

# THE STRATEGIC RELEVANCE OF AGRI IN EUROPE'S SOUTHERN GAS CORRIDOR

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## **Özet**

Avrupa, enerji açısından neredeyse tamamen kıta dışındaki satıcılara bağımlıdır. Son zamanlarda Avrupa Birliği (EU), çeşitli ülkelere enerji bağımlılığını azaltmayı başaramadı. Bu durum, Avrupa Birliğini dünya arenasında jeopolitik bir oyuncu olarak oldukça savunmasız bırakmıştır. Özellikle merkezî ve Doğu Avrupa ülkeleri doğalgazlarını Rusya'dan sağladıkları için neredeyse tamamen onlara bağımlıdır. Merkezi ve Avrupa kıtasındaki bazı ülkeler bu durumunu değiştirmeye çalışmaktadırlar. Azerbaycan, Gürcistan ve Romanya, 2010 Nisan ayında Rusya'yı atlayarak Hazar Denizi yoluyla Karadeniz'den Avrupa'ya doğalgazı taşımak için anlaşmışlardır. Bu yıl içinde Macaristan da AGRI adlı konsorsiyuma katıldı. Sonuç olarak, AB üye ülkeler, Rus kontrolündeki doğalgaz boru hatlarına daha az bağımlı olacak.

**Anahtar Kelimeler:** Enerji çeşitliliği, AGRI, LNG, Karadeniz, Jeopolitik.

## **Abstract**

Europe is almost completely dependent for her energy on outside suppliers. In recent years the European Union (EU) has not succeeded in reducing the energy dependencies by diversification, a keyword in European strategic papers (see, COM 2008 781 final). This makes the European Union as a geopolitical player in the world arena rather vulnerable. Especially the countries in Central and Eastern Europe are almost completely dependent for their gas supplies on Russia. Some countries in the Central and European space are trying to modify this state of affairs. Azerbaijan, Georgia and Romania have agreed upon in April of this year to transport gas from the Caspian Sea via the Black Sea to Europe bypassing Russia. Later this year Hungary also has joined this so-called AGRI consortium. As a result, EU-member states will be less dependent on the gas pipelines that are carrying Russian gas through states that are under Russian control.

**Keywords:** Energy diversification, AGRI, LNG, Black Sea, geopolitics

## **EU-RUSSIAN RELATIONS IN ENERGY POLITICS**

Russia is intrinsically involved in the EU debate on energy security. According to Richard Youngs, Russia 'completely dominates (...) debates over European energy policy (see Youngs 2009, 79).' Russia is the main

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actor engaged in the issue of supply. As one of the largest global suppliers of natural gas and oil, Russia can meet high European demands for energy. Due to its geographical proximity to the Union, the country's energy giant, the state-owned company Gazprom is also an obvious partner for European state members' energy providers. Russia on the other hand benefits from these European revenues. One fifth of its annual GDP income is derived from energy revenues (Godzimirski 2009). However, political unrest in the post-Soviet space can endanger reliable supply to Europe, as has happened several times in recent years. Having toppled the communist system only two decades ago, Russia remains an unstable partner in energy negotiations (Correlje and Van der linde 2006). In 1994 efforts to place Russia's pipeline network under multilateral regulations failed when Russia refused to ratify the Energy Charter Treaty (Youngs 2009, 80). To prevent further upheavals and ensure energy security, the EU established a Common Economic Space (CES) with Russia at a summit in St. Petersburg in 2003. The long-term goal of the agreement is the formation of an open market between EU and Russia.

Europe's demand for gas is high, however, and Russia can meet this demand like no other actor on the market (Progress Report 2008). Europe will not be able therefore to exclude Russia from gas deals. Maintaining good relations with Russia is a prerogative. By creating a more formal cooperation basis with Russia, EU can, however, avoid becoming a victim of the sort of unpredictable reactions the Ukraine has had to put up with regularly. Signed contracts can ensure EU energy safety and reasonable prices for Russian gas. The Common Economic Space between EU and Russia provides a framework to establish legally binding documents on gas deals.

Energy related issues form the "backbone" of CES (see Sutela 2005, 14). Due to asymmetrical provisions in supply and demand between the Union and Russia several gas disputes have had to be solved during the last years (see Progress Report 2008). Russia has turned out to be a politically unreliable partner in gas supply. Following political rows with neighbouring states Russia has regularly turned off the gas tap thereby hindering transit to Europe. During the Russian war with Georgia in 2008, following price disputes with Ukraine in 2006 (Stern, 2006; Youngs 2009) and as a reaction to failed debt payments by Ukraine in 2008 (Pirani et al. 2009), Russia demonstrated its power by causing severe gas shortages in Central and Eastern Europe following the pipeline cuts. As a consequence, EU and Russia agreed on an Early Warning Mechanism in 2009 to prevent further crises leaving EU countries at the mercy of Russian gas magnates (EU press release, 2009).

European energy security is highly dependent on diplomatic relations with Russia and joint ventures between European and Russian energy

companies. The foremost objective of Union's energy policy is to secure supply. As a 'net energy importer' (COM 2008 781 final) Europe is exposed to energy supply shocks, price volatility and decreasing fossil fuel reserves. Indigenous energy production covers barely half of Europe's need, with 56 percent of European energy imported from third countries. In fact, domestic production even started declining in 2004 (COM 2008 781 final). If this trend is not reversed, fuel imports will rise even further in the future. Oil and gas, i.e. 60 and 26 percent in 2008 respectively, compromise the largest share (COM 2008 781 final). Russia provided 36 percent of oil imports in 2007 (Europe's Energy Position, 2009, 21) and 42 percent of gas import in 2008 (COM 2008 781 final), rendering the EU highly dependent on Russian resources. Even if substantial increase in Russian energy supplies is achieved until 2020 twenty percent 'energy imports [are] set to rise under almost all scenarios' (COM 2008 781 final, 3).

### **THE GREAT PIPELINE RACE**

The European Union has not succeeded in developing a common energy strategy, nor a strategy of energy diversification. There is a lot of talking about the EU's sponsored Nabucco-pipeline that should carry gas from Central Asia and the Caspian Sea region via the Caucasus and Turkey to Europe thereby bypassing Russia and Ukraine but concrete steps to construct the pipeline have not been taken so far. It is extremely unlikely that the Nabucco project will be operative in 2015 as has been planned. Without a common energy policy and a successful strategy of energy diversification the EU will hardly become a major political player in the 21st century.

Europe is linked to the Russian gas fields by several large gas pipelines, like the North Stream. More gas pipeline routes, like South Stream will be planned in the near future and can be considered as a concurrent to the Nabucco pipeline in the southern gas corridor. These pipelines and projects are controlled or will be controlled by the Russians or will run through countries, like Belarus or Ukraine that are politically controlled by Russia. Also some richer countries in the Western part of Europe, like Germany have reached an agreement with Russia on the supply of gas. Russian gas will be carried by pipelines that run directly to Germany via the Baltic Sea, the so-called North Stream. North Stream is cooperation between the state-owned Russian company Gazprom, the German energy companies E.ON and BASF and the Dutch Gasunie. Poland is excluded from this pipeline and the Russian-German cooperation has been interpreted in Poland as a modern Molotov-Ribbentrop Pact referring to the Soviet-Nazi pact preceding the Second World War that determined the tragic fate of Poland and the other Central and Eastern European countries during and after the Second World War.

In the past Russia has successfully played EU members off against the others. The EU treats energy policy as a foreign policy issue, an area member states like to protect from too much interference from Brussels (Youngs 2009). By signing bilateral agreements with major national energy providers such as German E.ON, Italian ENI and French EDF, Russian energy giant Gazprom has managed to become a direct stakeholder in the largest national gas markets in Europe (Leal-Arcas 2009). Other competing non-EU gas suppliers to the EU, such as Algeria and Libya that are active on the Italian market, have been made business partners by the Russians in an attempt to monopolize gas supply into the EU. The Lisbon Treaty added a clause on energy solidarity amongst the EU-members. The clause has no legal binding, however and is not being obeyed (Progress Report, 2008). Companies like E.ON, ENI and EDF are therefore helping Russia along in gaining a gas monopoly.

Hence, Russia has used its monopoly position as a real geopolitical weapon that can be employed for 'divide and rule' tactics. Austria, Hungary and Serbia could not resist the temptation and were willing to accept the offer of Gazprom to buy shares in their local energy companies, i.e. Austrian OMV, Hungarian MOL and Serbian NIS to bind them to the South Stream project. Russian energy company Surgutneftegas has acquired 21.2 percent stake in Hungarian oil and gas company MOL, although MOL's constitution allows only for a foreign stake of 10 percent. This deal violating Hungarian law was concluded by the pro-Russian, oligarchic government of Prime Minister Ferenc Gyurcsány who was lobbying for the position of 'commissioner of the South Stream project' and made Hungary completely dependent on Russian interest. Recently the new Hungarian centre-right government under Viktor Orbán declared by his spokesman Tamás Fellegi, Hungary's National Development Minister that the state wants to increase its leverage in the energy sector and does not welcome foreign stakeholders in strategic national companies (See Politics.HU). It will be not easy to get rid of the Russian stake in the MOL company, however. Gazprom was able to buy the Serbian state energy company NIS for almost nothing and also acquired the control of pipelines on Serbian territory giving the Serbs the guarantee that South Stream will be running over Serbian territory. In the end South Stream will reach Silvio Berlusconi's Italy who is a frequent guest in the Kremlin and a strong supporter of Russian exclusive energy interest in Europe (see Lucas 2008).

In order to break the exclusive dependency on Russia gas that is not only the gas itself but also the routes carrying the gas to the Union the EU has launched several projects to diversify the routes. The best-known pipeline project in the southern gas corridor is the already mentioned Nabucco that will carry gas over the territory of Turkey. But several other smaller projects, such as the Trans-Adriatic Pipeline (TAP), the Turkey-

Greece-Italy Interconnector (ITGI) or the Azerbaijan-Georgia-Romania Interconnector (AGRI) all have the potential to be an important element of the southern gas corridor and even call into question the future of Nabucco itself. In any case, all these pipelines will draw gas from the same gas fields, i.e. Sah-Deniz 1-2 in the Caspian Sea region.

European pipeline project Nabucco has been undercut several times by the Russians. Under Ferenc Gyurcsány's pro-Russian government in 2007 Hungary signed a bilateral deal with Gazprom to receive gas via the Russian pipeline Blue Stream (Youngs 2009). Due to this deal Hungary temporarily withdrew from the Nabucco pipeline project triggering criticism from Brussels (see Aczél 2010). In 2010 Russia signed deals with Azerbaijan, securing gas supplies to stream to Russia instead of through the delayed Nabucco pipeline (Socor 2010).

Furthermore, Russian pipeline project South Stream will form a direct rival supply route to Nabucco as it also carries gas to Southern Europe (Finon 2010). With French EDF and Italian ENI financing the rival, it is hard to take Europe seriously in its attempts at solidarity. South Stream will bypass Romania and cut through Bulgaria playing off Romania and Bulgaria against the other. This is one of the main reasons Romania has been initiating AGRI bypassing Russia in order to guarantee itself a place within the South Stream project.

### **RUSSIAN GAS MONOPOLY IN CENTRAL AND EASTERN EUROPE**

As mentioned above Russia has an important share in the energy supply of the European Union. Especially the countries in Central and Eastern Europe are almost completely dependent upon Russian gas. Slovakia is depending for 99 percent, the Czech Republic for 78 percent, Hungary for 80 percent, Poland for 67 percent and the Baltic countries, Estonia, Latvia and Lithuania for 100 percent on Russian gas. The only exception in Central and Eastern Europe is Romania that satisfies 85 percent of her gas demands from internal resources. Furthermore, in these countries the connecting pipelines to Russia run over Ukrainian territory, i.e. in the case of Slovakia, Czech Republic, Bulgaria, Greece, Austria, Hungary, Slovenia and Romania and Russia or Russian controlled countries like Belarus in the case of the Baltic countries (compare Marác 2009, 17).

The Russians are very well aware of this and have used the energy weapon against those who are critical about present day Russia. The small Baltic countries can be blackmailed by threatening to cut off energy supplies from Russia. In recent winters Russia was not ready to deliver gas to Ukraine of president Viktor Yushchenko who was conducting a pro-Western policy. After the election in February 2010 of this year that was won by the pro-Russian politician Viktor Yanukovich Ukraine does not

have to be afraid that they will be cut off from Russian energy supplies. The government of Yanukovich will support Russian politics led by Putin and Medvedev in exchange for lower energy, especially gas prices that will keep the Yanukovich government longer in power.

Gazprom, Russia's state-owned sole exporter of Russian gas has not only succeeded in attaining large shares of European energy firms it also holds long-term supply contracts with European distributors (Dreyer 2010). In the cases of Slovakia and Bulgaria, where one distributor dominates the entire market for gas (Stern 2005) consumers are 100 percent dependent on Russian supplies. The Baltic states are also highly dependent on Russian gas with Gazprom holding a 37 percent stake in Eesti Gaas (Stern 2005, 127), Estonia's gas monopoly. These European bilateral ventures with Russian state-owned gas company Gazprom undermine EU attempts to speak with one voice and to take up seriously the issue of energy diversification. As some EU-members rely on only one supplier, i.e. the Baltic states on Russia securing supplies entails lowering dependency on these suppliers by diversifying the sources. The Union's strategy seems to construct 'reliable framework conditions' to realize this diversification (COM 2008 781 final, 5). Priority infrastructure projects aimed at interlinking European energy markets and subsequently decreasing their dependence on third countries is listed under this point. Projects include the 'Baltic Interconnection Plan' which entails key infrastructures necessary for effective interconnection of the Baltic region with the rest of the EU and the 'southern gas corridor' interconnections to link gas supply from Caspian and Middle eastern sources and Liquefied Natural Gas (LNG) develop LNG action plan on liquefaction and storage facilities. One of these latter projects is AGRI.

#### **THE STRATEGIC RELEVANCE OF AGRI**

As we have discussed above especially the countries between Germany and Russia in the Central and Eastern European zone are worried about their energy supplies that is strongly connected to their security and safety. To retake the initiative three presidents, the President of Azerbaijan Ilham Aliyev, the President of Georgia Mikheil Saakashvili and the Romanian President Trajan Basescu met in Azerbaijan's capital Baku on 14 September of this year and signed the Baku declaration in which the three heads of state decided to construct a gas pipeline that will connect the three countries. The construction of the pipeline labeled AGRI which is the abbreviation of 'Azerbaijan-Georgia-Romania-Interconnection' will connect these countries via the Black Sea. The Georgian president Saakashvili who is clearly on the side of the West and would like his country to join NATO has played a crucial role in setting up AGRI. With the help of the AGRI

project Saakashvili himself is using energy as a geopolitical weapon against Russia trying to embarrass the Russians at their own playing field.

AGRI will draw gas from the Caspian Sea that will be carried via a pipeline across land to Georgia for liquefaction. This process of liquefaction will take place in a plant for LNG exports at the Azerbaijan-owned oil export terminal of Kulevi in Georgia. Kulevi is by the way at "spitting distance" from the breakaway autonomous territory Abkhazia. Abkhazia is a marionette state of Russia and is providing Russia a stronger geopolitical position in the southern part of the Caucasus to put pressure on the AGRI project. Commentators are afraid that this will make the AGRI project vulnerable indeed. Further transport of LNG will take place via tankers from the Georgian port of Poti to the Romanian Black Sea port of Constanta. In Constanta a terminal will be constructed for the re-gasification of the LNG. The gas will be pumped through Romania's pipeline system to Hungary and to the rest of the Balkans and the European Union.

The Romanian President Traian Basescu has declared that the project will be set in motion by all means but that he is hoping for financial support from Brussels. An advantageous moment for this is the coming year 2011 because in the first half year Hungary will chair the Union and afterwards Poland. The latter country is strongly supporting the Eastern Partnership to establish all sorts of ties in the post-Soviet space having Georgia and Azerbaijan among its members. Basescu is counting on support from Hungary where recent elections in April 2010 have been won with a landslide by the pro-Western, centre-right coalition led by Viktor Orbán. This coalition took the government position of the Hungarian socialist party MSZP, an ardent supporter of Gazprom policy. On September 20 Hungary even announced it would become a shareholder in AGRI project. Now the following state energy companies, i.e. Romanian Romgaz, Georgian Oil and Gas Corporation (GOGC), the State Oil Company of Azerbaijan Republic and the Hungarian Magyar Villamos Művek Zrt. each holds a 25 percent stake in the project. Interestingly the Hungarian government had to leave out the MOL company because a Russian company has a stake in MOL, otherwise the Russians would have entered the AGRI project through the backdoor.

AGRI will carry eight billion cubic metres gas a year (bcm/year) to Europe. Compared to the planned 38 bcm/year of Nabucco this is a rather modest figure. AGRI's capacity will be about five times less than Nabucco's. The figure is indeed rather modest when we take into account the yearly LNG-import of a country like France that is about twice as much as the 8 bcm/year that is planned by AGRI. The project financing will require a relatively modest amount of money of 4-6 billion euro. These figures can be lifted quite easily as demands will increase, however. In speeding up the distribution possibilities of AGRI to Central Europe and the Balkans the interconnecting pipeline between Hungary and Romania has already been

constructed. On October 14 of this year the gas pipeline linking the Romanian city of Arad and the Hungarian city of Szeged making the distribution of AGRI gas to Central Europe possible has been opened. It is also one of the first gas pipelines running 'north-south' in the Central and Eastern European area. The opening was attended by European commissioner for energy, Günther Oettinger who announced that pipelines running 'north-south' on the territory of the Union, like the Arad-Szeged pipe line and their connections to the north will be sponsored by the European Commission. North-south pipelines play an important role in the energy security of the Union.

EU-projects in the southern energy corridor are strengthened by a decision of the European Commission to establish a Danube Region in order to interconnect a geopolitical territorial unit, a European macro-region through which the Danube river is flowing consisting of Germany, Austria, the Slovak Republic, Hungary, Croatia, Serbia, Romania, Bulgaria, the Republic of Moldova and Ukraine – six of which are EU Member States, and in a broader territorial context the region also comprises the Czech Republic, Slovenia, Bosnia Herzegovina and Montenegro. Concerning Germany and Ukraine only the regions have been invited that are crossed by the Danube, like the German federal states Baden-Württemberg and Bavaria. By doing so it is prevented that Germany with its enormous economic power would dominate the Danube strategy (European Parliament 2010). Note that the Danube strategy is a geopolitical 'Vorland' of the Black Sea with Romania and Bulgaria neighbouring the Black Sea and Romania holding a key position in the AGRI project. AGRI is in fact embedded in the Danube strategy and the Eastern Partnership program (compare Marác 2010, 10-14). Observe that one of the achievements of the Danube Strategy is energy diversification. Article 12 stresses 'the need to diversify energy sources and calls on the Commission and all riparian states to increase cooperation in the field of energy, to promote and implement joint projects on energy efficiency and renewable energy sources...' (European Parliament 2010, article 12). Without doubt both Hungary and Poland will try to put further flesh on the southern gas corridor concept when they assume the rotating EU presidency in 2011. Both countries will be a reliable partner of Brussels to decrease influence of Russian controlled gas flows to Europe.

Observe furthermore that AGRI is strengthening the bargaining position of those countries being involved in the project while weakening the position of other countries not being involved in the project. Azerbaijan will have a stronger position with respect to Russia's South Stream and the European Union's and Turkey's Nabucco. AGRI instead of Nabucco might become the alternative transit route for Azerbaijani gas. Hence, Azerbaijan will have more space in order to maneuver when negotiating with Russia,



Europe and Turkey on supplying gas. Georgia will be able to use energy supply as a geopolitical weapon against Russia by offering the AGRI route to Europe and the West bypassing Russia. Of course this policy might backfire putting more Russian pressure on the Caucasus state Georgia. Romania has been left out from Russia's South Stream plans and with Romania being a strong player in AGRI the Russians have recently announced that they will reconsider Romania to become a member of the South Stream consortium again, otherwise being afraid that the Russian gas monopoly will be threatened. AGRI will weaken Turkey's bargaining position with respect to Europe for with AGRI there will be an alternative transit gas route for Nabucco. Turkey will lose the 'only transit' option it had to Europe. From this it follows that AGRI is a small project with enormous strategic relevance, although due to this it will probably be the quickest of the projects in the southern gas corridor to be realized. Europe has to be prepared that the Black Sea also will be an important area forming a crucial energy and geopolitical front.

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