese products and improving their quality, and promoting Chinese brands in leading world markets. This policy aims not only to increase quantitative indicators, but also to create a Chinese subsystem in the international division of labour. It involves borrowing advanced technologies, close cooperation with nearby newly industrialized countries and territories (including cooperation in exports to third-country markets), trade and contract cooperation with developing countries in order to obtain resources for Chinese industry and infrastructure [Salitsky, Semenova 2016, p. 5–6].

The Belt and Road concept fits in with these priorities and is a gesture demonstrating China’s global ambitions not only in the economic but also in the global political arena on the way to creating a multipolar world promoted by the PRC. Despite the stated goals of the AIIB founders to cooperate with other organizations and the intention to make joint efforts for the sustainable development of the region, the establishment of the Chinese-led bank in 2014 was immediately perceived warily by other actors. In 2015, the American *Foreign Policy* journal wrote that the AIIB poses a threat to the global economic world order and expressed fears that the era of US dominance with the so-called “Bretton Woods institutions” (IMF, World Bank, WTO) is coming to an end. The issue is China’s sole decision-making on the allocation of financial flows and the establishment of Chinese standards of trade and investment. *Foreign Policy* warned that the emergence of the AIIB could lead not to multipolarity, but to the formation of two economic

blocs in Asia: one led by China, and the other led by the United States and Japan.²⁴

In the same year, the Japanese newspaper Nikkei wrote about the Japanese government's intention to dramatically increase lending to infrastructure projects in Asia through the ADB and other organizations in order to counter the AIIB. At the same time, judging by the report of the Japanese newspaper, the Japanese side does not see a contradiction in the simultaneous existence of the two banks, since several dozen countries that are members of the ADB joined the AIIB at the same time. Japan's membership in the AIIB was considered a real prospect at the time.²⁵

The voices in support of Japan's accession to both the AIIB and China's Belt and Road initiative were indeed quite strong. In 2017, Nikai Toshihiro, Secretary General of the ruling Liberal Democratic Party of Japan, known for his pro-Chinese position, indicated after his visit to Beijing for the summit on the Belt and Road initiative the intention of the Japanese authorities to join the bank. According to the politician, Japan is closely monitoring its work, and the only question is how quickly it will make a decision on membership.²⁶ According to the assessment of the Institute of Developing Economies of the Japan Foreign Trade Organization (IDE Jetro), by 2017, most of the AIIB projects (17 out of 24) had actually been implemented jointly with other organizations, including the World Bank, ADB, EBRD, and others. That is, there was no

²⁴ The AIIB Is a Threat to Global Economic Governance. *Foreign Policy*. 31.03.2015. <https://foreignpolicy.com/2015/03/31/the-aiib-is-a-threat-to-global-economic-governance-china/>

²⁵ Setsuritsu junbi susumu 'AIIB' Nihon wa dō suru? [Preparations for Establishment of "AIIB" are Underway. What will Japan do?]. *Nikkei*. 22.05.2015. <https://www.nikkei.com/article/DGXZZO75366460X00C14A8000078/> (in Japanese).

²⁶ Japan's ruling party heavy weight signals readiness to join AIIB: *Nikkei. Reuters*. 16.05.2017. <https://www.reuters.com/article/us-china-silkroad-japan-idUSKCN18B2S9>

reason to speak about the bank's monopolization of the lending market for infrastructure projects [Chūgoku "ittai ichiro"... 2018, p. 5].

However, Japan's accession to AIIB has not yet taken place. The reason for the difference of opinion in the Japanese government is doubts about the reliability of the lending mechanism, transparency of the bank's management with the decisive vote of China, taking into account the environmental and social problems of the recipient countries. A certain role is probably played by the US pressure exerted on Japan in the context of tensions existing between Beijing and Washington.²⁷

Interestingly, China has been a regional member and shareholder of the ADB since 1986 and has repeatedly demanded that it be given greater voting rights as a developing country. Nevertheless, its role is insignificant. As of 2022, China owns only 6.4 percent of the capital and is one of the largest borrowers of the bank (second after India by the accumulated total amount of assistance received and the first by the number of projects). Thus, the division of functions and hierarchy is maintained between the AIIB and the ADB.

Here we can also note some differences in the specializations of the two banks announced initially. While the ADB's goals are broad, and it strives for sustainable development and prosperity of the entire region primarily through poverty eradication, the AIIB considers its mission to achieve sustainable development by investing in the "infrastructure of the future." The functions of the banks do not coincide, but with regard to the development of the region's infrastructure, they undoubtedly overlap, and the desire of each of the parties – both Japan and China – to gain access to an alternative channel of investment indicates their increasing rivalry in the 2000s.

The same applies to the ADB CAREC program and the Chinese Belt and Road Initiative. While the program focuses on sustainable economic development, the Belt and Road megaproject is primarily

²⁷ Japan split on joining AIIB bank, caught between US, China. *Reuters*. 20.03.2015. <https://www.reuters.com/article/us-asia-aiib-japan-idUSKBNoMGo7Y20150320>

related to transport links (although one implies the other, both sea and land routes of the Chinese megaproject will be created with a focus on environmental issues, human capital, and peaceful development of the regions involved).

The increasing competition between Japan and China is also evidenced by the nature of the projects being implemented. Although the countries' investments in transport infrastructure cover different areas and routes, these routes will inevitably overlap (like the CAREC program, the Belt and Road initiative includes communication with the countries of Central Asia, and one of the CAREC economic corridors partially coincides with the China, Mongolia, Russia economic corridor). Ultimately, the distribution of freight flows between the largest economic centers will depend on the created network of motor roads and railways, and the map of land communication in the region.

Also indicative is the order in which projects of a similar profile are initiated and implemented. Like the establishment of the AIIB, which was undoubtedly conceived by China as an alternative to the ADB and other financial institutions, the Belt and Road initiative also challenged Japan in those areas where it had already been active in the 2000s (this applies, in particular, to the previously mentioned ADB projects on optimizing communication between Mongolia and China). Although Japan indicated its presence in the region earlier, China's goals are larger and more ambitious. Currently, both countries are simultaneously increasing their investments. Japan retains its already taken positions and high-tech specialization, while at the same time trying to raise its cooperation with Mongolia to a new level. It is significant that the conclusion of the EPA agreement between Japan and Mongolia followed shortly after the announcement by the PRC of its intention to create the China, Mongolia, Russia corridor. One of the factors that hold back the growth of Japanese investments in Mongolia is the high degree of uncertainty and imperfection of legislation in that country. The Embassy of Japan in Mongolia points out that Japanese companies face a lack of guarantees and unpredictability of partner behavior, difficulty in accessing information, lack of transparency of regulation, unlawful

interference of officials in the activities of companies, corruption, and other risks.²⁸ The business environment in Mongolia remains quite unfavorable for the Japanese, but, at the same time, it is not so unusual for Chinese companies and government agencies. Together with the geographical proximity and closer historical contacts with Mongolia, this gives China certain advantages.

The task of creating a modern transport cluster in the region is not easy and is designed for a long period of implementation. In the meantime, the true object of interests and the field of competition between the two countries is not so much infrastructure as natural resources and markets, access to which is provided due to this infrastructure. Another task facing the countries is to maintain and optimize the existing production clusters in the region, which requires them to make efforts to develop convenient logistics.

Issues leading to a conflict of interests are increasingly becoming a cause of tension. In 2006, the Chinese media accused their Japanese colleagues of publications discrediting Sino-Mongolian relations and overestimating the prospects of Japanese-Mongolian cooperation, allegedly in order to gain wider access to Japan's development of Mongolian minerals.²⁹ The Japanese media often criticize the Chinese mega-project "Belt and Road," which is accused of being an attempt to control transport routes from China and drag the participating countries into a "debt pit." In 2013, pointing out the rising standard of living and expanding access to services for an increasing number of Mongolian

²⁸ Mongoru de tōshi katsudō o okonau Nihon kigyō ni taisuru ankēto shūkei kekka [Summary Results of Questionnaire for Japanese Companies Investing in Mongolia]. *Embassy of Japan in Mongolia*. <https://www.mn.emb-japan.go.jp/news/jpb422.html> (in Japanese).

²⁹ Wei zhengduo menggu kuangchan kaifaquan riben eyi lijian zhongmeng guanxi [Japan Maliciously Drives a Wedge Between China and Mongolia in Order to Compete for Mongolia's Mineral Development Rights]. *Sina*. 04.08.2006. <http://finance.sina.com.cn/j/20060804/13292793251.shtml> (in Chinese).

people, the online edition of the Chinese newspaper *Renmin Ribao* wrote about the growing competition with Japanese small and medium-sized enterprises in the food market.³⁰

But while the Mongolian market as such is quite small (the country's population does not exceed 3.5 million), it is of much greater interest to establish access to larger markets, in the long term – with the successful implementation of the CAREC program and the Belt and Road Initiative – to the markets of Central Asia and Europe. China as one of the CAREC participants is closely monitoring its implementation, trying to correlate the goals set by the ADB with the main components of the Belt and Road megaproject.³¹ The Belt and Road initiative also continues to be in the field of vision of Japanese business and officials, who are watching it with wariness and interest.

Conclusion

The expansion of economic cooperation between Japan and China with Mongolia indicates the growing competition between the two countries, which is related both to the short-term results of the ongoing projects and their expected more global effects.

However, it should be taken into account that, in many cases, the projects of China and Japan complement each other, and this means not only competition, but also complementarity. The most obvious example of complementary projects is Japan's financing of the construction of an

³⁰ Riben zhongxiao qiye qinglai mengguguo yu yu zhongguo shangpin zhengduo shichang [Japanese SME Favor Mongolia and Want to Compete with Chinese Products for the Market]. *People.cn*. 18.11.2013. <http://japan.people.com.cn/n/2013/1118/c35463-23576311.html> (in Chinese).

³¹ Zhongya quyue jingji hezuo di 16 ci buzhangji huiyi zai tajikesitan dushangbie juxing [The 16th Ministerial Meeting of CAREC Held in Dushanbe, Tajikistan]. *Belt and Road Portal*. 30.10.2017. <https://www.yidaiyilu.gov.cn/xwzx/hwxw/32135.htm> (in Chinese).

airport in Ulaanbaatar, and China's financing of roads leading to it.³² There is an example of Japanese-Chinese cooperation in the extractive industry. In 2014, a consortium of Chinese Shenhua Energy, Japanese Sumitomo, and Mongolian Energy Resources won a tender for the development of one of the world's largest coal deposits Tavan Tolgoi (which was subsequently canceled due to a protest from the Great State Hural). The efforts of the parties to develop infrastructure in the area of the Zamyn-Uud border crossing and in other territories also undoubtedly complement each other. The entire infrastructure created with the participation of the two countries can form a convenient and modern transport cluster in the future.

The intention of productive cooperation between the parties is reflected in the agreements on 52 joint projects between enterprises and government agencies of Japan and China signed during the Japan-China Forum on Cooperation in Third-Country Markets, held in October 2018 in Beijing.³³

In general, the region's demand for infrastructure investment is very high, and, according to some estimates, it could not be fully satisfied even if several international financial institutions worked there.³⁴ Despite the overlapping interests of Japan and China, this makes the search for investment areas a relatively easy task for them, and the competition we see in Mongolia is rather a reflection of a more global rivalry.

³² China and Japan's Investment Competition in Mongolia. *The Diplomat*. 01.08.2018. <https://thediplomat.com/2018/08/china-and-japans-investment-competition-in-mongolia>

³³ Daisangoku kyōryoku wa seiji no sanbutsu kyūgoshirae kadai sanseki [Cooperation with Third Countries Is a Product of Political Relations. Many Urgent Tasks]. *Mainichi Shimbun*. 26.10.2018. <https://mainichi.jp/articles/20181027/k00/00m/020/135000c> (in Japanese)

³⁴ The AIIB Is a Threat to Global Economic Governance. *Foreign Policy*. 31.03.2015. <https://foreignpolicy.com/2015/03/31/the-aiib-is-a-threat-to-global-economic-governance-china>

But this does not mean that the countries should not monitor the economic and political situation in the region in order not to miss their opportunities. In 2016, after the conflict with China over the invitation of the Dalai Lama to Mongolia, Mongolia, which was in dire need of resources due to the debt crisis, chose Japanese financing.³⁵ This means that when a promising niche for investment is vacated, it can immediately be occupied by another party. Ultimately, the competition between China and Japan is in Mongolia's favour, as it makes it possible to obtain capital from another source in the event of deteriorated relations with one of the partners. At the same time, Mongolia itself has a lot of work to do to improve the investment climate.

References

- Chūgoku “ittai ichiro” kōsō no tenkai to Nihon [Development of China's “One Belt, One Road” Initiative and Japan]. (2018). *Dokuritsu gyōsei hōjin nihon bōeki shinkōkikō Ajia keizai kenkyūjo* [Institute of Developing Economies, Japan External Trade Organization]. Retrieved from https://www.ide.go.jp/library/Japanese/Publish/Reports/Seisaku/pdf/2017_1_10_001.pdf (In Japanese).
- Duiwai touzi hezuo guobie (diqu) zhinan. Mengguguo [Country (Regional) Guidelines for Foreign Investment and Cooperation. Mongolia]. (2022). *Shangwubu guoji maoyi jingji hezuo yanjiuyuan, Zhongguo zhu mengguguo dashiguan jingji shangwu chu, Shangwubu duiwai touzi he jingji hezuo si* [International Trade and Economic Cooperation Research Institute of the Ministry of Commerce, Economic and Commercial Office of the Chinese Embassy in Mongolia, Foreign Investment and Economic Cooperation Department of the Ministry

³⁵ China and Japan's Investment Competition in Mongolia. *The Diplomat*. 01.08.2018. <https://thediplomat.com/2018/08/china-and-japans-investment-competition-in-mongolia>

- of Commerce]. Retrieved from: <http://www.mofcom.gov.cn/dl/gbdqzn/upload/mengguguo.pdf> (In Chinese).
- Graivoronskiy, V. V. (2018). Kitaiskiy mega-proekt “Ekonomicheskiiy poyas Shelkovogo puti”: mesto i rol’ Mongolii [Chinese Mega-Project “The Economic Belt of the Silk Road”: the Place and Role of Mongolia]. *Vostochnaya analitika* [Eastern Analytics], 3, 49–59. (In Russian).
- Kovrigin, E. B. (2012). Yaponiya – Kitai: ofitsial’naya pomoshch’ razvitiyu kak instrument ekonomicheskogo vzaimodeistviya [Japan – China: Official Development Assistance as an Instrument of Economic Interaction]. *Prostranstvennaya Ekonomika* [Spatial Economics], 3, 9–33. (In Russian).
- Mongoru keizai gaikyō [Overview of the Mongolian Economy]. (2023). *Nihon bōeki shinkōkikō (Jetro) kaigai chōsa-bu* [Japan External Trade Organization (JETRO) Overseas Research Department]. Retrieved from: https://www.jetro.go.jp/ext_images/_Reports/01/c6d8aa83ee2280bb/20220064.pdf (In Japanese).
- Moving Forward Together. The 30-Year Partnership of Mongolia and the Asian Development Bank. (2021). *Asian Development Bank*. DOI: <http://dx.doi.org/10.22617/ARM210427-2>. Retrieved from: <https://www.adb.org/sites/default/files/publication/751566/30-year-partnership-mongolia-adb-chapter1.pdf>
- Nyamtsere, L. (2001). Relations between Japan and Mongolia – Towards a Comprehensive Partnership. *ERINA REPORT*, 43, 18–23. Retrieved from: https://www.unii.ac.jp/erina-unp/archive/wp-content/uploads/2001/01/Er43_tssc.pdf
- Salitsky, A., Semyonova, N. (2016). Shelkovoe nastuplenie Kitaya [China’s Silk Offensive]. *Perspektivy. Elektronnyi zhurnal* [E-journal “Perspectives and prospects”], 1 (5), 5–14. (In Russian).
- Ulagan, Y. (2021). Belt and Road Initiative: Opportunities and Challenges for Mongolia. *The Asia-Pacific Journal: Japan Focus*, 19, 3, 1–12.

KULNEVA Polina Victorovna – PhD (Economics), Researcher, Institute of Oriental Studies of RAS: 12, Rozhdestvenka Street, Moscow, 107031, Russian Federation.

ORCID: 0000-0002-8699-5568

E-mail: kpoline@list.ru

This article was originally published in Russian. The reference for primary publication is: *Yearbook Japan* 2023. Vol. 52, pp. 11–36

DOI: 10.55105/2687-1440-2023-52-11-36