RUSSIAN ENERGY POLICY AND THE ART OF GEOECONOMICS

by Ioannis Alexandris

In the present article we will examine the way Russia, under Putin, uses energy as a tool of statecraft and foreign policy. However, as it will be discussed below, overreliance on exported fossil fuels may run the risk of self-entrapment.

In their recent book, Robert D. Blackwill and Jennifer M. Harris define Geo-economics as “The use of economic instruments to promote and defend national interests, and to produce beneficial geopolitical results”. Also, geoconomy includes “the effects of other nations’ economic actions on a country’s geopolitical goals”.¹ Energy, as a good of vital importance, is being considered as a prime instrument of geo-economic power projection. According to the two authors, the country that plays a leading role in the chessboard of the geopolitics of energy, better than anyone else (Qatar, Saudi Arabia, Norway etc.), is Russia.

The energy sector is a key aspect of Russian foreign policy and a strategic pillar of its policy towards Europe. For Vladimir Putin, Russia's role in the global energy market largely determines its geopolitical influence. With his rise to power at the beginning of the millennium, the Russian energy influence reached new and unprecedentedly huge levels. This is due to certain reasons, some of them conjectural and some others calculated:

Firstly, it benefited from high oil and gas prices in the period 2000-08. Thus, in 1999 regarding crude oil each barrel’s price was approximately at 18 $. In less than ten years each barrel’s price reached at 147$. This steady rise stimulated the economy and signified a major growth that was unimaginable during the Yeltsin-era.²

Secondly, it was very important the government’s consolidation of the energy sector. At the beginning of the millennium, Putin, after taking the reins of a weakened and fragmented Russia proceeded in a «checkmate» move, by resetting the energy industry under state control, following a decade of extreme privatization. State companies-giants Gazprom, Rosneft and Transneft operated and are still operating as levers of Russian foreign policy, by completing newly negotiated energy agreements under harshest conditions, in full

¹ Robert D. Blackwill, Jennifer M. Harris, «War by Other Means: GEOPOLITICS AND STATECRAFT.», Belknap Press, 2016, p.20
² John Lough (2011) ,Russia's Energy Diplomacy, Chatham House , page 3
Available at: https://www.chathamhouse.org/sites/files/chathamhouse/19352_0511bp_lough.pdf
consultation and coordination with the central Russian government and its strategic imperatives. Transforming the "old system of oligarchs" of the 1990s into a network of managers ‘‘faithful’’ to him, he managed to elevate the energy sector into a lever of maintaining political power.

Thirdly, aiming to gain control and a bigger say over energy projects - with the prime example of the major pipelines carrying energy reserves, the Russian government moved more aggressively and actively abroad. It shows an attempt by Russia to reconcile security and energy. By taking advantage of Russia’s geographical proximity to certain countries - especially when it comes to newly established EU members - Russia makes them almost exclusively energy dependent to its large supplies.³

As the second supplier in natural gas and oil reserves energy policy means for Russia a key pillar of its foreign policy. Typically, the annual revenue from the energy sector accounts for approximately 50% of total government revenue.⁴ It is worth noting that the energy sector contributes substantially to the domestic political stability of the country and is also being used as a mean of ensuring the political acceptability of Russian citizens, which the government takes care of, by supplying them at low prices.⁵ Additionally, revenues from energy export and taxation supply two Russian state funds: the “Reserve Fund” and the “National Wealth Fund”.

European energy companies have developed autonomous –to a certain extent- action by taking advantage of the reduced role of the European states, unlike in the case of Russia, where Gazprom can be seen even as an integral arm of its policy. By exploiting this specific difference, the Kremlin used it as another weapon of offering attractive co-shares in foreign companies for energy projects (see. ENI, BP, etc.). Russia promotes joint ventures between foreign energy giants, using its advantageous position in order to benefit, among others, by knowledge diffusion. Economic interests are harnessed by the close control of the states and

⁴ Energy International Agency, RUSSIA: Overview Available at : https://www.eia.gov/beta/international/analysis.cfm?iso=RUS
gain closely geopolitical content. Undoubtedly, it is a capability that the US, EU countries and Japan are deprived of.  

EU, INTERDEPENDENCE AND THE POST-SOVET AREA

The issue of European energy dependency on Russia has always been used by the Kremlin as a bargaining tool that serves geopolitical objectives. Indeed, during the latest years the search for cleaner energy sources has amplified the importance of gas. The hydrocarbon reserves in Europe are not enough to meet the great domestic demand. Considering the fact that Russia is the second worldwide producer of gas and oil, it comes at no surprise that the aspect of energy is strongly connected with the whole spectrum of its external relations, with a particular significance in the case of the EU.

It is also a common trend when some scholars and American policy analysts, who espouse a Cold War approach, are applying an alarmistic rhetoric considering energy as the Russian weapon for breaking the Euro-Atlantic unity and for potentially leading to Europe's disengagement from the US. Despite the exaggeration of such statements, the fact that the EU imposed limited sanctions, in the aftermath of the Ukrainian crisis, is due to high level of reliance on Russian energy. After all Germany, Europe’s powerhouse, is a major energy partner to Kremlin.  

Of course, it is worth noting that this dependence is highly interactive, since the European market is an important destination for Russian gas and oil. Any loss of the European market from the Russian energy clientele would involve painful losses and bankruptcy of the Russian public. Therefore, it is, but rather a relationship of interdependence rather than a relationship of dependency. This is why Russia has sought, in turn, to diversify its customer base by looking eastward, -China serves as the greatest example - a move that will be discussed below. However, the European market remains, for the time being, vital for Russia, as the

---

7 Tim Marshall, ”Prisoners of Geography”, Elliott & Thomson Limited, 2016, page 19
8 Judy Dempsey (2015), Germany’s Ambiguity Toward Russia and Energy Security, Carnegie Europe. Available at: http://carnegieeurope.eu/strategiceurope/62243
largest recipient of exports. Russia covers 1/3 of the European demand for natural gas, while about half of it is being transported via Ukraine.

While North American countries are seeking to achieve energy independence through self-sufficiency and new energy projects elsewhere, mainly in China and the Far East, are faltering, since they have become non-viable due to the current low energy prices, Russia is once again supporting its energy monopoly in the European market. Lately, Russia has sought to strengthen its influence and control of the northern European market by projects such as the Nord Stream II pipeline, which aims to bypass Ukraine as transit point.

However, the situation is different when it comes to the South Eastern Europe and the Eastern Mediterranean, where the Russian energy primacy is by no means assured. Washington’s policy entails halting Russian energy projects, and promoting attractive alternatives. Energy-sufficient Azerbaijan and the Turkey are serving those plans, as a supplier and a hub, respectively. Russia faces the challenge of catching up with competitive projects, such as the pipeline TAP. The plans for both the Turkish and the South Stream are hidden behind this notion. 

---

9 Eurogas Statistical Report, Deutsche Bank Research

10 In Russia, a new strategy for a new pipeline (2015) Available at: https://www.stratfor.com/analysis/russia-new-strategy-new-pipeline
However, the Russian energy strategy does not end here. Besides of preserving its status as the key energy supplier of the EU, Russia also endeavors to prevent the development of viable alternatives, by using its geopolitical position and power. Therefore, Russia has used its position as a security guarantor thereof, in order to actively seek to impede the efforts of the Central Asian countries to provide Europe with alternate supplies of natural gas.

In order to maintain its influence in the neighboring countries of the post-Soviet space, Moscow has occasionally indulged in a series of pressure instruments with a focus on energy policy, either by seizing control of the regional energy production as in the case of oil deposits of Azerbaijan and Kazakhstan, by providing gas and oil at cheap prices in countries which are of pro-Russian, or, finally, with the Russian control over energy infrastructures. The way in which Russia uses oil and natural gas in its foreign policy, it could be likened to the tactics of "carrot and stick". On the one hand, oil and gas are being used by the Kremlin to attract allies, either within the EU or in sensitive areas of the post-Soviet space. On the other hand, they are also being used to punish countries that oppose Russia, by temporarily freezing the flows of gas or through expensive price to individual energy agreements.  

11 Randall Newnham Oil, carrots, and sticks: Russia’s energy resources as a foreign policy tool, Journal of Eurasian Studies, 2011, pp.137-138
Undoubtedly, the most typical example of the aforementioned Russian policy is Ukraine. At times, Russia has interrupted the energy flow to Ukraine during the winter in order to bring Kiev closer to the Russian sphere of influence, keeping thus the primacy in its near abroad. It is also a way of forcing Ukraine to fall back in line or acquiesce with Russian demands. Similarly, the Kremlin, as of 2014, is providing Crimea with considerable financial assistance.

**TURNING EASTWARD**

As the EU strives to diversify its suppliers of energy resources, similarly Russia seeks to expand the list of its clientele turning to the energy hungry, rising Asian markets. The booming East Asian market highlights new opportunities. Thus a 30-year agreement was signed [between Russia and China, last year, for the construction of the pipeline «Power of Siberia», with the total volume of contract approximately at 400 billion $. It is estimated to carry about 100 billion cubic meters of gas annually. In the long term, any expansion of the Russian «pivot» to Asia would help Kremlin transform its symmetric energy interdependence with the EU, into an asymmetric and unbalanced one, upsetting the current status quo. However, in the short and medium term, the EU market will remain vital for Russia.  

---

13 TASS (2015) China expects Russia to supply 100 bcm gas annually — CNPC. Available at: http://tass.com/economy/824749
Of course, the Far East, correspondingly, having seen how the Kremlin exploits its role as a supplier, is expected to avoid excessive energy influence, especially after the emergence of Iran as a potential alternative source.

The chaotically extensive eastern side of Russia provides maritime access to the Pacific, as well as land routes to China and the Korean Peninsula. Of course it noteworthy that in this special relationship, Beijing has the upper hand, rather than Moscow, and China is expected to compel specific concessions, by taking advantage of the Russian need to diversify its clients. The introduction of the "Eastern Economic Forum" gave Russia a reliable platform exploring economic opportunities in the region. Undoubtedly, the energy sphere is the most vital aspect of these opportunities, especially regarding the three most dynamic Asian markets: Indonesia, China and Japan - countries that are closer to the hydrocarbon-rich eastern Siberia, from Moscow-itself. Indeed, , the rapprochement between Russia and Japan, a country that happens to be the fourth largest oil buyer worldwide, that has been in the making the past years, as an attempt to mitigate the importance of China as a buyer, is equipping the Kremlin with one more reliable alternative.15

---

14 Tyler Durden (2015), Russia, China Delay "Holy Grail" Gas Pipeline Sequel As China's Economy Swoons, Zero Hedge
Indicative of the mutual provision for deepening partnership is the fact that, even in the open 70-years long bilateral dispute over the Kuril Islands, it seems like we are closer than ever to a solution. Moreover, Japan, the world’s third largest economy, is an industrial country with non-existent raw materials deposit and an energy-hungry domestic demand. The tragic events of 2011 in Fukushima created a necessity for the Japanese to lessen their dependence on nuclear energy and seek alternate forms of energy, with predominant - for the time being - the gas solution. Thus Japan has already established itself as the largest importer of natural gas, surpassing even Germany. Mostly, Tokyo introduces liquefied gas (LNG). Russia, at present, is only the fifth largest exporter of LNG to Tokyo, following Malaysia (19%), Australia (18%), Qatar (15%) and Indonesia (12%). Aiming to catch up with the latest developments in the field of liquefied gas (LNG), Russia signed an agreement with Singapore last year for the sale of LNG supplies of Gazprom Group’s portfolio, while in the field of nuclear energy, emphasis was given to the last year's agreement between the Russian Rosatom and the government of Indonesia for the construction of nuclear reactors.

Finally, it is worth noting the fact that Moscow tries to invest in nuclear energy too, with particular emphasis in the Middle East, having already arranged agreements with Egypt, Jordan, Algeria and Saudi Arabia. Similarly the first nuclear reactor is being designed in Turkey, a plan with great geopolitical importance, although temporarily put on hold, in the aftermath of the episode last November.

MODERN CHALLENGES AND THE (DARKER?) FUTURE

Two main events have questioned the viability of Russian energy influence: The American shale gas revolution in 2011 and the sudden drop in oil prices in 2014. While those two events are neutralizing each other, they both demonstrated the inherent weaknesses of the Russian energy dependence. Moreover, major issues, such as the gradual transition to cleaner energy and the internal pathologies of Russian state oligopoly, contribute the overall spirit of uncertainty.

17 Sputnik (2015) Russia, Indonesia sign memorandum on building high-power, floating NPPs. Available at: https://sputniknews.com/business/201509171027132036/
The first one is expected to transform the global energy market, reshaping inevitably the whole geopolitical landscape. The United States as an energy self-sufficient country in the long run could be turned into an energy exporter, thus providing Europe with a reliable alternative.\textsuperscript{19} Aiming to that direction, the United States are already approving licenses for export facilities, while the building of LNG terminals.\textsuperscript{20} The construction of LNG terminals in Europe, would not only facilitate the American gas exports but will also increase supplies from North Africa and the Middle East.

However, in the short term, those changes are not expected to affect the Russian energy primacy, as the threat from Caspian seems bigger and more imminent.

It is, moreover, an inherent weakness of the Russian geo-economic power, the volatility that characterizes the energy prices level – as it has been demonstrated in recent years. When oil prices plummeted beyond any expectation.

In the case of the European Union, the creation of a single European energy policy, following the "Third Energy Package", would result to the emergence of a politically strong and united[European Energy Union], depriving Moscow of its hallowed practice of "divide and rule" that currently applies within the Union. However, given Europe’s own unresolved problems and the overall climate of disunity and deconsolidation, this is currently nothing but a scenario.

Still, despite the advantages that are deriving from the state control of the energy sector, the whole system itself contains some, far from negligible, shortcomings.\textsuperscript{21} Firstly, the natural gas giant Gazprom has lost in recent years its comparative advantage in terms of expertise, while unable to attract foreign investment. Correspondingly, Rosneft also requires modernization. Both firms, due to low competition, are also lagging in technology. Moreover, corruption is inherent in these companies, a problem which had for years covered by the lucrative energy market. In the fall, however, of the prices, the problem obviously has been revealed and is threatening now their viability.\textsuperscript{21}


\textsuperscript{20} Tim Marshall, "Prisoners of Geography", Elliott & Thomson Limited, 2016, page 19

Last but not least, under the framework of the Paris agreement and at a time when the international community urges for the intensification of the use of alternative energy sources, and calls for a transition to cleaner energy alternatives -with a view to prevent climate change- Russia should invest more in such energy forms in order to differentiate its highly dependent-on oil and gas- economy.

A liberal and inspired by the spirit of globalization criticism to the Russian energy policy would say that in a world where greater connectivity –and not territorial capacity- accounts for greater influence, the world's largest country is in danger of losing a great deal of leverage due to its entire dependence on commodity exports.

On the other hand, under the prism of a more traditional and realistic approach, Russia, despite its military might is still a vulnerable country. Military power is based on economic might and demographic growth. As the "demographic storm" is seriously infesting Russia, economic differentiation and adjustment to a new era through structural reforms, are of great urgency.

Overdependence in energy exports is an objective reality that needs to be reversed. Ironically enough, its main geoeconomic instrument may eventually turn against Kremlin.

---