

Shell, Statoil, and Norsk Hydro have demonstrated experience and records in developing offshore resources. Cooperation between all these players seems necessary to develop the Arctic hydrocarbon potential. Similarly, Russia's relations with its largest import market, Europe, and the other main oil and gas producing region, the Middle East and OPEC, can be characterized as a combination of cooperation and rivalry.

## 8.5 Russia–EU Energy Partnership

An energy partnership between Russia and Europe is almost inevitable. Russia is the world's largest natural gas producer and exporter and the second largest oil producer. The EU, with a population of nearly half a billion and one of the highest standards of living in the world, is a major energy consumer. Geographical proximity further cements these hydrocarbon ties. Little wonder that the EU imports a large proportion of its gas and oil needs from Russia and that the revenues Russia receives from Europe represent a major source of government income and overall gross national product. Finally, European energy companies play a significant role in oil and gas exploration and development in Russia.

Recent Russian–European energy cooperation goes back to 1968, when the Soviet Union started selling natural gas to Austria. Five years later (1973), Germany started buying Soviet gas. In the ensuing decades more European countries were added to the list and Russia emerged as the major oil and gas supplier to the EU as a bloc and to several individual European countries.

The two sides sought to institutionalize their emerging energy cooperation by negotiating and signing the Energy Charter Treaty (ECT). The roots of the ECT go back to a political initiative launched in Europe in the early 1990s, at a time when the end of the Cold War offered an unprecedented opportunity to overcome the previous economic divisions on the European continent [18]. The ECT and the Energy Charter Protocol on Energy Efficiency and Related Environmental Aspects were signed in December 1994 and entered into legal force in April 1998. By 2010 the ECT had been signed or acceded to by 51 states plus the European Communities. The ECT is a legally binding multilateral instrument dealing specifically with intergovernmental cooperation in the energy sector [19]. The ECT is designed to promote energy security through the operation of open and competitive energy markets, while respecting the principles of sustainable development and sovereignty over energy resources.

Specifically, the ECT's provisions focus on five broad areas: the protection and promotion of foreign energy investments, based on the extension of national treatment, or most favored-nation treatment; free trade in energy materials, products, and energy-related equipment, based on WTO rules; freedom of energy transit through pipelines and grids; reducing the negative environmental impact of the energy cycle through improving energy efficiency; and mechanisms for the resolution of state-to-state or investor-to-state disputes [20].

The EU spent years trying to get Russia to abide by the provisions of the ECT, which compelled Russia to open up the development of its hydrocarbon reserves and the running of its pipelines to foreign commercial involvement. Moscow, on the other side, signed the ECT and applied its rules on a provisional basis, but never ratified the Treaty. For years Russian officials had complained that the ECT was outdated and favored consumers. In August 2009 Prime Minister Vladimir Putin signed an order withdrawing from the ECT [21].

In another attempt to cement Russian–European energy cooperation, the two sides launched an Energy Dialogue on the occasion of the Sixth EU–Russia Summit (Paris, October 30, 2000). It was agreed to institute an Energy Dialogue between the EU and Russia in order to enable progress to be made in the definition and arrangements for an EU–Russia energy partnership. The overall objective of this partnership is to enhance the energy security of the European continent by binding Russia and the EU into a closer relationship in which all issues of mutual concern in the energy sector can be addressed while, at the same time, ensuring that the policies of opening up and integrating energy markets are pursued.

The Energy Dialogue aims at improving the investment opportunities in Russia's energy sector in order to upgrade and expand energy production and transportation infrastructure as well as improve their environmental impact, to encourage the ongoing opening up of energy markets, to facilitate market penetration of more environmentally-friendly technologies and energy resources, and to promote energy efficiency and energy savings [22]. The Energy Dialogue has permitted a good and frank debate at different levels between the EU and Russia and has allowed broad participation and involvement of the various Russian governmental bodies, the European Commission, EU Member States, and international financial institutions such as the European Bank for Reconstruction and Development, as well as a wide variety of EU and Russian energy companies.

Of course, the Energy Dialogue does not exist in a political vacuum. Rather, it simultaneously reflects and contributes to a broader economic, security, and strategic relationship between the two sides. For example, a more economically and politically stable Russia is less likely to show signs of compromise and accommodation with the EU on a variety of issues including pipeline routes and stability in transit countries such as Ukraine and Georgia. Thus, despite heavy mutual dependence, both Brussels and Moscow are pursuing separate strategies to improve their energy security and the overall perceived national interests.

One major reason for frequent disputes between Russia and some of the former Soviet republics (FSR) is Moscow's sensitivity to the political orientations of these former allies. Strategically, some Russian leaders do not wish to see Western influence in their "near abroad." Economically, Russian officials resent being beholden to these FSR, mainly Ukraine and to a lesser extent Belarus, for access to pipelines they once built and controlled. Against this backdrop, in the 1990s Moscow allowed a number of FSR to buy gas at hugely discounted prices, hoping to buy their loyalty. Apparently this policy did not work and Russia started demanding market prices close or similar to the ones West European consumers pay.

As early as 1990, Moscow cut energy supplies to the Baltic States in a futile attempt to stifle their independence movement. A similar episode took place in 1992 in retaliation for Baltic demands that Russia remove its remaining military forces from the region. In 1993 and 1994 Russia punished Ukraine, the conduit for about 80% of Russia's gas exports to Europe, by reducing gas supplies to force Kiev to pay for previous supplies and to pressure it into ceding more control to Russia over the Black Sea Fleet and over Ukraine's energy infrastructure. In addition, Russia resented the "Orange Revolution" that brought President Viktor Yushchenko to power in Kiev and his avid push for Ukraine to join NATO and the EU. A similar technique was applied to Belarus in 2004. In December 2005 and December 2006, Russia again cut or threatened to cut gas supplies to Ukraine and Belarus respectively to demand higher prices. In January 2009, Russia again cut off gas deliveries to Ukraine. Little wonder that a recent report by the International Energy Agency (IEA) stated that the flow of Russian gas through Ukraine may be subject to disruption "at almost any time" [23]. In order to face this challenge,

the European Commission proposed new regulations in July 2009. These require all Member States to have a competent authority that would be responsible for monitoring gas supply developments, assessing risks to supplies, establishing preventive action plans, and setting up emergency plans. The regulations also obliged Member States to collaborate closely in a crisis, including through a strengthened Gas Coordination Group and through shared access to reliable supply information and data [24].

Like his counterpart in Ukraine, President Mikheil Saakashvili of Georgia promoted economic and political reform at home and sought close relations with the West and membership of NATO and the EU. His domestic and foreign policy orientations further complicated relations with Russia. Tension between Tbilisi and Moscow was further escalated in August 2008 when Russian troops attacked Georgia in support of the breakaway Abkhazia and South Ossetia regions.

For many years, Georgia has been considered by the EU and the United States as one of the main building blocks in the formation of alternative energy routes which bypass the territory of Russia [25]. Major pipelines that carry Caspian oil and gas to Europe via Georgia had been built since the late 1990s and others are in the planning process. The Baku–Tbilisi–Ceyhan (BTC) oil pipeline and Baku–Tbilisi–Erzurum (BTE) gas pipeline are the most prominent. Russian air strikes did not hit any of the international oil and gas pipelines crossing the country or any oil ports, but they forced BP, which is an operator of both the BTC and BTE, to stop oil and gas shipments through Georgia as a precautionary measure [26]. In the aftermath of this military operation Russia recognized Abkhazia and South Ossetia as independent states and signed defense pacts with them. These defense agreements allow Russia to establish and maintain military bases in the two regions for the next 50 years [27]. These uncertain security conditions in Georgia raise serious doubts about the country's ability to maintain its role as a major corridor between the Caspian Sea/Central Asia and Europe.

Some Europeans perceive their reliance on Russian energy, in particular gas, as a threat. In order to mitigate this perceived threat, the EU and several individual European countries have taken several steps to reduce their dependence on Russia. Most prominently, Europe is investing in alternative energy sources, particularly renewable fuels and nuclear power. Equally important, Europe is establishing energy partnerships with other major oil and gas producers in Africa, Caspian Sea/Central Asia, and the Middle East. Finally, Europe is seeking to diversify pipeline routes away from Russia. A major part of this strategy is the Nabucco pipeline project. It would bring Central Asian and Middle Eastern gas to Europe without passing through Russian territory. It would run from eastern Turkey through Bulgaria, Romania, and Hungary, ending in Austria. In May 2009, Azerbaijan, Egypt, Georgia, and Turkey signed an agreement committing themselves to the project. Two months later (July 2009), the five transit countries (Austria, Bulgaria, Hungary, Romania, and Turkey) agreed a deal allowing work on the pipeline to start.

In addition, the EU is encouraging the construction of new intra-EU interconnecting pipelines. Several schemes have already been built, are under construction, and are being planned. These include routes connecting Hungary and Romania, Bulgaria with Romania and Greece, and Greece and Italy.

On the other hand, Russia is pursuing a two-fold strategy that seeks to further consolidate the EU's dependence on its hydrocarbon supplies and simultaneously open up new markets, mainly in Asia, to its oil and gas exports. In recent years the Russian government has invested great financial and political capital in promoting two pipelines – the Nord Stream and South

Stream. The Nord Stream (also called the North European Gas Pipeline) will pass under the Baltic Sea starting from Vyborg in Russia to Greifswald in Germany. It will transport gas to Germany where it can be shipped to Denmark, the Netherlands, Belgium, the UK, France, and other countries. The shareholders are Gazprom (51%), two German companies, and one Dutch company: Wintershall Holding AG (20%), E.ON Ruhrgas AG (20%), and NV Nederlandse Gasunie (9%) [28]. The Nord Stream scheme underscores Russia's strategy of avoiding transit countries and building direct pipelines to Europe.

South Stream is a joint venture between Gazprom and ENI, the giant Italian oil company. The pipeline will run from Beregovaya in Russia, underneath the Black Sea, to Bulgaria. From there the pipeline would branch off in two directions: one toward the north-west, crossing Serbia and Hungary and ending in Austria; the other directed to the south-west through Greece and Albania, linking to the Italian network.

In May 2009 Gazprom and ENI agreed to double the capacity of the South Stream pipeline from 31 to 63 bcm. The agreement was signed in the presence of Prime Minister Vladimir Putin and his Italian counterpart, Silvio Berlusconi. The agreement also defined how Gazprom and ENI would divide the gas between them. At the same time, Gazprom and national gas companies from Bulgaria, Serbia, and Greece signed deals to create joint ventures in these countries to perform feasibility studies and construction for the project [29].

Two other major pipelines carry Russia's oil and gas to Europe: the Druzhba pipeline and Blue Stream. The Druzhba pipeline, also known as the Friendship pipeline, is one of the oldest pipelines supplying Russian oil to Europe. It was built in the early 1960s to supply oil to the former Soviet bloc and to Western Europe. It carries Russian and Kazakh oil to points in Ukraine, Hungary, Poland, Germany, and other destinations in Central and Eastern Europe.

Blue Stream connects the Russian system to Turkey underneath the Black Sea. It is a joint venture between Gazprom and ENI. The pipeline became operational in December 2002. Part of this Russian gas is re-exported to Europe via the Turkey–Greece interconnector (inaugurated in November 2007), and another link connecting Turkey to Greece and ending in Italy is planned.

It is also important to point out that Moscow has skillfully exploited divisions among EU Member States by striking bilateral deals that undermine Brussels' efforts to forge a common energy policy. The gas trade divides the EU almost as much as it unites it. The EU's new Member States depend on Russia's gas to a far greater degree than Western Europe does. Thus, big Western customers such as Germany, Italy, and France are in a position to strike bilateral deals with Moscow, while Eastern states, particularly the most vulnerable ones such as Bulgaria, the Baltic States, Slovakia, and Hungary, plead for EU-wide solidarity [30].

Finally, European efforts to develop alternative fuels and to forge partnerships with oil and gas suppliers from Africa, Central Asia, and the Middle East have raised concern among Russian officials about the security of demand for their energy supplies to Europe. Accordingly, Russia has negotiated oil and gas deals with other consumers, particularly in the fast-growing and energy-hungry Asian market. In December 2009 a new oil export terminal at Kozmino, near the port city of Nakhodka on the Pacific Ocean, was inaugurated. The terminal has since been used to export oil from fields in East Siberia to China and other Asian markets. At the same time Russia launched the East Siberia–Pacific Ocean (ESPO) pipeline which runs from Irkutsk Oblast to Skovorodino near the Chinese border [31]. The terminal and the pipeline open the way for East Siberian oil to the Asia-Pacific region and contribute to the diversification of Russia's export markets.

This discussion of the uneasy energy partnership between Russia and the EU suggests a number of conclusions. First, both Moscow and Brussels depend on each other. Russia's oil and gas supplies are crucial to maintain Europe's economic prosperity and high standard of living while the revenues Russia receives in return provide a major proportion of the nation's national income. Second, this mutual dependence or interdependence is good economically and strategically for both sides. It raises the stakes that each side has in the other's prosperity. It can serve, and indeed has served, as the core for broader European integration. Third, Russia's stagnant oil and gas production, its unstable legal system, and changing attitude toward private and foreign investment mean that Europe has more reasons to worry about Russia's ability, rather than willingness, to deliver sufficient quantities of oil and gas to the EU in the future. Fourth, Russia's geographical proximity to Europe and the long and extensive historical and strategic ties between the two sides mean that Russia will always be an important player in Europe's energy outlook. At the same time, the EU's aggressive efforts to establish partnerships with energy producers in Africa, Caspian Sea/Central Asia, and the Middle East suggest that Russia's share in the European oil and gas imports is likely to decrease [32].

## **8.6 Russia, the Middle East, and OPEC**

Soviet policy in the Middle East was largely driven by a combination of ideological orientation, Cold War geopolitical considerations, and perceived Soviet national interests. The rise of military leaders with leftist orientations in key Arab countries like Egypt, Syria, Iraq, Algeria, and Libya provided a golden opportunity for Moscow to establish itself in the region and to counter US and European influence. The Soviet Union had very little contact with Iran and the rich Arab states on the Persian Gulf. The opportunity to mend fences came on the eve of the Gulf War (1990–1991), when Mikhail Gorbachev, the last Soviet president, supported the anti-Iraq coalition and, in return, secured major loans from Saudi Arabia and Kuwait [33].

Interestingly, Russian policy in the Middle East since the early 1990s has not been a complete departure from that of the Soviet Union in the preceding decades. Russian officials still seek to counter US and European influence and present their country as a superpower and an alternative to the West. A major difference, however, is that perceived Russia's national interests, rather than Cold War ideological considerations, have taken a prominent role in driving Russia's policy in the region [34].

The Shah of Iran was a close ally of the United States and was highly suspicious of what he perceived as Soviet imperialism. The hostility between the Islamic Republic in Tehran and the United States since 1979 has provided Moscow with a great opportunity to forge a closer relation with Iran. Iran needs the backing of global powers. Russia, and to some extent China, fulfill this role. Cooperation between Moscow and Tehran includes a variety of important issues such as arms sales, nuclear technology, the Caspian Sea, and energy. Iran buys a substantial proportion of its weapons from Russia. Russia is building the nuclear reactor in Bushehr and is protecting Iran from severe economic sanctions promoted by the United States and European powers based on allegations that Iran is trying to build nuclear weapons. Meanwhile, Tehran and Moscow do not agree on how to divide the Caspian Sea, but they do agree on containing the US role in the region. Finally, Russian firms are taking advantage of Western companies' hesitancy to do business with Iran. In December 2009 the French oil giant Total dropped out