

TWELVE MONTHS: THE SHORT LIFE OF COMFORTABLE ASSUMPTIONS ABOUT RUSSIA'S ENERGY POLICY IN 2006

by Vladimir Socor

The Kremlin's confiscatory assault on Royal Dutch Shell and threats to other Western energy majors in Russia on Black Tuesday, December 12 (see EDM, December 13) is the latest in a series of moves disproving Western wishful thinking about Russia's energy policy.

That wishful thinking burgeoned, ironically, in the wake of the January 2006 Russian gas supply cutoff to Ukraine, which rippled farther downstream in a number of European countries. While the "wake-up call" for coordinated Western energy policies resounded mainly in the editorial pages after that crisis, most Western governments and energy corporations embraced the set of assumptions that are now being exposed as illusory by Moscow's own actions.

Assumption One during 2006 held that Russia and Western consumer countries would benefit through strategic relations of "reciprocal access." Namely, access by Western energy majors and "national champion" companies to Russian oil and gas deposits in return for Russian companies' acquisition of Western infrastructure, distribution systems, and direct access to Western consumers. However, by the year's second half, Russia embarked on a policy of excluding Western investors (most notably from the super-giant Shtokman gas field) and, by the year's end, threatening confiscatory measures against existing Western projects in Russia (Shell, ExxonMobil, BP) under tax or ecological regulatory pretexts. Meanwhile, turning the "reciprocity" into unilateralism, Russia's state-controlled energy companies rapidly acquired infrastructure and production assets in the West as well as in countries that traditionally supply the West with energy. This Kremlin-driven strategy brought a qualitatively novel type of threat to Western energy security.

The year's Assumption Two, equally popular and partly related to the first, spoke of "mutual dependence." It held that the West's growing dependence on Russian supplies is not particularly risky because it is offset by Russia's dependence on revenue from Western importers of Russian energy. As the year wore on, this Western postulate shattered against Russia's active planning for construction of oil and gas pipelines leading to the Asia-Pacific region, setting the stage for Moscow to play Western against Far Eastern consumers in a none-too-distant future. Moreover, the "mutual-dependence" assumption blithely ignored Russia's advantage as a single-actor state exporter versus a multiplicity of eager, uncoordinated, and often competing Western buyers, with ample scope for manipulation by Russian state companies. Mutual dependence might become possible between the European Union collectively and Russia, if the EU develops a common energy policy, which however does not seem to be on the cards for now.

Assumption Three during 2006 claimed that Moscow cannot afford to exclude or mistreat Western energy companies because Russia's state companies do not have sufficient means to invest in energy projects on Russian territory. However, Moscow successfully

challenged that proposition through the Initial Public Offerings of Gazprom, Rosneft, and other state-controlled companies, which quickly raised multibillion-dollar investment funds on Western private capital markets. Those IPOs launched a process of transferring Western resources to Russia for energy projects under the Russian state's discretionary control, without a real say by Western consumer countries regarding future production levels or the export destinations. When Russian President Vladimir Putin announced the go-it-alone policy on Shtokman, he did so with the argument that Russia does not need to invite Western investors, as it can itself raise the necessary capital on Western financial markets. The Kremlin took that argument one step further in December by initiating, in effect, a partial confiscation of Western energy investments in Russia.

The year's Assumption Four clings to a hope that Russia's ratification of the Energy Charter Treaty and signing of the attendant Transit Protocol would help the West overcome its collective vulnerability on energy security. It envisages in particular that Russian pipelines would provide transit of oil and gas from third countries via Russia to Western consumer countries. However, Moscow's actions during the year showed how risky this proposition is. The Russian government shut off energy pipelines repeatedly in 2006, not only to Ukraine and Georgia early in the year, but later also to EU member country Lithuania (adding to the earlier oil pipeline shutoff to Latvia); it blocked access for oil from Kazakhstan via Russian ports or pipelines to EU member countries; conclusively defeated the Odessa-Brody oil transport project, which was an EU priority; it is attempting to kill the Nabucco gas transit project, also an EU priority; and is blocking the expansion of the Caspian Pipeline Consortium's (CPC) line, threatening to transfer its section on Russian territory into state monopoly Transneft's control and imposing extortionate terms of transit on Chevron, ExxonMobil, and other companies on that pipeline.

Thus, the idea of relying on Russia for transit under the Energy Charter Treaty and Protocol has been shown during 2006 to entail unacceptable risks. This idea is partly an excuse for not pursuing direct Western direct access by pipelines to eastern Caspian oil and gas. Moscow's refusal to adopt the Treaty and Protocol is a blessing in disguise for the West and should re-focus attention on the need for direct access to the eastern Caspian basin via the Black Sea region.

Moscow actively cultivated that set of Western assumptions during most of 2006; but apparently felt strong enough to abandon parts of that soothing discourse in the latter part of the year, and to resort to overt bullying by the year's end. The comfortable Western assumptions about Russia's energy policy in 2006 should now come to the end of their 12-month lifespan.

--Vladimir Socor