2 Energy and Russia's foreign policy towards post-Soviet states

State–business relations in Russia placed energy companies in positions where they could become foreign policy tools. That is the supply side of Russian foreign economic policy. There is also a demand side. Without energy companies, Russian foreign policy would have been qualitatively different, especially in the post-Soviet region. Company operations were crucial to wider economic power projection. In the 2000s, Russia aimed to exploit regional influence in the energy sector to develop as a great power.

This chapter discusses how energy policy towards other post-Soviet states developed within the context of overall Russian foreign policy. It is instructive to look at the post-Soviet period in terms of the constraints on Russian foreign economic policy. The constraints mattered, and in the 1990s, they were of a domestic nature. Overall foreign policy was rhetorically ambitious, but Russia lacked in real power in global and regional affairs. The use of energy tools in the post-Soviet region stood out, because they were based on real economic power. It demonstrated a potential for influence that could be used coercively as well as for cooperative ends, even as Russia in practice often prioritised dominance. Still, domestic constraints mattered. In the 1990s, either economic weakness or a lack of policy priority and consensus limited Russia's use of energy power. The following boom in global energy markets increased activity in the global energy industries, also in the post-Soviet region, and contributed to growing Russian economic power.

In the 2000s, Russia became a genuinely attractive partner and investor, and foreign economic policy was highly prioritised. But as it started to use regional energy power to claim a global great power position, the limits to what energy power did and could potentially achieve began to show. This was a general foreign policy challenge (Rutland, 2008; Orttung and Øverland, 2011) visible in relations with Europe (Finon and Locatelli, 2008; Stent, 2008; Stegen, 2011; Closson, 2014), and post-Soviet states (Closson, 2011; Meister, 2013). This chapter shows that where in the 1990s, Russian foreign policy distinguished between a regional and an international level, in the late 2000s and 2010s it was no longer possible to isolate relations with its western post-Soviet neighbours from those with other European states. Moreover, it shows how a foreign policy based on economic power in interconnected energy markets is subject to market-related constraints. As any energy producer, Russia depended on global energy markets and on maintaining good working relations with energy consuming states (Rutland, 2008, pp.207–208; Orttung and Øverland, 2011, p.76; Closson, 2014, p.72). This was particularly salient for Russia due to its position as a price taker in global energy markets, and its role in supplying Europe with pipeline gas. Russia was in an interdependent energy relationship with European customers, and subject to the ups and downs of the oil price. These constraints were less consequential for Russian power projection as long as the oil price and the demand for gas and nuclear power were high. When market conditions changed, they had immediate effects.

Foreign policy fragmentation

In 1992 it was difficult to foresee that the energy sector's foreign policy lobbying power would become unsurpassed, comparable to that of the defence industry in the Soviet period (Pravda, 1996, p.183). During the break-up of the Soviet Union, policymakers were more preoccupied with the new possibilities that opened for Russia once it became free of what was perceived as the Soviet burden. Integration into the global economy, and above all, with the West, was a central aim of Boris Yeltsin's first government (November 1991 to December 1992). The intention was to support economic development aims – becoming a normal civilised country with a market economy, in short, a "normal great power" integrated into the global economy, as articulated by Foreign Minister Andrei Kozyrev (1992–1995) (Kozyrev, 1992, p.10). Energy relations with Europe and the rest of the world were important to integration. Especially in the Ministry of Foreign Affairs (MFA), relations with the other post-Soviet states had lower priority than those with the "far abroad" (Arbatov, 1993, p.20). When the "near abroad" was discussed, it was to emphasise that bilateral and multilateral relations would be reformed based on Russian interests (*Diplomaticheskii vestnik*, 1992). There was little attention to energy relations, with the crucial exception of the possibility of using them to influence other post-Soviet states.

This early period was characterised by a lack of foreign policy coordination and coherence within the government, and between government and the Presidential Administration. Combined with a lack of interest on the part of the Ministry of Foreign Affairs, this opened relations with post-Soviet states to other actors, from political factions and regional politicians to security agencies, military commanders, and industrialists. These groups maintained relations with bases of support, old colleagues and contacts, suppliers and markets in the region. Fragmentation was exacerbated by a difficult relationship between Foreign Minister Kozyrev and key elite groups, like the foreign policy committee in the State Duma (hereafter the Duma), from December 1993. In addition, responsibility for foreign economic policy was shared between two new ministries, the Ministry of Foreign Economic Relations (1992–1997) and that of relations with the Commonwealth of Independent States (CIS) (1992–1997).

Duality was maintained until the formation of the Ministry of Economic Development and Trade in May 2000. As a result, overall relations with the post-Soviet region deteriorated in the 1990s, and company priorities shaped foreign economic policy.

From mid-1992, parts of Russia's foreign policy elite began to perceive Russia as strategically weakened in the region (Sovet po vneshnei i oboronnoi politike—SVOP, 1992). Overall foreign policy priorities changed somewhat in December 1992, when Yeltsin replaced Yegor Gaidar's reform government with that of Viktor Chernomyrdin. Chernomyrdin's government[1] was far more attuned to the interests of sectoral lobbies, and was, as this book shows, closely related to the energy industries. It was a conservative government in the sense that it emphasised Russia's position in the region and abandoned the idea that Russia's interests could be subsumed into any broadly Western community. This increased consensus on foreign policy, with a more widely shared priority on the post-Soviet region (Light, 1996, pp.77–78). The consensus comprised an understanding that Russia's position in the region should be defended "in extreme cases by the use of force", especially when responding to "one-sided actions" on the part of the other states (Ministry of Foreign Affairs, 1993, pp.4, 8).

The new policy priorities also reflected popular discontent with economic reform, and with it, the policy of comprehensive economic and political integration with the West. The population had begun to yearn for a more active Russian policy towards the post-Soviet region as a whole (Dunlop, 1997, pp.55–57). This was articulated at the ballot box in December 1993, when nationalist and Communist candidates enjoyed great success in the Duma elections. However, actual foreign policy making remained fragmented, and priorities in the post-Soviet region remained divisive, until the end of Kozyrev's period as foreign minister in 1995.

Regional disintegration: Russia as a "leading force"?

At the regional level, the ties that bound the post-Soviet economies together were loosening. Post-Soviet elites disagreed over the speed of economic change, leading to the collapse of the ruble zone in 1993 (Dabrowski, 1993, pp.29–30). The trade patterns of the Soviet period ceased to exist, in part due to Russia's priority to integrate with the global economy (Michalopoulos and Tarr, 1994; Drabek and Benacek, 2013). While in 1989, Soviet trade had been overwhelmingly internal, by 1995, the CIS members had diversified their trade. For five member states (Armenia, Azerbaijan, Russia, Tajikistan, Uzbekistan) the regional CIS share of total export more than halved from 1989 to 1995 (Freinkman et al., 2004, pp.12–13). For six member states (Belarus, Georgia, Kazakhstan, Moldova, Turkmenistan, Ukraine) the share of export destined for other CIS states decreased from 85 per cent or more of all export in 1989, to 63 per cent or less in 1995 (Freinkman et al., 2004, pp.12–13). Only for Kyrgyzstan did the CIS share of all export remain at a relatively high level, 73 per cent in 1995, compared to 98 per cent in 1989 (Freinkman et al., 2004, pp.12–13).[2] This reorientation of trade towards states outside the region was accompanied by a "precipitous decline" in total international trade (Freinkman et al., 2004, p.7). The post-Soviet economies went through a serious crisis.

The economic effects of post-Soviet economic disintegration came as a serious political shock to elites in all the states (Light, 1996, p.83). The 1993 Russian policy turn in relation to the post-Soviet region was therefore part of a broader yearning in the region for selective post-Soviet reintegration, combined with policy coordination within the CIS framework. But unlike the other states, Russia approached the CIS as a framework within which it could assert regional hegemony. This ambition was tempered by a realisation that regional economic integration would come with drawbacks for the Russian economy. This ambiguous approach, lack of consistent implementation, and especially, Russian attempts to assert hegemony, met with a mix of selective engagement and disengagement by the other states. As a result, Russia's ties with other post-Soviet states were mainly managed in bilateral fashion. There was no regional strategy.

Another gap emerged between rhetoric and capacity for implementation in Russian policy towards the other states. The first policy document on Russia's approach to the region, the Strategic Course towards the Participant States in the Commonwealth of Independent States (hereafter the "Strategic Course"), was issued in September 1995. A brief, general outline, its central objective was to integrate the CIS countries economically and politically with Russia as a "leading force". This would create a region capable of "claiming a worthy place in global society" (Decree No. 940, 1995). In light of the transformational recession in the Russian economy, and unresolved security issues throughout the region, this was a proposition for the very long term at best. The other post-Soviet states were opening to the world and amidst a process of developing relations with European states, Turkey, the US and China. The Baltic states pursued integration with the EU and NATO. In some states, especially in Georgia, Azerbaijan and Turkmenistan, there was a profound scepticism towards Russia's policies. Other states, like Belarus and Kazakhstan, were closer to Russia in terms of strategic orientation, but still had reservations regarding the scope of integration. To all post-Soviet elites, escaping from Russian dominance was an integral part of state-building. The implementation of a Russian claim to leadership in the region was bound to be difficult, especially if that claim would include attempts to establish hegemony. The somewhat aggressive tone, emphasis only on Russian interests, and lack of mention of any potential for mutual advantage in the Strategic Course, appeared to confirm that this was indeed the aim. Russia's haphazard approach to the region in 1992–1993 and its decreasing attractiveness complicated its strategic return. In consequence, the gap between a rhetoric of undisputed regional leadership and weakening real control persisted through the 1990s.

Asymmetric energy dependence

Energy dependence on Russia was a Soviet legacy and a given for most post-Soviet leaders. Even with substantial oil and gas production in other union republics, 80 per cent was in the Russian Soviet Republic (Dodsworth et al., 2002, pp.9, 12). There had been few ties to international markets for oil, gas and nuclear fuel, and they were under central control. Within the post-Soviet region, energy supply was not easily transferred from existing suppliers in Russia to others. In 1992, the other post-Soviet states were highly dependent on imports for both oil and gas supply. Eleven of fourteen states depended on import for 80 to 100 per cent of their oil supply, and for 77 to 100 per cent of their gas supply (author's calculation based on IEA, 2016). Russia was their main source of energy.[3] The oil and gas producing Central Asian states, on their side, depended on Russian markets, or on transit through Russia to international markets. The nuclear energy industry in Kazakhstan and Ukraine depended on access to Russian technology for further development, including market access. In all cases, non-delivery, subsidy withdrawal, or a lack of development would threaten political legitimacy across the region.

Following the break-up of the Soviet Union, the Russian energy sector suffered from economic crisis, falling oil production and low hydrocarbon prices. The government decided on serious cuts to energy exports, especially of oil and oil products, to the CIS from 1993 (Becker, 1996, p.125). The aim was to make larger volumes available for export to global markets, at market prices, instead of supplying set quotas for CIS states in return for barter goods (Konoplyanik et al., 1992, p.44). The cuts were effective. In 1993, more than 50 per cent of Russia's crude oil export and 18 per cent of its oil products went to CIS states, while in 1997, 90 per cent of all oil and oil products export went to other parts of the world (Nekrasov and Sinyak, 2001, p.94).

Oil trade within the CIS transferred to market principles. This change contributed to an energy crisis, especially serious in Armenia and Moldova, and exacerbated tendencies towards fuel poverty across post-Soviet countries (Anex, 2002, p.400; Gentile, 2015, pp.585–586). In light of such consequences, gas and electricity trade remained non-market based and a matter of political negotiation. Russia continued to subsidise gas prices. All the western post-Soviet states were also transit states for Russian oil and gas, and their economies depended in part on the income generated by transit. This was often paid in kind, on barter terms. To post-Soviet governments, continued subsidies in gas pricing, acceptance of barter payment and soft payment terms reduced the cost of energy dependence on Russia, while at the same time increasing the cost of reducing it.

To Russia, the economic cost of regional energy trade remained substantial. Even with reduced oil trade, energy was less affected than other sectors by the overall trade collapse. In 1996, the first year for which there is data available in the UN Comtrade database, exports of fuel, electricity and nuclear reactors constituted 39.4 per cent of Russia's total exports to the post-Soviet states.[4]

To ease the terms for post-Soviet customers, price subsidies in energy sales were from 1992–1993 combined with loss-incurring loans ("technical credits") to CIS members to help them pay. But this exacerbated the problem, resulting in mounting debts. CIS energy trade burdened Gazprom and RAO UES in particular (Becker, 1996, p.125).

Nevertheless, Russia's foreign policymakers saw the benefits of maintaining relations as they were. Asymmetric energy dependence was an attractive lever of economic power towards other post-Soviet states. Russia's energy policy prioritised the development of what was rather vaguely referred to as "mutually advantageous energy relations with CIS states" (Decree No. 472, 1995), and emphasised that energy export should facilitate Russia's integration into the global economy (Korsun, 1994). The Strategic Course, on the other hand, contained the foundations of an instrumental approach to energy relations. Economic relations were not only a foundation for "non-compulsory" integration "at different speeds", they were also described as instrumental (Decree No. 940, 1995). They were tools for lifting Russia out of economic crisis and sources of Russian influence, including through "the formation of joint equity". In particular, post-Soviet states' willingness to pursue closer relations with Russia would be "an important factor in deciding the extent of Russian economic, political and military support". Russia's interests in bilateral relations included "the prevention of indebtedness in trade (…); the most favourable regime for transit of Russian goods" (Decree No. 940, 1995). In the energy sector, Russia had the capabilities to match these phrases. Energy trade and transit could, and would, be used to influence, reward and punish individual states, as a response to their foreign policy towards Russia.

In the beginning, debt was exchanged for equity in the gas industry. The state allowed Gazprom to recover debts through equity acquisitions, in the Baltic states and Moldova in 1994 and 1995, respectively. This was also the case with Belarus in 1993, except that the process took many years to accomplish (Chapter 7). But debt was exchanged for equity in Belarus's oil sector, creating the jointly owned company Slavneft. It was promised that Rosneft and Lukoil would acquire stakes in Belarusian oil refineries upon privatisation, but in the event this did not happen. By 1997, debt-for-equity deals were found useful in relation to Armenia, whose foreign policy position was also close to Russia. This policy was a rational business strategy, providing at least some compensation to e.g. Gazprom when it was otherwise difficult to obtain full debt repayment. To the government, debt for equity deals fitted well also with the idea of mutually advantageous energy relations. The practice spread to the electricity and nuclear industries in the 2000s, becoming a universal approach that could coerce and reward post-Soviet states regardless of their policy towards Russia.

Another characteristic of the instrumental approach to energy ties, Gazprom and Transneft's transit avoidance policies, appeared in the mid to late 1990s. They entailed the development of alternative routes, sometimes with excess export capacity, in avoidance of existing pipelines inherited from the Soviet period. The aim was to minimise the risk in relation to what from the Russian point of view were troublesome transit states like Belarus, Ukraine, Latvia and Lithuania. To elites in post-Soviet states, policies like these signalled that Russia pursued regional integration on its own terms, and that they would need to balance Russia in order to make room for strategic manoeuvre.

Outside the energy industries, Russia's integration policies in the post-Soviet region continued to display a gap between rhetoric and reality. Economic integration with Belarus, including a free trade zone from 1995, a Commonwealth of Belarus and Russia from 1996 and a Union State from 1997, went far on paper. Belarus's complete dependence on subsidised oil and gas from Russia made it willing to agree to integration. When Russia proposed terms that reinforced its dominance and subjected Belarus to further pressure, implementation stalled. One of Russia's aims with the Union State was to attract other states, Ukraine and Kazakhstan in particular, to closer integration. When this failed, Russia was left to observe how its influence began to erode in Central Asia and the South Caucasus. The Baltic states developed closer relations with, and eventually acceded to the EU and NATO. Ukraine and Moldova tried to maintain as balanced a foreign policy as they could, not committing to close integration with Russia.

Russia's foreign policy towards the post-Soviet region continued to develop based neither on assessments of neighbouring states' interests, nor on analysis of its overall effectiveness in promoting Russia's influence in the longer term. The changing international relations in the region were in the late 1990s increasingly perceived as a function of a global multipolar system. Now, Russia saw itself as a weakened great power facing competition in its regional sphere of influence from other great powers, above all the US. From 1996, the new Foreign Minister Evgenii Primakov's[5] multilateral foreign policy aimed at improving Russia's global position and advancing Russia's interests in what had become a far more conflictual relationship with the West (Katz, 2006, p.145). Russia's foreign policy in the region aimed to maintain control and hegemony in order to preserve some of its previous global influence. Under Primakov, foreign policy articulated a broader political consensus, but policy in the post-Soviet region remained incoherent.

A new approach: expansion and commercialisation

In the late 1990s, Russia's economic ties with the post-Soviet region were changing. Following the 1998 financial crisis, Russian recovery and catch-up growth entailed that companies accumulated the capital necessary for regional expansion (Crane et al., 2005, p.414). Russia's vertically integrated corporations and holdings were no longer muddling through. Instead they were consolidated entities pursuing bottom-up regional economic integration, at the very time when politically motivated top-down integration projects were failing (Libman, 2007; Libman and Kheifets, 2007, p.19). By the turn of the century, the importance of economic ties for foreign policy and Russia's international position was increasing, and the gap between bold rhetoric and real capabilities narrowed.

From the beginning of Vladimir Putin's presidency in 2000,[6] Russian companies' business operations were given a more central place in foreign policy. Ahead of the 2000 presidential election, Putin emphasised the need to rebuild and develop the state, not just in terms of internal capacity, but as a great power in the international system (Putin, 1999; 2000). In his view, this would be achieved through economic power projection across the post-Soviet region. This was a continuation of Primakov's foreign policy, especially its emphasis on Russian interests. The domestic constraints on foreign policy implementation were now reduced. The political landscape had changed. During Putin's first period, the Russian state went through a period of recentralisation. The scope for sectoral policy initiatives in foreign policymaking diminished. Compared to the 1990s, state capacity for policy formation and power projection increased. The elites, many of whom now had a reduced influence on foreign policy, in general saw this in a positive light. Part of Putin's attraction was that he seemed capable of delivering on Russia's return as a global great power, with a regional position that underpinned this aim. The 1998 financial crisis had demonstrated the dangers of elite infighting, and how this weakened the state. A stronger Russian state appealed to many elite groups, whether they understood it in terms of state capacity and economic development, or of national pride and great power status.

The economic realities began to change: there was more power to project. In part this was due to increasing oil production in the post-crisis recovery period. In addition, developments in global energy markets, and in oil markets in particular, had a substantial impact on Russia's economy. Oil prices recovered from a low of nine to ten US$/barrel in the winter of 1998–1999, to 30 US$/barrel in summer 2000, above 40 US$/barrel four years later and then 70 in 2006. The oil price boom was followed by substantial increases in gas prices, and beginning in 2003 increasing prices for uranium and other commodities. From 2001 to 2006, oil revenue increased from three per cent of GDP to 11.2 per cent (IMF, 2007, p.10; 2016, p.28). Russia's increased means, in relative and absolute terms, made a difference to its regional influence.

An energy strategy in pursuit of power

Strategic documents were revised. A comprehensive Energy Strategy appeared in 2003. In the previous energy strategy, issued in 1995, a major aim was to "support the export potential of the Russian fuel and energy complex and broaden its export potential" (Decree No. 472, 1995). There was also a need to attract foreign investment to the energy industries, especially to facilitate reorganisation based on market principles (Korsun, 1994). In 2003, circumstances had changed, and so had policy priorities. The new Energy Strategy was more specific, and reflected a new political reality. The energy sector should now be used to strengthen the state (Ministry of Industry and Trade, 2003). In 1995, there was an emphasis on "mutually advantageous cooperation with CIS states (...) [and] widening the mutually advantageous cooperation with other states" (Decree No. 472, 1995). Integration at the regional level was mentioned, referring to electricity, but this was not an immediate task (Korsun, 1994). In 2003, this gave way to a forthright description of the energy industries as a "core element of Russia's diplomacy", which could be used to deliver benefits to pro-Russian states (Ministry of Industry and Trade, 2003, Ch.7). The new Energy Strategy thus applied the foreign policy line from the Strategic Course of 1995 to the energy industries. The emphasis on their instrumental role in relation to foreign policy, which had appeared there, was now expanded to give them a more explicit political role. Great power, in this approach, meant economic power.

The context was a more assertive foreign policy, intended to bolster Russia's power in the post-Soviet region, and its international position as a counterweight to the US. In October 2003, several statements by Putin and Defence Minister Sergei Ivanov[7] highlighted the link between the state and foreign energy operations (RFE/RL, 2003; Suslov, 2003). Russia now reserved the right to intervene militarily in the CIS to settle disputes as a means of last resort, and the prerogative to maintain the natural gas and oil pipelines to the West in order to protect Russian interests, even "beyond Russia's borders" (RFE/RL, 2003). In this way, a sphere of influence in the post-Soviet region, aimed at protecting Russian national interests, would be supported by energy relations. Maintaining close relations with post-Soviet states gradually became more highly prioritised, also in practice. This change of priorities was further strengthened following the "colour revolutions" in Georgia (2003), Ukraine (2004–2005) and Kyrgyzstan (2005). Ukraine's Orange Revolution in 2004–2005 especially demonstrated to Russian foreign policymakers that their attempts at wielding influence had a limited impact (Kuzio, 2005; Wilson, 2010, pp.28–29). Regional integration processes, with Russia as the region's great power, came to the fore, and energy relations were a foundation for integration (Ministry of Foreign Affairs, 2007; 2008). The emphasis on integration in the post-Soviet region was to remain central to foreign policy in the coming years (Ministry of Foreign Affairs, 2013).

In the 2000s, strengthening Russian companies' positions abroad became a more pronounced priority (Ministry of Energy, 2009, p.9; Ministry of Foreign Affairs, 2013). The state offered the companies support in return for their role in foreign policy. This resulted in, for example, that the government from 2005 supported Gazprom's adoption of a commercially based pricing policy towards post-Soviet customers (called "European netback prices" by Gazprom). Making this change had long been anathema to the Russian government. A commercially based pricing policy reduced subsidy costs to Gazprom, but appeared to deprive Russia of the possibility of using price subsidies as a tool of influence. As will be discussed in Chapter 7, the use of carrots and sticks in post-Soviet gas trade continued, only now with price increases as a new stick and temporary postponement as a carrot. The exact terms and timing of the transition to "European netback prices" was used to expand Gazprom's control of post-Soviet gas sectors, through more exchanges of debt, or price subsidies, for equity. Russia's economic dominance in the energy sector increased further in the states that obtained a slower schedule towards European netback prices. In some cases, Russian dominance in the electricity and nuclear industries complemented Gazprom's position in the gas sector. In terms of overall Russian foreign policy, the implication was that Russia refused to underwrite regional integration. Other post-Soviet gas importers had little choice but to pay for Russian hegemony, either through equity transfers or in cash. In practise, post-Soviet gas prices continued to be differentiated on a scale of dependence/independence in their political positions towards Russia. The novelty was that, compared to the 1990s, states that were closer to Russia politically now found it difficult to resist Russia's economic dominance in the energy industries.

In the view of Russia's top leadership, energy power would increase Russia's international leverage, above all in Europe. Energy power enabled international action independent of other great powers. In August 2006, oil revenue was used to repay Soviet-era debts to international creditors ahead of schedule. When asked about his main achievements during his time in power, Putin made a point of this at the 2006 meeting of the Valdai Club (Kremlin.ru, 2006). Oil revenue made it possible to accumulate a Stabilisation Fund from 2004, in 2008 split into the Reserve Fund and the National Welfare Fund.[8]

Energy wealth could be channelled into local communities to develop and expand energy infrastructure and production, and support other economic sectors and the state. Before the financial crisis hit Russia in early 2009, energy was a wealth generator that increased the attractiveness and influence of the energy industries in the post-Soviet region. The high oil price, and debt-for-equity exchanges in non-petroleum industries, opened business opportunities for Russian companies in the post-Soviet region. The additional investment needed to take advantage of existing assets was not always large, but made a major difference to communities and elites in the region. Energy resources, it seemed, were an asset which Russia could continue to use to influence other states, to accumulate financial resources, and to support its claim to great power status.

The problems of energy power

Relations with the US and the European Union, Russia's most significant international partners, turned more complicated. The popular protests and "colour revolutions" in Georgia (2003), Ukraine (2004) and Kyrgyzstan (2005) were met with American and European engagement and support.

Georgia in particular began to pursue closer relations with the West, looking to NATO for a Membership Action Plan (MAP) and to the European Union for a more comprehensive European Neighbourhood Policy than the one launched in 2003. To Russian policymakers, these events combined two wholly undesirable developments, popular protest leading to a change of government, and increased western influence in the post-Soviet region. They were seen to be instigated by the West, with the US as the main culprit. Much of Russia's elites shared a zero-sum approach to great power politics, and concluded that Russia's influence in the post-Soviet region would disappear if left undefended.

But Russia's moves towards a strategy of dominance in the region further complicated relations with the EU. The strategy, intended as a basis for great power status, was founded on a distinction between major states and smaller ones, where the former dominated and competed for influence over the latter. The European liberal principle of equally valid claims to national sovereignty was incompatible with the introduction of distinctions among European states on the basis of their proximity to Russia. Particular attention was paid in Europe to how Russia used energy relations with regard to other post-Soviet states, since this had direct consequences for its European customers. Moreover, when Russia used energy power to claim great power status, it was seen as indicative of its overall approach to energy customers, especially weaker ones (Harsem and Claes, 2013, p.8). To the EU, Russia's energy policies were particularly important because Russia was its largest supplier.

Russia began to face market-related constraints in Europe also with regard to its energy relations with post-Soviet states, at least in gas. The problem became apparent when a dispute over gas transit terms between Russia and Ukraine reached crisis point in January 2006, leading to temporarily reduced gas supply to several European countries. In response, Gazprom and Russia blamed Ukraine. Following the crisis, governments across Europe started to question Gazprom's reliability of supply and to discuss how to reduce, or mitigate, dependence on Russian gas. Trust in Russia as a gas supplier was weakened (Finon and Locatelli, 2008). The reaction was particularly strong in Poland and Hungary. But Germany and Italy, too, expressed concern over the crisis.

When in August 2008 war broke out in Georgia, both the Russian state and energy companies carefully distinguished between state policy and business operations, insisting that business considerations dominated in relationships with customers and transit states. Inter RAO and Gazprom, the two Russian energy companies with significant operations in Georgia, were relatively unaffected by the brief war. The relatively limited European and American reactions that followed did not directly target Russian energy companies. However, only months later, another gas transit crisis soured relations between Russia and Ukraine. This crisis was to have much greater impact on Russia's position as energy supplier to Europe.

At this point, Gazprom began to face reduced demand and increased competition in European gas markets. It was slow to respond to those changes, insisting that everyone, including its European customers, gained from the status quo of long-term contracts tied to the oil price. To many in Europe, the Ukrainian transit crisis in 2009 indicated otherwise. Russia's proposed terms to Ukraine, and rhetoric during the crisis and subsequent negotiations to settle it, exploited Ukraine's weak position to the maximum and escalated the crisis. The European public and political elites were shocked by the implication, that by using gas transit to settle political scores with Ukraine and Viktor Yushchenko's government, Russia had jeopardised security of supply to Europe. By also using the crisis to promote the Nord Stream project as an alternative transit route (Stegen, 2011, p.6509), Russia played up the political side of the conflict. To many in Europe, this indicated that Russia was using the interdependence inherent in pipeline gas on long-term contracts to press for a greater market share, just as the market was turning in Gazprom's disfavour. In consequence, the established image of Russian energy companies in Europe as reliable and non-politicised suppliers suffered. They were seen as more closely connected to the government, and in consequence, as sources of Russian influence.

Increasingly, the dividing line between Russia's relations with post-Soviet states and other states, especially in Europe, began to blur. The strategy of re-establishing Russia as a great power based on energy had linked the post-Soviet level in Russian foreign policy to its global position. Around 2008–2009, the international reactions to that strategy affected both levels of Russian foreign policy. For example, Gazprom's projects to bypass Ukraine and Belarus as transit states occasioned alternative European proposals to reduce dependence on Russian gas. The Nabucco pipeline project[9] was one project that, in spite of uncertainties over supply and a lack of willing investors, attracted political support in Europe (Guillet, 2011). Gazprom's return proposal, South Stream, again bypassed Ukraine[10] and further reinforced the European perceptions that Russia aimed to use gas export as a tool to pressure Ukraine and take European markets captive. Russian efforts to control infrastructure and influence economic development in the post-Soviet region resulted in policies to balance Russia on the part of Georgia, Ukraine, Moldova and later Armenia. When in 2008 the EU engaged with Georgia, Ukraine and Moldova through the Eastern Partnership, Russian foreign policy towards these countries became entangled with its relations with the EU. This reinforced Russian perceptions of a zero-sum competition for influence over post-Soviet states.

The great power project backfires

Oil prices remained high to 2014. But in 2008–2012, the financial crisis and the "shale revolution" in global oil and (especially) gas markets profoundly affected the outlook for Russia as an energy-based great power. In the post-

Soviet region, policies of integration continued, finally with some success. Regional economic integration, which for so long had existed largely on paper, moved forward in 2010 with the establishment of the Customs Union of Russia, Kazakhstan and Belarus.

One reason for this was that Russia had changed its approach to integration with the global economy. The international financial crisis in 2008–2009 hit Russia particularly hard. Russia, like many other states, responded with increased protectionism (Solanko, 2016, p.5). Part of the response was to halt the pursuit of integration into the global economy, in favour of limited, regional economic integration within the Customs Union. Russia unexpectedly paused the World Trade Organization (WTO) accession negotiations in June 2009, at a point when they were close to completion. Russia would now pursue accession jointly with Kazakhstan and Belarus within the framework of the Customs Union. In 2012, the Customs Union was complemented by the foundations of a single market, the Eurasian Economic Space. But Russia's foreign policy aims in the post-Soviet region remained ambiguous. Tangible, selective, and possibly successful integration in the post-Soviet region seemed to indicate that Russian foreign policy could become based on shared interests and mutually advantageous terms. However, the means by which Russia pursued this goal were not mutually advantageous. By pausing WTO negotiations in favour of joint accession, all three Customs Union members were slowed down in their WTO accession process. And within the Eurasian Economic Space and from 2015 the Eurasian Economic Union (EEU), Russia was reluctant to take steps that could limit its room for manoeuvre. For example, it postponed the introduction of a single market for trade in oil, gas and petrochemicals.

The backdrop to this spurt of integration was nevertheless one of centrifugal tendencies and weakening Russian influence in the post-Soviet region. China dominated investment in Central Asia, and Central Asian governments in various ways balanced the two great powers. Russia did not have the economic resources to match Chinese investment. After the 2008 war with Georgia, Russia's engagement in the South Caucasus was by necessity more selective. In Ukraine, the approach of using economic ties for political influence, combined with selective engagement with pro-Russian politicians, made its real influence contingent on the prevailing forces in Ukrainian politics. A similar situation obtained in Moldova. Belarus was a partner and ally, but also adept at maximising overall returns from its alliance with Russia.

As Russia aimed to dominate the region, and saw its relationship with the West in terms of competition, its approach to the post-Soviet states was increasingly one of "either–or", driven by the approach that states had to choose, and pursue integration in one direction only (Samokhvalov, 2015, p.1372). Russia's view of the post-Soviet region was framed by competition with the West. Above all, the centrality of competition with the West was visible in the importance attached to attracting Ukraine as a member of the

Customs Union and the Eurasian Economic Space. In bilateral negotiations, Russia exerted pressure on Ukraine to join the Customs Union, reflecting its hegemonic position (Socor, 2010). With Ukraine, the potential for a regional economic and political bloc would be realised.

Euromaidan

The Euromaidan crisis in Ukraine in 2013–2014, and Russia's response to it, intensified the centrifugal tendencies in post-Soviet international relations. Energy relations played a part in the long run-up to the crisis, and Russian energy companies were considerably affected in the fall out. In 2010, the Kharkiv Accords between Russia and Ukraine exchanged a gas price discount in return for an advantageous deal for Russia on the terms of its military presence in Ukraine. According to this deal, the Russian Black Sea Fleet would be based in Crimea to 2042, possibly 2047. However, the returns disappointed Ukraine. The gas price discount turned out to be insubstantial. In addition, Russia did not follow up on its side of accompanying plans for closer nuclear energy cooperation. Russia's continued pursuit of bypass pipelines placed Ukraine in a disadvantageous position. Moreover, other post-Soviet examples of economic, and energy, integration with Russia, particularly pertaining to Belarus, demonstrated how energy integration with Russia could erode economic independence. Therefore, while April 2010 appeared as a high point in Russian–Ukrainian bilateral relations, it was followed by further erosion of trust in Russia's intentions amongst the Ukrainian elite (Moshes, 2013; Samokhvalov, 2015, pp.1379–1380). Energy played a part in the immediate run-up to Euromaidan in November 2013, when Putin offered the Ukrainian President Viktor Yanukovych a substantial package of economic incentives, including 15 US$ billion in economic aid, reduced gas prices and continued cooperation in the nuclear sector, in return for pausing Ukraine's integration with the EU and not signing the Association Agreement. Similar pressure had been employed in September, when Serzh Sargsyan, the Armenian president, called off the signing of Armenia's Association Agreement with the EU and embarked on accession to the Customs Union, and later the Eurasian Union (Ter-Matevosian et al., 2017). But in the Ukrainian case, popular protests followed, and they were met with violence. In late February 2014, Yanukovych departed from Ukraine and was subsequently removed from office. Russia's reaction, covert military intervention and illegal annexation of Crimea, provided yet another confirmation of post-Soviet elites' worst fears as to how Russia viewed its role in the region. To other post-Soviet capitals, Crimea and then Donbas demonstrated that the war in Georgia was not a one-off. To the contrary, Russia had shown itself willing to use military means to assert regional hegemony.

This was a watershed for the post-Soviet region. Russia now met with far lower levels of trust among its neighbours (Guedes Vieira, 2016), alienating even the potentially more Russia-friendly "inner circle" of EEU partners.

Ukraine's rejection of integration with Russia was comprehensive, and the ties that continued to exist were much reduced. Selective regional integration continued within the Eurasian Economic Space and then the EEU. But Belarus, Kazakhstan and Kyrgyzstan took balancing precautions (Kudaibergenova, 2016; Nurgaliyeva, 2016) and opposed Russia's aim to use integration in the EEU as a precursor to political integration (Smith, 2016, p.180). Russia's own policies were also a brake on EEU integration, for example, by continuing to postpone the introduction of a single market for oil, gas and petrochemicals in the EEU. Energy relations continued to matter within existing bilateral frameworks. During Russia's economic crisis in 2015–2017, Russian companies found it more difficult to deliver on their investment promises and scaled down their presence across the post-Soviet region. Russia became less important to regional economies, especially in Central Asia. A major company like RusHydro stalled the Kambarata and Naryn hydropower plants in Kyrgyzstan, both important projects. Its agreements with the Kyrgyz government were nullified in 2016. The same year, Gazprom terminated its gas relationship with Turkmenistan, due to a fall in European gas demand. In Armenia, household tariff increases spurred the "Electric Yerevan" protests in summer 2015, leading to Inter RAO's exit from the country. The protests raised the question of how EEU membership benefited ordinary Armenians. When more political protests led to a peaceful change of government in April 2018, Russia's role was reduced to that of an onlooker. Russia's declining economic power in the post-Soviet region exposed its lack of broader engagement with post-Soviet societies (cf. Just, 2016).

Sanctions

The annexation of Crimea and war in Donbas caused the greatest setback for Russian foreign policy after 2000. European states and the US jointly isolated Russia, and its international prestige was considerably reduced also among non-western states (Rutland and Kazantsev, 2016, p.409). Before March 2014, Putin regularly met with Western leaders, both bilaterally and in multilateral settings like the Group of Eight (G8). After the annexation of Crimea, the level of contact was markedly reduced. Russia was suspended from the G8, with the 2014 summit in Russia replaced by a scaled down G7 meeting in Brussels.

This change in Russia's international position was accompanied by concerted economic sanctions. They targeted the energy industries, in particular investment and prospects for development. The first and second rounds of European, US and Canadian sanctions, imposed in March and April 2014, restricted the possibilities of a number of individuals, including Gennadiy Timchenko and Igor Sechin from the energy sector, to visit the US and Europe and hold accounts there. The third round of sanctions imposed from July 2014 had wider implications. Financial measures against several companies curtailed access to long-term financing in European and US financial markets. The sectoral sanctions affected all oil and gas companies' access to equipment and technology for development of deep water and Arctic offshore oil fields, and unconventional shale oil formations.

The sanctions had considerable effects. As global companies, banks, and financial markets rigorously assessed them and potential consequences of breaches, costs mounted, and some decisions inevitably went in favour of staying out altogether. The prospects of further sanctions, and the intentionally vague formulations of the US sanctions, heightened the sense of risk attached to transactions and investment connected to Russian companies. In addition, Russia's rating with international agencies slipped below investment grade. In a risk-averse period for international financial markets, this amounted to a quasi-closure of global finance to Russia.

Conclusion

In the initial period after the break-up of the Soviet Union, integration with the global economy was an important foreign policy aim. As this became less central, economic relations were increasingly perceived as instruments of Russian foreign policy, especially in relations with the other post-Soviet states. From around 2003, Russia aimed to return to great power status through its position as regional energy supplier, using relations with post-Soviet states in support of its ambitions. This was possible as long as market conditions were relatively stable. It was more difficult when changing markets began to constrain the possibilities to project energy power. As external reactions mattered relatively little in Russian foreign energy policy formation, Russia was less inclined to respond to such rapid changes in international markets and changing policies among its customers.

Russia's approach to power projection made a difference to its possibilities of becoming a great energy power. The 2003 Energy Strategy linked Russia's policy towards post-Soviet states more closely to relations with other energy markets. Trust in Russia as a supplier would demand that it maintain a strategic, more consistent approach to energy relationships. This was at variance with Russia's use of post-Soviet energy relations as tools of coercion. A consistent policy towards all energy customers demanded that Russia compromise on its aim of creating and dominating a regional bloc in the post-Soviet space. As the difficulties associated with integration into the global economy increased, opting for post-Soviet integration appeared to be the easier route for Russia as a great power. The latter years under study in this book show how Russia's foreign economic policy has failed to resolve the tension between two views of Russian power in the world. On the one hand, post-Soviet economic integration remained attractive because it came with a promise of making Russia a regional great power. On the other hand, Russia could project power in global energy markets in a beneficial way, if it restrained its regional power projection. Energy power and regional power, which seemed to be so closely related in the early 2000s, turned out to be irreconcilable aims for Russian foreign policy.

Notes

1 First government December 1992 to August 1996, second government August 1996 to March 1998.
2 As discussed in some detail in the cited report, there are some deficiencies in the data used for these calculations (Freinkman et al., 2004, pp.1–5). The unavailability of consistent price data is particularly relevant to the discussion here.
3 Due to deficiencies in trade reporting, it is generally difficult to estimate the exact value and volume of foreign trade flows among CIS member states in the period from 1992 to 1996. The UN Comtrade Database contains data from 1996 onwards. Deficient reporting and very high inflation in some states make it difficult to estimate precise values for CIS energy trade before 1996 (Belkindas and Dikhanov, 1994). For energy, widespread barter payment complicates the picture further. On this background, this chapter does not include calculations for Russia's share in energy imports for other CIS states.
4 Author's calculation based on data from the UN Comtrade Database. Energy exports calculated on the basis of export flows from Russia as reported by Russia to Armenia, Azerbaijan, Belarus, Georgia, Estonia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Tajikistan, Turkmenistan, Ukraine and Uzbekistan of goods reported under the commodity codes 2709 Petroleum oils, oils from bituminous minerals, crude; 2710 Oils petroleum, bituminous, distillates, except crude; 271121 Natural gas in gaseous state; 2716 Electrical energy; 8401 Nuclear reactors, fuel elements, isotope separators. Calculations in US$.
5 Foreign minister January 1996 to September 1998, prime minister September 1998–May 1999.
6 Acting president 31 December 1999 to March 2000, president 2000–2008 and 2012–.
7 Defence Minister March 2001 to February 2007.
8 At its peak in September 2008, the Reserve Fund held 142.6 billion US$, while the National Welfare Fund exceeded 80 billion US$ in 2009. The Reserve Fund was established to offset future shortfalls in oil revenue. Having been used to cover deficits during the 2015–2017 economic crisis, the Fund was depleted by the end of 2017. In January 2018, what remained was merged with the National Welfare Fund. This Fund had been designed to cover national pensions in the mid-term. This did not prevent the government from resorting to the National Welfare Fund to meet income shortfalls.
9 Early proposals were for a pipeline through Turkey, Bulgaria, Romania and Hungary to the gas hub at Baumgarten in Austria. A later proposal, Nabucco West, included only the part from Bulgaria's border with Turkey to Baumgarten.
10 Across the Black Sea to Bulgaria, Serbia, and Hungary to Baumgarten and Slovenia, with a second leg to Greece and Italy.

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