
2009 : Russian Gas Policy - First Step Taken

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For the past few years, the New Year has begun with a tradition: confrontation between Russia and Ukraine. The two countries celebrated this New Year with differences in their views of Ukraine's natural gas price and a transportation fee for Russian gas to pass through Ukraine territory to European countries. While in previous years these two countries have been able to reconcile their differences before resorting to confrontation, the situation this year has changed. Russia and Ukraine have accused each other of suspending of gas transportation, which has left European countries without gas.

Russian gas is normally transported through four export pipelines traversing Ukraine. Recently, though, they have not carried natural gas to their normal European markets, specifically Bulgaria, Romania, Slovakia, Slovenia, Croatia, Czech Republic, Poland, Hungary, Turkey, Bosnia-Herzegovina, Greece, Macedonia, Serbia, in short all of Central and Eastern Europe. These countries depend varyingly on Russian gas, with the annual percentage of consumed gas supplied by Russia totaling 45% in Poland, more than 60% in Greece, Austria and Hungary, and more than 80% in Bulgaria, the Czech Republic and Lithuania; Slovakia depends entirely on Russian gas. In addition, many Western European countries also import Russian gas. Approximately 43% of Germany's annual consumed gas comes from Russia, in Italy 20 %, in the Netherlands 6%, and in Great Britain 4%. As such, the dispute between Russia and Ukraine has affected many states in Europe.

It is noteworthy that Russia is the first large-scale gas owner and uses this advantage as an instrument of pressure in foreign policy. It is no secret Russia has long been trying to reap dividends from the existing potential in order to secure a privileged position in the export of natural gas to Europe. For the past several years, beginning with an annual increase in gas prices, Russia has attempted to pressure former Soviet states by giving a discounted price to the countries allied with Russia and charging more to objectionable regimes.

If the policy of providing cheaper gas prices for its allies was to provide Russia with a lever of pressure, then it has not been successful. The reason is that the pro-Western regimes, formed after the Velvet Revolutions in Georgia and Ukraine, have the opportunity to import cheaper gas. Ukraine, in particular, has been able to import cheap gas from Central Asia with Russia only responsible for its transportation. Georgia, in turn, started receiving gas from Azerbaijan, which by early 2007 sharply increased production , thereby ensuring an adequate supply for both domestic and international demand and saved Georgia from paying higher gas prices. But on the eve of 2009, Russia took a series of steps, in accordance with the leverage, to become more efficient.

First of all, Russia has agreed to a sharp increase in prices for natural gas imports from Central Asia, in order to prevent Ukraine from acquiring cheaper gas from these countries and forcing the country to pay a higher price. Moscow's purpose is to prevent regimes of Central Asia from seeking alternative routes to European markets, as well as to fill the shortage of gas resulting from a decline in production in Russia itself. It is no secret that the European countries, especially the EU members, are considering Azerbaijan, Turkmenistan, Kazakhstan, and Uzbekistan as alternative gas suppliers to their markets. In this case, European countries have proposed the Nabucco pipeline project, in which gas from these countries would be sent to Europe. By paying double the gas price to

Central Asian countries, Russia has succeeded in reducing the interest of these countries to the Nabucco project ` dispelling a potential political risk.

During President Medvedev's expected visit to Uzbekistan on 22-23 January 2009, it is expected that Russia will offer a price of \$326 per thousand cubic meters to import Uzbek natural gas. If so, Ukraine's hopes of acquiring gas at \$201, as well as Russia's original offer of \$250, are inconceivable. As the Prime Minister of Russia Putin has said, the time of cheap gas has passed.

In addition, in 2008, Russia took a step towards the creation of a gas OPEC, together with the other two largest holders of natural gas reserves: Iran and Qatar. Although this plan is unfeasible as the countries lack common interests on the issue of export of gas, the psychological significance of the matter is still filed a response in the international arena.

Due to the gas crisis between Russia and Ukraine, Russia expects some promising payoffs in foreign policy. First of all, 2009 is an election year in Ukraine, and this visible conflict with Russia could lead the electorate in Ukraine, an industrialized country totally dependent on outside energy supplies, to lose trust in its pro-Western government. Ukraine, which after the Velvet Revolution switched to a parliamentary system of government, could not recover from the political crisis taking place between the two branches of the executive branch, and within the coalition government. In addition, the accession of Ukraine to the WTO, which was seen as a further step in the integration into Euro-Atlantic space, has paralyzed several sectors of the economy. The situation worsened after the recent international financial crisis, which also adversely affected the industrial sector. These events open the door for the rise to power of the pro-Russian opposition, led by Yanukovich.

Secondly, the transit of Russian gas through Ukrainian territory will be observed by international monitors. It's no secret that Ukraine from time to time siphoned certain volumes of natural gas from the transit pipeline for domestic consumption. It should be noted that 80% of the gas exported from Russia to Europe passes through Ukraine. In this case, Russia has made possible an unhindered supply of gas to Europe, even the parties do not agree on the price of gas, and Russia stop sending gas to Ukraine.

Thirdly, the crisis in Ukraine once again prodded European gas importers to search for alternative ways of receiving Russian gas. In this case, the relevance of two Russian pipeline projects, Nord Stream, which will be constructed on the floor of the Baltic Sea and the South Stream, which is intended to be laid in the Black Sea, once again increased. And if at times some countries have resisted the implementation of these projects, expressing fears for various reasons, ranging from environmental issues to the security, the lack of heating could cool the zeal of the hottest skeptics on this issue.

Demand in Europe is constantly growing. By 2020, Europe will consume 720 billion cubic meters of gas. In this case, importing such quantities of gas will require additional transport routes. Particularly interested in the construction of the Nord Stream pipeline is Germany, which will receive direct access to Russian gas and will be able to play the role of a distributor to EU countries, thereby strengthening its position in Europe? In addition, according to the press information, despite the fact that the price of Russian gas has already exceeded \$400, Germany supposedly pays only \$280. Despite unconfirmed information, it brings to mind serious

questions regarding the Russian-German alliance to determine European gas policy.

Fourthly, the situation with Ukraine allows Russia to develop new foreign policy responses to events directly related to the interests of the country. As the experience of confrontation with Russia by Georgia during the August 2008 `five-day war`, Russia does not choose from a wide range of options, particularly in conflict situations. As a result of its use of force in Georgia, Russia had to recognize the independence of the two entities on Georgian territory, which in the long term may adversely affect the situation in the North Caucasus autonomous republics of Russia. In this case, the Ukrainian experience could become a kind of experiment in the development of alternative instruments of pressure on other countries.

There is no doubt that the crisis in Ukraine could encourage European countries to seek alternatives to Russian natural gas, as well as new means of importation. In this case, the main alternative is the Nabucco project, the implementation of which has perhaps been stimulated by the crisis in Ukraine. However, the passivity of European countries in realization of this project, as well as the increase in gas prices from Russia for Central Asian countries, has led to a situation in which the Nabucco is unlikely; the only country that still could supply gas to Nabucco is Azerbaijan. But Azerbaijan, which must deal with the Karabakh conflict, is trying to be more cautious in its policy towards Russia, especially after the events in Georgia. Besides, concerns of Azerbaijan about this are unfounded. Moreover, Russia, despite being a co-chair of the OSCE Minsk Group, created to resolve the Karabakh conflict, in late 2008 provided Armenia, which is in actual conflict with Azerbaijan, with a variety of weapons at a total cost of \$800 million dollars. This step can be regarded as the actual pressure on Azerbaijan, which holds a more independent energy policy, and has been increasing its military capabilities. At the same time, Russia has proposed to Azerbaijan to sell, at world prices, the entire additional amount of gas that the country plans to export. Azerbaijan has not yet made a specific agreement, but the pressure of Russia and the passivity of Western countries in realization of Nabucco are likely to lead Azerbaijan to agree to Russia's proposal.

In general, it is possible to say that Russia has quite effectively met the New Year, increasing its capacity in the management of energy policy in the field of gas in the Eurasian space and the use of these advantages as an instrument of foreign policy. Thus begins a new era in which the energy power factor will be more effectively used by Russia, prompting one to question how the European countries, currently lagging far behind Russia, will respond. One thing is clear: we will not have to wait long for an answer. Western countries, used to various disasters in the field of energy, are not the first to look for ways out of this situation. A new round of resistance in the field of energy in the Eurasian space begins.

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