Geopolitics of Energy®

Volume 38, Issue 7
July 2016

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State capitalism refers to the situation where the means of production for the whole economy or an economic sector are organized and managed as state-owned business enterprises. This paper provides evidence that Gazprom is a constituent part of Russian energy policy and as such it reflects the perception of energy resources as a foreign policy tool. This paper also provides evidence that Gazprom's current policy is still targeted at foreign markets aiming to influence routes or foreign reserves, mainly in the Former Soviet Union, thus allowing a decrease in Gazprom's market share in domestic markets. The current leadership role of Gazprom enables further strengthening of its global position, but this can only be implemented by radical re-adjustment of its policy to the actual market dynamics of global gas markets.

Geopolitics of Energy was founded by the late Melvin A. Conant of Washington, DC in 1979.
Since 1993, it has been published under the auspices of the Canadian Energy Research Institute.

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Gazprom's Strategy: Natural Resource as a Foreign Policy Tool

Athanasios Dagoumas and Michael Charokopos

Introduction

In a recent paper, Bremmer (Bremmer, 2009) identifies four waves in the historical evolution of state capitalism. The point of departure (first wave) is the 1973 oil crisis, which generated the model of modern national oil corporations, applied to the natural gas sector as well. The second wave appears during the 1980s and continues during the next decade when a number of developing countries achieved rapid growth. The governments of several emerging markets were driven by 'state-centric values and traditions' which allowed only partial market liberalization leaving certain economic sectors under government control. The third wave of state capitalism is related to the rise of Sovereign Wealth Funds (SWFs) generated by the export increase and the trade surplus of emerging markets. Lastly, the recent global economic downturn has bred a fourth wave of state capitalism, where not only the governments of developing countries intervene in their economies but also those of free market economies including the United States, Japan, Australia and European countries.

In light of this conceptual framework, we seek to provide evidence that Gazprom over the Putin administration is an active example of state capitalism. Gazprom is a constituent part of Russian energy policy and as such it reflects the perception of energy resources as a foreign policy tool, which was intensified after President Putin's ascent to power. The energy sector played a key role from the beginning of the Putin era, since it lay at the core of the Kremlin's ambition to restore Russia's influence, at least, in the Former Soviet Union. To recapitulate, we argue that state capitalism permeates the Russian natural gas industry. Considering the record of Russian energy power projection in the country's regional influence, it becomes apparent that natural gas exports emerged as one of the most powerful assets of Russian foreign policy during the Putin era.

However, Gazprom is facing new challenges in the domestic, regional and global gas market. While Gazprom's market share in the domestic market is weakened due to competition from non-Gazprom Producers (NGPs) (Henderson & Pirani, 2013), the greatest challenge to the Russian gas market has emerged from the profusion of gas suppliers and export options, at the international level, providing large volumes of gas at competitive prices. The low level of oil prices is arguably contesting the viability of the new liquefied natural gas (LNG) projects. However, it constitutes a menace to Russia's oil and gas industries as well, as long as the oil price remains lower from the fiscal break-even point of the Russian economy. At the same time, in the European market, Gazprom is facing challenges related to the reputational impact of Russia's dispute with Ukraine, the considerable decrease in gas demand and the EU regulatory framework (Johnston and Stromquist, 2014). Moreover, the European Commission opened in 2012 formal proceedings to investigate suspected dominant market position abuses by Gazprom in breach of EU antitrust rules. Although Gazprom seems to welcome a mutually satisfactory solution on the issue of gas pricing, the investigation is still underway.

The question that arises is whether such a business model could be sustainable for Gazprom, as despite the challenging international milieu, there does not seem to be any major change in the model of the Russian natural gas policy. In light of this conceptual framework and international market environment, we seek to provide evidence that Gazprom is still used as a foreign policy tool. The next section provides official data on the market shares of Gazprom and the strategy of the company, judging the information in the context of using natural resources as a foreign policy tool.

Gazprom Strategy

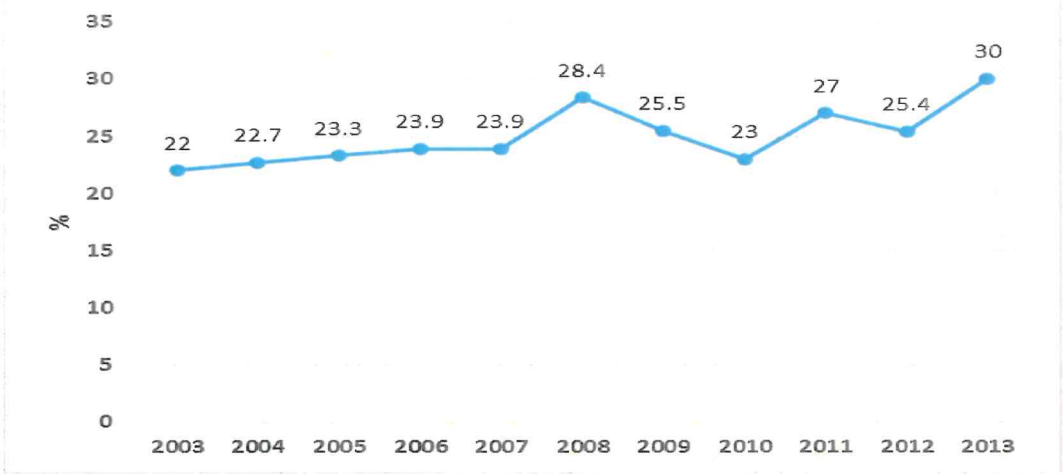
Global leader in gas market

Gazprom, according to the Gazprom Annual Report 2014 (Gazprom, 2015), is a global leader in natural gas reserves and gas production, having shares equal to 17% and 12% in global gas reserves and production, respectively. It's the dominant gas company within the Russian Federation, as it has 72% of national gas reserves and 69% of national gas production. The major field is in the Urals Okrug, while a number of other smaller fields exist in the Western part of Russia, close to Europe. The exploitation of those fields required the development of a number of critical gas pipelines. Gazprom has the largest gas transportation system, 171,000 km of Gazprom's trunk pipelines in Russia, while it owns a well-developed network of 26 Underground Storage Facilities (UGSFs) in Russia and has access

to foreign UGSFs. Moreover, Gazprom over the last year has diversified its core business, in addition to its gas business. Therefore, it's operating in oil and power markets, ranking among Russia's top 5 oil companies and is considered the national leader in Russia in power and heat production. More specifically, it has 39 GW of installed power capacity at 85 power stations in Russia, providing 15% of total Russian electricity generation and 24% of Russian heat energy.

Concerning its market activity, based on the same report, Gazprom is the major supplier to consumers in Russia and FSU countries, the largest gas exporter to the European market, providing 30.2% of European gas consumption in 2014. Figure 1 provides the percent share of Gazprom's overall gas imports in Western Europe over the period 2003-2013, showing that Gazprom, besides the several Russia-Ukraine gas disputes over the last decade, kept an important share in the European gas market. Moreover, it is a relatively small player in the global Liquefied Natural Gas (LNG) trade, entering the global market in 2005 when Gazprom's first LNG shipment to a US regasification terminal and entering the promising Asia-Pacific gas market in 2009 when the Russian's first LNG plant was put into operation.

Figure 1: Gazprom's Share in Overall Gas Imports in Western Europe



Source: Gazprom Annual Report 2014

Gazprom Strategic Target Indicators

Gazprom's strategy is to remain a global leader in the gas market. The Board of Directors in 2014 approved the Long-term Development Programme, which incorporates some Strategic Target Indicators (STIs), as reported in the same Gazprom Annual Report 2014:

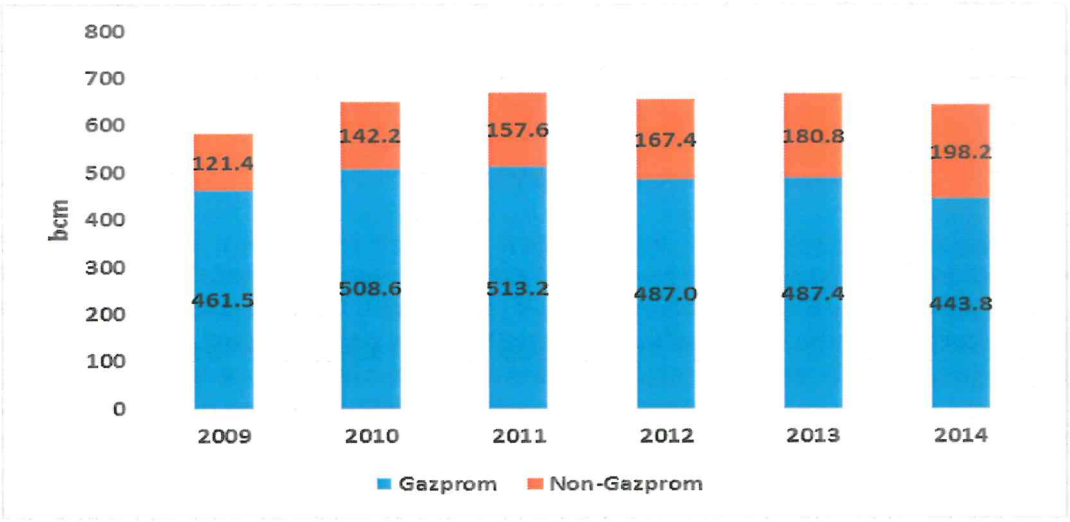
- Return of capital, at least 6%: It was 7.5% and 2% in 2013 and 2014, respectively.
- Debt/equity ratio, not more than 40%: It was 19.1% and 23.4% in 2013 and 2014, respectively.
- Gross production of natural gas, not less than 550 bcm: It was 487 and 444 bcm in 2013 and 2014, respectively
- Sales of natural gas, not less than 490 bcm: It was 462 and 425 bcm in 2013 and 2014, respectively
- Total gas reserves, not less than 29 tcm of natural gas: It has 23.49 tcm of gas and 0.85 tcm of proved and probable gas condensates at 31 December 2014, according to DeGoyer and MacNaughton, as reported in the Gazprom Annual Report 2014. Furthermore, there are 0.023 tcm of gas reserves attributed to Gazprom in investments classified as joint operations.
- Gas reserve replacement ratio, not less than 100%: In 2014, the PRMS reserves increased compared to 2013, due to an audit of reserves at the Khandinsky block of the Kovyktinskoye field and exploration performed at the Chayandinskoye and Semakovskoye fields and Gazprom's neft Group's fields in Eastern Siberia.

Those targets are in accordance with previous Board decisions, as reported in previous Annual Reports and can be accessed on the Gazprom website. From the above data, it can be easily taken out it has violated its profit target in year 2014, as it was 2% far less than 6%, attributed mainly to low oil prices and therefore the low gas prices, due to their price formula correlation. This is

expected to worsen in 2015 and to become even negative, due to the persistent low oil prices. Moreover, Gazprom decreased profits is attributed to the loss in its gas sales, from 462 bcm in 2013 to 425 bcm in 2014, being in both years below its 490 bcm target. A similar 9% decrease can be shown in the performance of Gazprom in gas production. More specifically, in 2014 Gazprom lacks by about 19% its 550 bcm gas production target, while it lacks by about 13% its gas sales target. Similar growth pattern can be derived concerning gas reserves, as Gazprom is lacking its 29 tcm target by about 16%. However, over the last year it has developed its gas replacement ratio, as mentioned above, which means it has increased its gas reserves.

The decrease of Gazprom production over the last years, as can been seen in Figure 2, is also explained from the increasing competition within the Russia Federation. Figure 2 also shows that companies outside the Gazprom Group, also of Russian interest for the majority of them, have increased significantly their production in years 2009-2014, leading to an increase in Russia's gas production over the same period. Combining the facts that Gazprom has increased its share in European countries over the last years and that Russian internal demand is almost stable during years 2010-2014, means that Gazprom is losing share in the internal market, towards supporting its global leadership role. This conclusion enhances the argument that Gazprom is the preferred company for Russia for forming its foreign policy.

Figure 2: Russia's Gas Production, 2009-2014



Source: Gazprom Annual Report 2014

Although the assessment of Gazprom's performance on the above mentioned indicators seems to be negative, this is not the case. The Board of Directors has set ambitious targets for the majority of its Strategic Target Indicators, as this is the role of any decision maker, namely to provide a strategy based on the current situation. Practically, Gazprom is close to its volume targets, lacking about 15%, and is able to track on implementing them as it has a considerable range to lend money in order to finance its gas developments. This derives from the fact that its debt/equity ratio is far more than the 40% target, although it was 23.5% in 2014, an increase of 4.3% compared to 2013.

Gazprom Strategy on Gas Transportation

In order to achieve those targets, Gazprom plans to achieve strategic milestones in all its activities: in gas production, through the development of new gas production centers in Yamal Peninsula in Eastern Siberia, in gas transportation, through the development of critical infrastructure projects, providing alternative routes for supplying gas, mainly to the West but as well as to the East following the 30-year gas supply contract signed in 2014 with China CNPC for over 1 tcm, and unifying the Gas Supply System. Finally, Gazprom aims to increase its limited share in LNG at the levels of 10-15% in the longer term, concerning the Northeast Asia markets. Europe remains the most important market for Gazprom and Russia and therefore the development of critical projects, such as the Nord Stream II and the TurkStream. Those projects are considered as priority projects for Gazprom, together with the existing Yamal-Europe, Blue Stream and the Nord Stream I projects, the existing Sakhalin-2 integrated oil and

LNG project in East Russia and the planned Power of Siberia gas transmission system which will provide access to China for the Russian gas.

Towards the West, there are two major new projects: Nord Stream II, TurkStream, as well as its extension to Europe.

Concerning the Nord Stream II: On June 18, 2015 Gazprom, E.ON, Shell and OMV signed the Memorandum of Intent stipulating the joint construction of two strings of the Nord Stream II gas pipeline with an aggregate annual capacity of 55 billion cubic meters of gas from Russia to Germany across the Baltic Sea.[1]

Concerning the TurkStream: On December 1, 2014, during the state visit of Russian President Vladimir Putin to Ankara, Gazprom and Turkish company Botaş Petroleum Pipeline Corporation signed the Memorandum of Understanding on the construction of an offshore gas pipeline from Russia to Turkey across the Black Sea, while on June 22, 2015, Turkey issued a permit on engineering surveys for the offshore section of TurkStream.[2] The TurkStream has replaced the South Stream project, but in a Press statement following Russian-Hungarian talks and answers to journalists' questions in February 2015,[3] President Putin stated "If we are not hindered, we could build part of the former South Stream via Turkey". Some months later, on June 18, 2015,[4] the Minister of Energy of Russia, Alexander Novak and the Minister of Productive Reconstruction, Environment and Energy of Greece, Panagiotis Lafazanis signed a Memorandum of Cooperation on the construction and operation of the TurkStream pipeline on the territory of Greece. This can be part of a reformed South Stream project, as Greece, FYROM, Serbia and Croatia have applied to include the national branches of the Tesla gas project in the selection list of the Project of Common Interest (PCIs).[5] Those branches, in contradiction to earlier bilateral intergovernmental agreements between Russia and the South Stream participating countries, will be in accordance with the European Union's Third Energy Package. Therefore, concerning the European strategy for Gazprom, there seems to be "inside" competition between the Nord Stream II project, which is the favorite project for the time being, and the extension of the TurkStream, which will possibly be the Tesla project.

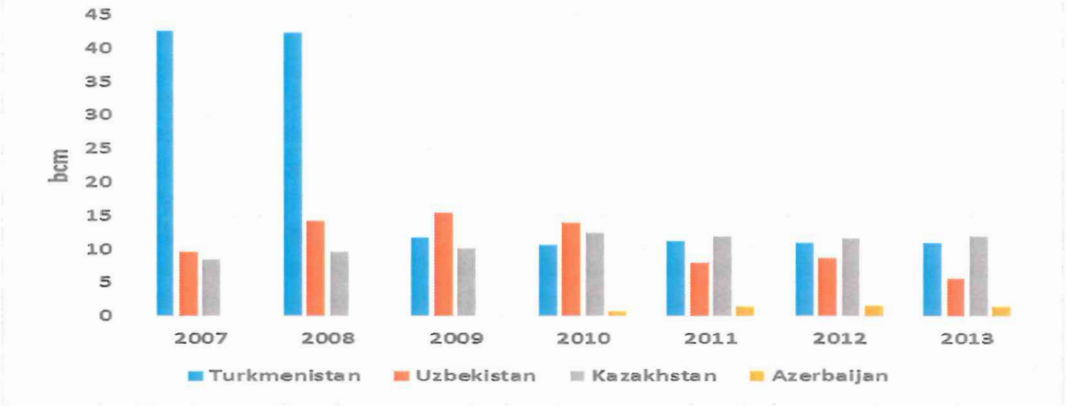
Gazprom Strategy in Former Soviet Union Countries

Part of Gazprom's historic strategy was to exploit natural gas from Central Asia countries. Natural gas supply via the Central Asia – Center (CAC) gas pipeline system, initiated in 1967, still remains a crucial component in Gazprom's comprehensive resource base to meet gas demand on the domestic market, in CIS and Europe. This gas pipeline runs about 5,000 kilometers and runs via Turkmenistan, Uzbekistan, Kazakhstan and Russia. Those countries have entered into a number of agreements regulating natural gas purchase and transit across Russia. On April 10, 2003 Russia and Turkmenistan entered into a 25-year Agreement of Cooperation in the gas industry. Under the Agreement, Gazprom and Turkmenneftegaz gas transmission company concluded a long-term contract to purchase and sell Turkmen natural gas throughout the period of the Agreement.[6]

A very important aspect in Gazprom and Russian energy policy was to contract significant volumes from the region even with unfavourable prices, aiming at eliminating the chance considerable volumes in the Central Asia region to be exploited by competitive companies. As part of this strategy, the head of Russian, Kazakhstan and Turkmenistan states signed in 2007 the Joint Declaration to build the Pre-Caspian gas pipeline, due to the CAC capacity reduction after many years of operation. The volume of gas transported by the Pre-Caspian gas pipeline is estimated to be: up to 10 bcmpa from Turkmenistan and up to 10 bcmpa from Kazakhstan. Figure 3 shows the natural gas purchased by Gazprom Group in Central Asia from 2007 through 2013, in billion cubic meters. It is obvious that Gazprom is buying significant volumes from those three countries, although purchases from Turkmenistan were at much higher levels until 2008. The reduced demand, due to the 2008 economic crisis, the Ukrainian 2009 crisis and the delay in the construction of the Pre-Caspian gas pipeline eliminates the capacity of volumes purchased by Gazprom. Moreover, Gazprom's cooperation with Azerbaijan is very limited, as it is unanimously considered as a pro-western state. This Russian strategy has led to the fact that only Azerbaijani gas has proved to be available for export to Europe. Therefore, the ambitious Nabucco project has

been withdrawn, due to lack of adequate quantities, leaving its space to the much smaller project of Trans-Adriatic Pipeline (TAP)[7] to transport the alternative – to Russian-gas to Europe.

Figure 3: Natural Gas Purchased by Gazprom Group in Central Asia, 2007-2013



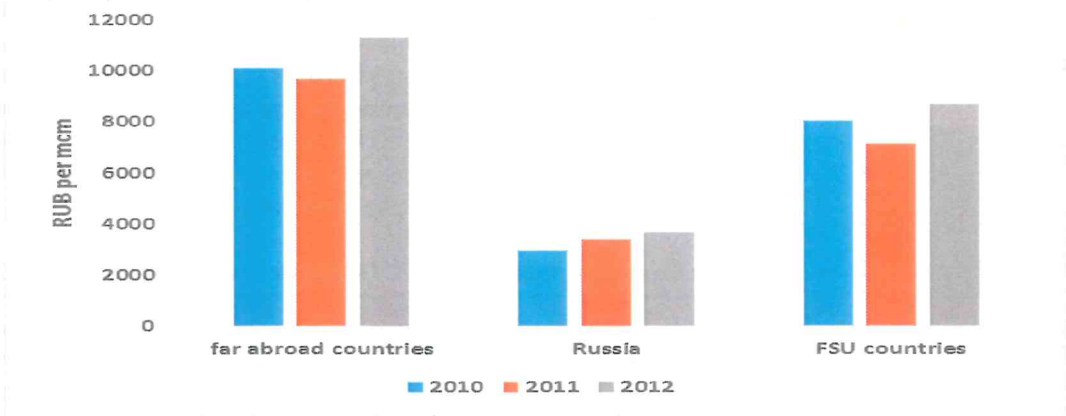
Source: Gazprom Annual Report 2014

Gazprom Strategy in European Union Countries

Figures 4 and 5 show the Gazprom's Group sales of natural gas to far abroad countries, to the Russian market and to the Former Soviet Union countries respectively, over the period 2010-2012. Figures 4 and 5 also depict the significant different pricing policy between those regions. Prices for domestic customers are less than 25% of the prices in the European countries. Prices for the Former Soviet Union countries are about 70% of the prices in the far abroad countries. Although, some of the above differences can be attributed to the different allocation of the transmission and storage costs from Gazprom to the final destinations, it is not clear that the criteria that Russia, through Gazprom, applies pricing formulas to different countries are only based on market dynamics. This has led the European Commission's investigation of Gazprom policy.[8] The European Commission's preliminary view is that Gazprom is breaking EU antitrust rules by pursuing an overall strategy to partition Central and Eastern European gas markets with the aim of maintaining an unfair pricing policy in several Member States. Gazprom implements this strategy by: (i) hindering cross-border gas sales, (ii) charging unfair prices, and (iii) making gas supplies conditional on obtaining unrelated commitments from wholesalers concerning gas transport infrastructure.

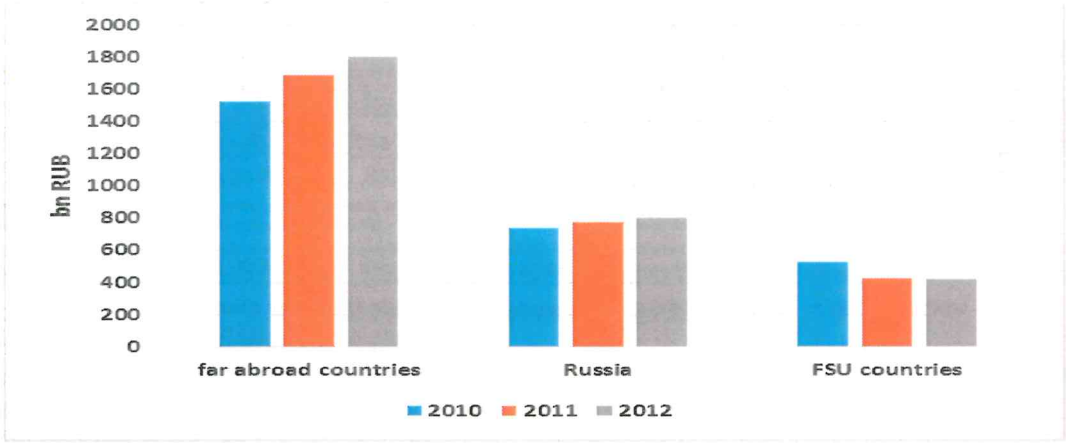
The Commission has concerns that Gazprom leveraged its market dominance in some Member States, namely Bulgaria and Poland, by making gas supplies conditional upon obtaining certain infrastructure-related commitments from wholesalers. Considering that the European Union is targeting to a fully competitive European market, requiring ownership unbundling between producer and transmission, as well as allowing third-party access to other gas market participants, the European Commission is working towards alleviating its concerns over Gazprom concerning the abuse of its dominant market position. Those concerns are in accordance to the conclusions of a paper on Gazprom's policy in CIS countries (K. Svoboda, 2014), stating that "By controlling pipeline routes and junctures, Gazprom has a huge influence on Russia's foreign policy".

Figure 4: Gazprom Group's Average Selling Price (net of customs duties): To Far Abroad Countries, Russia and FSU Countries, 2010-2012



Source: Gazprom Annual Report 2014

Figure 5: Gazprom's Group's Sales Revenues (net of customs duties): To Far Abroad Countries, Russia and FSU countries, 2010-2012



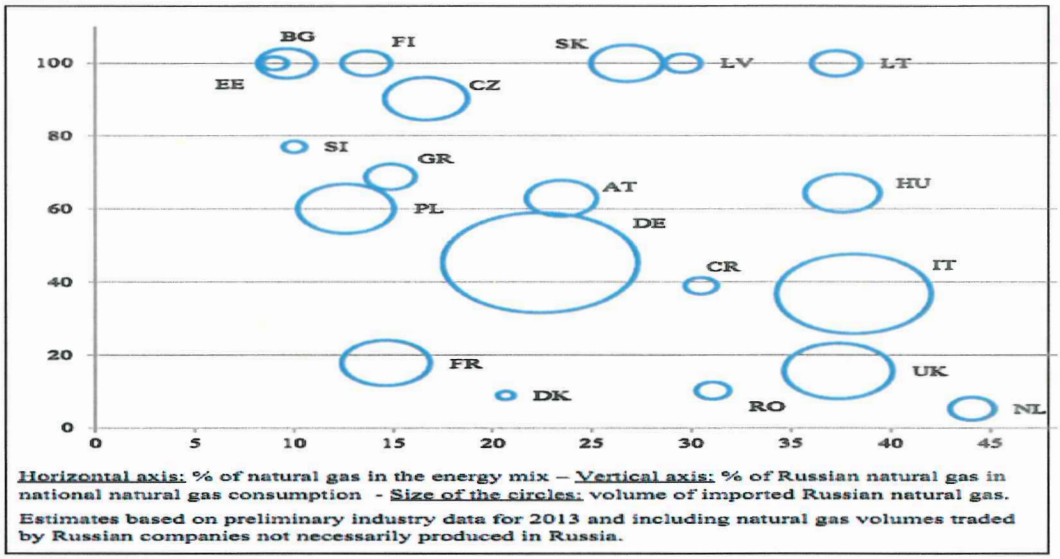
Source: Gazprom Annual Report 2014

Moreover, it derives that the share of Gazprom in the domestic market has been decreased, as it is facing internal competition and is not a core priority. At the same time, sales to far abroad countries have been decreased, with the exception of Turkey. Sales in the Former Soviet Union have decreased significantly, which is attributed to the sharp decrease in Ukrainian consumption due to the 2014 crisis. The Ukrainian crisis revealed a strong willingness to reduce energy dependence from Russia but as well as Ukraine as a transit country. It has revealed the importance of Energy Security for the European Union (EU), as well as the need for an Energy Union. A recent report examines how the EU can diversify its energy supply to improve its Energy Security (Leal-Arcas et.al, 2015). The European Commission has conducted an in depth study of the European Energy Security (European Commission, 2014a), accompanying its Communication on European Energy Security Strategy (European Commission, 2014b). The key facts of those studies are that the EU imports 53% of the energy it consumes. Energy import dependency relates to crude oil (almost 90%), to natural gas (66%), and to a lesser extent to solid fuels (42%) as well as nuclear fuel (40%). Energy security of supply concerns every Member State even if some are more vulnerable than others, in particular the less integrated and connected regions. The diversification of routes and resources, as well as the enhancement of indigenous energy resources are the main policies for tackling energy security. The implementation of those projects is however a complex issue that incorporates techno-economic but as well as geopolitical parameters (Floros and Dagoumas, 2016).

Energy Security as a Priority Policy for the EU

The most pressing energy security of supply issue is the strong dependence from a single external supplier. Figure 6 presents the natural gas dependency of each EU Member State from Russia. In order to assess the effect of gas disruption on the EU, the European Commission has published a Communication on the short term resilience of the European gas system – preparedness for a possible disruption of supplies from the East during the fall and winter of 2014/2015 (European Commission, 2014c). This communication examines the effect of a 6-month gas disruption from Russia in each of the EU Member States, where it is obvious that specific regions in the EU, such as the Baltics, Eastern Europe and Balkan area are vulnerable to an energy crisis.

Figure 6: Gas Dependency of Each EU Member State from Russia

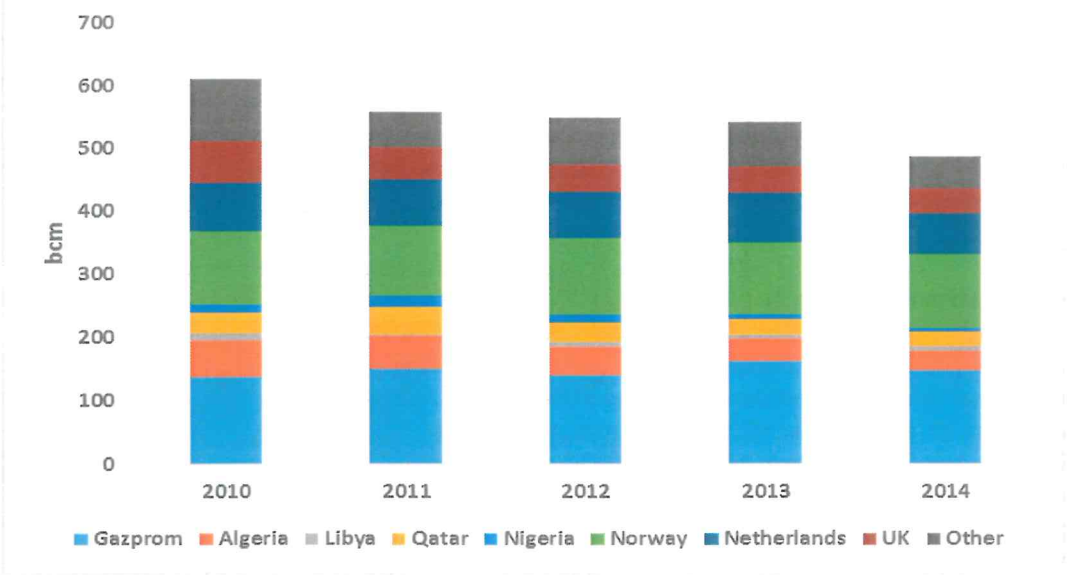


Source: European Commission COM/2014/330

The European Commission is tackling energy security and creating an integrated EU energy market, resulting in a list of 248 Projects of Common Interest (PCIs). The majority of gas projects concern South and Eastern Europe, towards tackling the lack of diversification of routes and resources. The Project of Common Interest may benefit from accelerated licensing procedures, improved regulatory conditions, and access to financial support totalling €5.85 billion from the Connecting Europe Facility (CEF) between 2014 and 2020.

The willingness for reducing energy dependence from Russia is very clear for the Baltic States, based on the fact that a strategic contract was signed between the Lithuanian natural gas supplier and trader LITGAS and Norwegian Statoil for supplying LNG at an annual volume of 540 million cubic meters, starting in 2015.[9] The first LNG cargo is expected to be delivered to the Lithuanian Klaipėda terminal at the end of December 2014 so that the terminal could start commercial operation from the 1st of January 2015. The pricing formula is de-linked from oil products as those contracts provided by Gazprom, but is linked to the value of the NBP index, the Great Britain natural gas exchange. This might upset Gazprom's leading role in Europe, as Norway – through Statoil – is in a position to challenge Gazprom. Figure 7 shows that besides the significant decrease of domestic production in European far abroad countries, Norway has slightly increased its production over the period 2010-2014, increasing its share. This trend is expected to continue as Statoil prefers hub-based pricing, which enables adjustment to market dynamics (J. Stern, 2011; J. Stern and H. Rogers, 2013).

Figure 7: Natural Gas Supplies to Europe, 2010-2014



Source: Gazprom Annual Report 2014

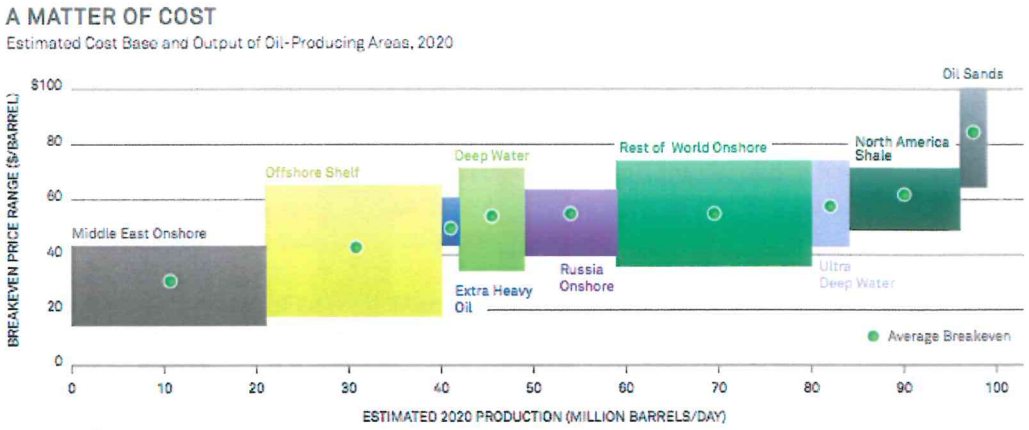
The Influence of Low Oil Prices

Oil prices crashed in the second half of 2014, with Brent and Urals losing about 50% of its selling price. The oil price remains at the same low level of $45 US/barrel for 2015. According to the Gazprom Annual Report 2014, as well as a recent report from BlackRock,[10] the decrease is attributed to:

- The deceleration of the oil consumption growth caused by the economic downturn in China, which was the main driving force behind the oil consumption growth in recent years.
- Soft demand and strong US dollar.
- Cheap energy is a game changer for monetary policy in oil-importing nations, as shown from the recent initiative by China.
- Increased oil production, due to the shale oil projects, and reduced oil and petroleum products by the USA.
- Growth of oil production in Iraq and Libya with other OPEC countries' output remaining flat.
- Saudi Arabia's reluctance to cut production to keep oil prices high.

In the medium-term, there are no signals that oil prices will increase. This is attributed to the insistence by Saudi Arabia to keep oil production high. The persistent low oil price is expected to deteriorate the financial situation of many companies, such as Gazprom. Even a radical change towards hub-based pricing is not expected to provide significant gains in the short-term, as there seems to be available a lot of cheap oil and gas, as shown in Figure 8.

Figure 8: Breakeven Price Range for Different Oil Fields in 2020



Sources: BlackRock Investment Institute and Rystad Energy, January 2015. Notes: The boxes represent different oil sources. The width of each box shows the level of potential production in 2020; the height shows the breakeven range for 75% of the production from that source. Dots show the average breakeven prices. The breakeven price is the oil price that gives a zero net present value using a 10% discount rate. Numbers are based on an average of currently producing, under development and not yet sanctioned projects.

Source: BlackRock

Over the last years, the global gas market has faced unprecedented growth in gas production in North America due to shale gas. The increased gas production has led to a self-dependence for the US, therefore no need for gas imports and a sharp decrease in gas prices in the US, in the Henry Hub exchange. This has affected the European and Asian hubs indirectly, meaning that the shale gas was not traded to those markets but led to oversupply of gas due to the decrease of a need for imports to North America. Exports from North America are expected in 2016, which is expected to create further pressure on gas prices in Europe. In combination, this downward pressure is enhanced by discoveries in Israel and Egypt that will enter the market in the coming years. Gazprom has a very small share in the global LNG market, less than 1%, although its LNG production has increased over the last years.

Concerning shale gas, its development in Russia is currently of little interest for Gazprom, since its conventional gas reserves-to-production is over 80 years with current production and consumption rates. Considering that the cost for unconventional natural gas resources production (shale gas, tight gas, coalbed methane) is generally much higher than for conventional fields, Gazprom does not intend to invest in their development in the medium-term, although Russia might be rich in geological and technically recoverable unconventional resources.

Discussion on the Gazprom Strategy

The above analysis presented the Gazprom strategy, towards maintaining its global leadership in the gas market. Some key elements to the Gazprom strategy include:

- priority in foreign sales, leaving domestic space to internal competitors
- preference on long-term contracts instead of hub-based pricing,
- preference on pricing formula based on petroleum products,
- ambitious targets for gas production, sales and reserve developments
- transmission developments in Central Asia towards long-term contractual agreements of local reserves, for eliminating the control of reserves in Central Asia from competitive schemes, with Azerbaijan as the only exception,
- creating new markets (e.g., deal with China in 2014),
- delay in showing flexibility in European Commission requirements over the Third Energy Package,
- participation in global LNG market, aiming at obtaining a small share in North-Asia markets in the long-term, and
- no interest in unconventional gas.

In this strategy, Gazprom has managed to enhance its role as a global leader in gas markets. However, some major events/facts are challenging its dominant role:

- The several Russia-Ukraine disputes over the last years have facilitated the willingness of several European countries to reduce energy dependency from Russia.
- The unprecedented growth in oil and gas production in North America, due to the shale gas and oil revolution, leading to considerably cheap energy in the USA as well as reduced oil and petroleum products imports by the USA.
- The discovery of several new off-shore fields, providing alternative LNG supplies.
- the economic downturn in China, leading to reduction in energy demand growth, while cheap energy is also a game changer for monetary policy in oil-importing nations, as shown from the recent initiative by China.
- Saudi Arabia's reluctance to cut production to keep oil prices high.
- Ending of Iran sanctions will provide considerable volumes of oil and gas in the market.

Conclusions

The above conditions challenge the profitability of Gazprom and therefore its capability to finance critical infrastructure and gas production projects, although it has a relatively low debt/capital ratio. However, even more important for Gazprom long-term profitability and role is its radical re-adjustment of its policy to the actual market dynamics of global gas markets. This conclusion is in accordance with a recent paper (Henderson, 2016) which discusses the competitive position of Russian gas in a new lower price environment and examines whether a more actively competitive strategy can benefit both Gazprom and the Russian government in the short- and long-term.

This paper provides evidence that Gazprom is a constituent part of Russian energy policy and as such it reflects the perception of energy resources as a foreign policy tool. This policy is further enhanced over the Putin administration. Russia insists on this policy although Gazprom is facing a great challenge from the emergence of gas suppliers in international markets, providing large volumes of gas at competitive prices. This paper provides evidence that Gazprom's current policy is still targeted at foreign markets with the aim to influence routes or foreign reserves, mainly in the Former Soviet Union. The focus on foreign markets leads to a decrease in Gazprom's market share in the domestic market, due to competition from non-Gazprom Producers (NGP).

This policy has proved to be effective for Russian and Gazprom's interests over the last decades, providing political and financial gains for Russia. However, some major events/facts are acting against Russian interests over its political control in Former Soviet Union states, requiring Russia to re-adjust its foreign and energy policy. At the same time, in the European market Gazprom is facing challenges related to the reputational impact of Russia's dispute with Ukraine, the considerable decrease in gas demand and the EU regulatory framework. The dispute also considers Gazprom's preference on long-term contracts instead of hub-based pricing as well as its preference on a pricing formula that is based on petroleum products.

This preference is challenged by low oil prices, affecting the capacity of Gazprom to implement its strategy. It constitutes a menace to Russia's oil and gas industries as well, as long as the oil price remains lower from the fiscal break-even point of the Russian economy. However, the level of low oil prices is arguably contesting the viability of new liquefied natural gas (LNG) projects. Gazprom is at a turning point, where it should show some flexibility in its policy, which is also an internal debate between the market-based approach of the Gazprom Marketing & Trading (GMT) branch in London with the "old-fashioned" approach of the Gazprom headquarters in Russia.

The above conditions challenge the profitability of Gazprom and therefore of its capability to finance critical infrastructure and gas production projects, although it has a relatively low debt/capital ratio. This paper states that the current leadership role of Gazprom enables the further strengthening of its global position, but this can only be implemented by radical re-adjustment of its policy to the actual market dynamics of global gas markets.

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Endnotes

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Publication Date: August 12, 2016

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Publisher: Canadian Energy Research Institute, #150, 3512 - 33 Street NW, Calgary, Alberta, Canada T2L 2A6
Telephone: (403) 220-2370; Fax: (403) 220-9579; Email: mmurphy@ceri.ca.

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