

STRUGGLE FOR THE COMMON EU ENERGY POLICY ON THE EXAMPLE OF THE COMPETITION OF SUPPLY DIVERSIFICATION ROUTES¹

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ABSTRACT

Energy trade between Russia and the European Union is highly securitized. Russia is blamed for using European dependence on Russian supplies in order to reach its political aims. It is argued that the development of common energy policy towards Russia is essential for European energy security. Even though, the solidarity between the states is a basic rule of the European Union membership, which can allow using its combined weight in the world affairs, but the national interests, competition between the states over access to energy resources and sometimes political disagreement between separate EU members and Russia are still influencing the behavior of the countries within the EU. To investigate this question I choose the example of two competing pipeline projects: European NABUCCO and Russian South Stream. In this paper I will try to answer the question if Russia really tries to use the lack of solidarity between member states to challenge European program of supply diversification and to increase the EU dependence on Russian supplies or not? Structurally the paper is divided into two parts: 1. why the common energy policy is important and why it is difficult to develop it; 2. the case study of the South Stream and NABUCCO pipeline projects and their influence on the supply diversification.

Keywords

Energy Security, Common Energy Policy, NABUCCO, the South Stream

Why the common energy policy is important and why it is difficult to develop it?

Self-sufficiency of the European Union in energy resources consumptions is gradually falling. At the moment, the European Union imports about half of its energy requirements and it will increase up to 80 – 90 per cent. Russia supplies Europe with one-quarter of its gas consumption and 40 per cent of its total import of energy requirements. (Tekin, 2009) And in the nearest future it would be difficult to diversify gas supplies. If oil can be easily transported from all over the world, gas supplies depend on pipelines and are usually imported from geographically close regions. Nowadays, the EU depends on three main energy supply regions, including Russia. In its turn, around 58 per cent of Russian oil exports and 88 per cent of its natural gas were destined to the European Union in 2003. (Haghighi, 2007) In 2003, 65 per cent of Gazprom's revenues were from European sales (European prices are six times those of domestic consumers). (Spanjer, 2007) Moreover, oil and gas together comprise around 15 per cent of Russian overall GDP. (Tekin, 2009)

The necessity of common energy policy development is on the EU energy security agenda due to high dependency on energy sales. It is discussed by the European Union institutions as well as by energy security experts. But what does the common energy policy mean? For instance, Pami Aalto writes about the importance of construction of "energy security society" based on the three main principles: markets and competition, security of supplies, and sustainability. (Aalto, 2010) Aalto also provides the definition of energy security society - "a group of states that have established common rules and institutions for the conduct of their mutual energy relations with a firm interest in maintaining these arrangements". (Aalto, 2010)

This definition sounds logical, considering the high levels of interdependence both sides should be able to develop basic principles of trade on the grounds of mutual trust and partnership. But why in reality energy relations between Russia and the European Union are highly securitized? Ideally this security society is supposed to include not only energy consuming states, but also energy producers and transit states. However, as you can see three main principles include only security of supplies (i.e. interests of energy consumers). The interests of the energy producers are overlooked. It makes this "energy security society" invalid. Energy producing states don't have other choice, but to lobby their interests on the bilateral level undermining the interests of "the society" as whole.

Due to the high levels of securitization and lack of mutual trust between Moscow and Brussels, both sides are developing the ways of supply/demand diversification. For instance, the Second Strategic Energy Review is aimed to draft a plan of

¹ This paper was presented in May 2010 at the RPC Conference at Nottingham Trent University by Olga Khrushcheva

decreasing the dependence of the European Union on the energy imports. 20-20-20 strategy is developed to reduce greenhouse emissions by 20 per cent, to increase the share of the renewable energy by 20 per cent, and to improve energy efficiency by 20 per cent, all of it by 2020. This strategy is orientated to the medium and long-term development, because it requires serious and time consuming changes in the energy system of the European states (including public authorities, energy regulators, infrastructure operators, the energy industry and citizens) to create a diversity of non-fossil fuel supplies, flexible infrastructures and capacities for demand management. The European Union is looking for the ways of its energy supply diversification, for instance, by the development of supply from Caspian and Middle Eastern sources or development of infrastructure for Liquefied Natural Gas (LNG) transportation and usage to and between the Member States. (2nd Strategic Review, 2008)

Gazprom is also concerned with the security of demand and looking for the alternative markets for Russian gas. In 2006 Russia signed an agreement to provide gas to China from Siberia. According to the original plan two new pipelines it has to be constructed by 2011. However, up to the current moment this project still exists only on the paper. The official reason for the delay in the realization of the project is the price disagreement between Beijing and Moscow. (Guangjing, 2010) At the moment the level of gas consumption in China is rather low. Only 4 per cent of Chinese energy comes from gas, the country is still depends a lot on coal. (Economidies, 2010) Even though Chinese leaders admit that they need more gas, they cannot offer the price which can compete with one on the European market. The Gazprom representative I talked to in Moscow commented on it as follows: “Chinese market will never bring as much income as European market does. At the same time the construction of necessary infrastructure is quite expensive enterprise. In the condition of the economic recession it is not profitable project. That is why for the next couple of years this plan is not going to be fulfilled”. (A.R., 2010) Konstantin Simonov, the Director General of National Energy Security Fund agreed that any project for demand diversification by Russia is not economically viable. However, the EU keeps pushing Russia away by the lack of coherence of European energy policy and constant paranoia regarding Russian ambitions to use energy as a political tool. (Simonov, 2010)

Coming back to the discussion on the common energy policy to Russia, I would agree that within the EU member states there is no firm agreement on how to build the energy dialogue with Russia. The former EU Commissioner for Trade Peter Mandelson said once: “The incoherence of European policy towards Russia over much of the last decade has been, frankly, alarming. No other country reveals our differences as does Russia”. (Mandelson, 2008)

This problem exists for many reasons. Among other important ones is the difference in approaching Russia by “old Europe” and new Eastern and Central European member –states. New member states brought to the European Union the flavour of their own historically formed difficulties and contradictions in relations with Russia. Moreover, some of the member states are more dependent on Russian energy supplies than others. (Leal-Arcas, 2009) Andreas Goldthau divided European consumers into two groups on the basis of their dependence levels from Russian energy supplies. The first one is “old” Europe, who are less dependent on Russia and import less than half to no gas from Russia (Germany is the biggest consumer in this group with 46 per cent import share); the second group is so-called “new” European states, which are almost 100 per cent dependent on Russian supplies. For instance, the Baltic Republics or Poland and the Czech Republic are importing around two-thirds of their supplies from Russia. (Goldthau, 2007) That is why the issues of the security of supply are of the key importance for these states.

Considering these differences within the EU, the majority of member states argue that there is “Russian threat” to European energy security, Kremlin use its position of the energy-producer as a foreign policy tool to reach its political goals. The danger is that Russian government may cut the energy supply in case of any disagreement with its foreign policy. Russian is criticized for high levels of governmental interference into energy production, the lack of competition in the oil-and-gas industry and democratic values. Moscow, in its turn, disagrees with these accusations completely. Kremlin, admits, that the level of governmental control of energy industry is higher than in majority of the European states, but Russian state depends on energy sales to reconstruct economy and strengthen social sector. For these reasons Russian interests in European energy sales are mainly economic ones.

To sum it all up, the EU and Russia prove to be unable to hear each other. The lack of understanding and trust between the partners strengthens the feeling of insecurity and makes it even more difficult to build up mutually beneficial energy dialogue. The vision of Russia as a threat to energy security pushes the EU member states to develop common energy policy to restrain Russian ambitions to control Europe via energy sales. However, the defensive nature of the common energy policy would not help to overcome the difficulties in the energy trade between the two partners. In my opinion the solidarity between the EU members is, indeed, important. There are a lot of challenges in energy relations and coherent position of the European Union towards Russia with clearer understanding would benefit all sides involved. However, in order to create energy security society mentioned in the beginning of the paper, “the Russian threat” should not be exaggerated. On the contrary, Russian interests should be considered to build valid ground for effective partnership. In the second part of the paper I will demonstrate on the example of competing pipeline projects, how the extreme levels of securitization of energy

trade and the lack of solidarity between the EU member states complicate the realization of the plan for supply diversification.

The case study of The South Stream and NABUCCO pipeline projects and their influence on the supply diversification

In this section I will talk about the competition between Russian pipeline project South Stream and the EU pipeline project NABUCCO. It is argued that Kremlin is trying to sabotage the construction of NABUCCO pipeline in order to prevent the EU from supply diversification and continue using “energy weapon” in its foreign policy. Russia is using the lack of solidarity between the EU member states to slow down the realization of NABUCCO project in favor of the South Stream project, which is more expensive and useless from the perspective of supply diversification. Below I will look on the two projects in more details in order to evaluate their importance for supply diversification and to suggest how the development of Common Energy Security can contribute to this diversification.

I will begin by brief description of NABUCCO project. The idea of 3300 km long pipeline construction which would connect European customers with gas fields in Iran first was designed by Austrian company OMV in the late 1990s. NABUCCO would transport gas from Caspian region via Turkey to Bulgaria, Romania, Hungary and Austria. The construction should begin in 2011 and finish in 2014. NABUCCO will cost around 5 billion Euros and have a capacity of 31 billion cubic meters (bcm) per year. (Nanay, 2010)

The main problem of this project is the uncertainty about the possible suppliers. Azerbaijan is able to provide only 10 – 12 bcm per year, which is not enough. (Nanay, 2010) According to the original plan, the rest of the gas was supposed to come from Iran, but considering the current intense situation around Iran it is not likely. At the moment investors consider Central Asian states to become potential suppliers. (Simonov, 2007) It may include also Iraq or Egypt. (Socor, 2008) This uncertainty creates the risk that there would be no gas to pump through the pipeline. Moreover, recent announcement made by Baku that Azerbaijan delays the beginning of the Shah-Deniz gas-field development at the Caspian Sea until 2016 instead 2014, creates additional concern about the gas supplies for NABUCCO project. (New Europe, 2010)

Speaking about Russian project, the South Stream planned to go under the Black Sea to supply Russian gas to Bulgaria and further to Italy and Austria. At the moment, seven states apart from Russia are involved into the South Stream pipeline project: Croatia, Bulgaria, Serbia, Hungary, Greece, Slovenia and Austria. In the next couple of months Gazprom is planning to finish negotiations with France about French power group EDF participation in the project. (Filatova, 2010) The South Stream is more expensive as compared to NABUCCO. Estimated cost is around 10 billion Euros. However, it is important to mention, that the total cost of NABUCCO depends on the potential suppliers. At the moment it is difficult to say who will provide the rest of the gas apart from Azerbaijan. But the construction of one or several additional pipelines to connect new suppliers with Europe would defiantly increase the cost of NABUCCO.

The competition between two projects is the complex game. Russia is blamed for the high-levels of governmental interference into the South Stream project. The pipeline is often represented by Vladimir Putin, who is using the lack of solidarity to sign the bilateral agreements with countries along the planned NABUCO route. (Socor, 2008) Recently Putin visited several EU member states, including Italy and Austria. The majority of visits are related to the discussion about the South Stream project. In this sense the level of governmental interference is higher as compared to NABUCCO.

In official interviews Vladimir Putin emphasizes that Russia is not threatened by NABUCCO and is not going to sabotage the competing project. However, in my opinion it is not totally true. The pipeline from Azerbaijan to Europe bypassing Russian territory does, indeed, interfere with Russian interests, because it would reduce its share on the European energy market. But it is important not to exaggerate the potential threat to Russia from NABUCCO. At the moment it is still not clear who will produce the rest of the gas required. To start construction without signing any contracts with energy producers is risky and expensive enterprise. (Simonov, 2007) To sum it up, Russia wants to keep the dominating position for energy supplies to Europe. And the lack of solidarity gives an opportunity for Russian officials to sell the South Stream project to separate member states. To come back to the argument back in the first section of the paper, the EU policy towards Russia is rather defensive. The EU-Russia energy dialogue is not effective because Moscow and Brussels refuse to listen to each other and to consider the interests of each other in energy sphere. This context of confrontation and unclear vision of the EU on which project is more important for energy security gives Russia an opportunity to use alternative ways of protecting its interests.

Is the competition between South Stream and NABUCCO actually threatens European Energy Security? Austria, Bulgaria and Hungary (states involved in both projects) argue that there is no conflict between these projects - both pipelines will contribute to supply diversification. It is important to remember that these two projects have two different aims. NABUCCO is aimed to connect Azerbaijan and Central Asian gas with Europe bypassing Russia. At the same time, the South Stream and

Nord Stream² are aimed to reduce the dependence on the transit states. 95 per cent of Russian gas supplies transit through the territory of at least one country before reaching its consumers in Europe. This creates transit risks for both Russia and Europe. (Spanjer, 2007) The transit rows with Ukraine in 2006, 2008 and 2009 resulted into the gas short-cuts to the EU customers. The South Stream would help to avoid such short-cuts.

To conclude, in this paper I did try to demonstrate that the high levels of interdependence between Russia and the European Union in energy sphere is accompanied by the inability to consider interests of each other and the lack of trust. Russia exploits the lack of solidarity between member states to pursue its interests. For instance, Russia use bilateral ties with individual states to sell the South Stream project, which seen by some experts as the expansion of EU dependence on Russian gas. To overcome the feeling of energy vulnerability the EU member states want to develop common energy policy, which would allow them to prevent Russia from using energy supplies as foreign policy tool. This common policy is seen as defensive mechanism and does not include the interests of energy producers. This approach is distractive and would not allow the EU and Russia to overcome problems in energy trade. Coherent common European energy policy is essential. It should formulate clearly the priorities of the European Union as a whole in energy sphere in general, and in relation to Russia in particular. However, Russia should not be presented as a threat in this strategy. On the contrary, it is important to build the common ground for cooperation, considering needs of each other. Common energy policy may help to prevent Russia from blocking NABUCCO project, to encourage potential energy-suppliers to sign up for this project; but it should not be orientated against South Stream project, which as you can see from the section above is equally important for the supply diversification.

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² Nord stream is a Baltic Sea pipeline project aimed to connect Russian city of Vyborg with Germany. The construction began in April 2010,

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