Russia, Germany and European energy policy

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Created 2006-12-14 00:00

Energy policy has shot up the European political agenda in the last couple of years, as the realisation has dawned that the decades of cheap energy are over, and that external dependency is not only going up, but is increasingly focused on a worryingly small number of countries - Russia; in the middle east, on the trio of Iran, Iraq and Saudi Arabia; and in the Caspian ex-Soviet countries such as Kazakhstan, Azerbaijan, Turkmenistan, Chechnya (and again Russia and Iran).

None of these has, as yet, developed liberal open markets (or, indeed, full democracies) and, in almost all, raw political power rules energy policy. Getting access to some of these resources is complex, too, requiring pipelines which, in the Russian case, pass through Belarus and Ukraine (and with the new Baltic pipeline [1] will bypass the former Soviet satellites in the Baltic and Poland). In the Caspian case, the problems are even more complex, with a choice of routes between Russia, Iran or via Georgia and Turkey.

For Europe [2], Russia is the key to energy security. The dash-for-gas as the preferred fuel for electricity generation makes gas, rather than oil, the priority; and gas is cheaper through pipelines than shipped around the world in tankers for LNG. Russia has the pipeline gas that Europe needs.

It is not just that Europe has a growing dependency on Russian gas supplies; but also that Russia has a powerful hand [2] in influencing and controlling some of the major pipeline supply options - in particular, in the Caspian and the Caucasus. The other sources for European gas - Algeria and Libya - can watch the Russian moves and benefit from the higher prices and insecurity that result, and Norway, with its small population and more money than it can possibly spend, can husband its resources and enjoy the price level.

To date Europe has approached this growing dependency in two ways: by trying to persuade Russia to ratify the energy charter, and in particular to sign up to the Transit Protocol [3], which would open up access to Gazprom's [4] pipes (its dominant gas company); and by pushing on with liberalisation and competition policies within Europe. The former has failed [5]; the latter, though of merit, does little in itself to mitigate the external position. A third option - diversification to non-carbon sources, like nuclear and renewables, has yet to have made serious impact; indeed, Europe is primarily pursuing the gas option.

Europe's response

The failure to come up with a coherent [6] and credible European external policy towards Russia might not matter much if Russia was in any case going down the open market route and developing its democratic institutions in a way that made property rights bankable. But recent events have raised a question mark here, too.

The shooting of a leading journalist (Anna Politkovskaya [6]) in Russia, the poisoning of a former Russian security agent (Alexander Litvinenko [6]) in London, and the suspicious illness of a former Russian prime minister in Dublin (all so far unsolved) have added a sense of public unease, which has encouraged a more fundamental reconsideration of the energy relationship between the European Union and Russia.

This relationship had already come under strain in January 2006 when Gazprom turned down the gas supplies to Ukraine [6] (thereby starkly exposing Europe's dependency on Russian gas), and then again as Russia turned up the heat on Georgia [6] (a vital link in the lines of oil and potentially gas supplies from the Caspian).

Russia may have backed down quickly in the Ukrainian case, and indeed has had good reasons for trying to increase prices, but there can be little doubt that the episode - as with Georgia - has had a marked political impact. But murders with political resonance obviously create nervousness, and what makes them different in the Russian case is the combination of history, economics and energy.

Russia is now, in practical and political terms, a carbon economy: oil and gas dominate its economy, and the rise of President Vladimir Putin [7] has been closely correlated with the oil price rises since 2000. Indeed, Putin himself has written on the role of energy in re-establishing Russia's prestige on the international stage.

Moreover, with the re-nationalisation of natural resources, the monopoly established by Gazprom over gas pipelines, and the incestuous relationship between Gazprom's board and the Putin regime, the core role of energy has been cemented into the fabric of the Russian state.

Being pipeline-dependent, and with the natural outlet for Russian gas being Europe, the Russian approach has been twofold: to build up its relationship with Germany as the pipeline and contracting hub; and to squeeze the alternative supplies from the Caspian, by trying to continue the Soviet strategy of routing its exports via Russia, whilst frustrating alternative (non-Russian) outlets via (for example) Georgia. Whereas early squeezes on (oil) pipelines focused on Chechnya, now there is a more widespread competition for resource access in the Caspian area - from not only Russia and Europe, but also China, Iran and the United States (via Turkey).

The European Union has woken up to the seriousness of the situation, and with the Hampton Court summit [8] in October 2005, followed by the energy green paper [9] in March 2006, a series of sensible measures have been proposed - notably, reinforcing the interconnections within the EU and completing the physical infrastructure, and thereby not only gaining greater efficiency and security of supply internally, but also increasing resilience against external shocks and facilitating mutual assistance between member-states. Implementation, however, is another matter.

But what the EU really wanted was to be the external face in direct negotiations [10] with the Russians. This made sense at three levels: it would give real meaning to the solidarity that former eastern Europeans craved from membership (having experienced energy dependency in the raw during the cold-war era); it would prevent Gazprom engaging in divide-and-rule and hence confront a monopoly producer with real bargaining power; and it would provide a practical way for Europeans to see their commission playing an important role - especially in foreign policy.

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Also by Dieter Helm in openDemocracy:

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(11 June 2003)

"Russian gas, Ukraine and Europe's energy security [14]"
(20 January 2006)

"Russia's energy policy: political assertiveness or rational economics? [15]"
(17 October 2006)

A special relationship

This European Union approach has, however, been thwarted so far by national governments, some of which have pointedly wanted to keep energy as a national competence. At the heart of this has been the role played by Germany. It has pulled away from a community approach, developing its bilateral relations with Russia to such an extent as to have, in effect, a "special relationship" (though it fiercely resists this description [16]).

Like all such relationships, the form and content is multi-faceted, complex and deep. It has personal [17] as well as formal components. Thus, at one level, the Baltic pipeline, bypassing the eastern European member-states, provides a core physical link, and the Gazprom-Ruhrgas relationship is cemented in shares and contracts. At another level, Gazprom is a public and explicit critic of the commission's plans on ownership unbundling, making Ruhrgas's case for it, and at yet another, key politicians are directly involved.

Former German chancellor, Gerhard Schröder, is chairman [18] of the North European Gas Pipeline (NEGP), a project which he approved just before he left office. More personally still, Putin helped the Schröder family adopt Russian orphans. The warmth of that relationship echoes some aspects of that between Margaret Thatcher and Ronald Reagan in Britain and the US's "special relationship". Under Schröder's successor, the personal aspects are not on the same level, but nevertheless it is worth noting that the Baltic pipeline will come ashore in Angela Merkel's constituency in northeast Germany.

A two-way street

The German-Russian "special relationship" has economic interest at its core. Gazprom's position is a very rational one: monopoly control [19] of pipelines and therefore resources in Russia; a stable core partner for contracts; and a staging-post into Europe. For Germany, long exposed to energy insecurity, it has a natural dependency, and with the Baltic pipeline, it receives the rents from transporting gas which would otherwise have been shared out with eastern European countries. The decision to route the giant Shtokman [20] field through the Baltic pipeline (rather than via LNG to the US and elsewhere) is a further coup.

For Germany, this eastern perspective has a much longer pedigree, stretching back to the 19th century. In the cold-war years, *Ostpolitik [21]*, under Willy Brandt and Hans-Dietrich Genscher, was the natural forerunner of today's eastern orientation. The economic opportunities in this "new Europe" are immense, with its cheaper labour and high skills, and investment opportunities in Russian's carbon economy are similarly large-scale. For the export-orientated engineering and technology skills base of Germany, a "special relationship" with Russia is obviously attractive. So, for both sides, this is a national relationship to build upon.

The German "special relationship" is, however, quite a headache for Europe and the commission. It is in the middle of trying to negotiate [22] a new partnership and cooperation agreement (PCA) with Russia (the current one expires in December 2007) and its ambitions on the energy front are not helped by the bilateral arrangements being put in place. Indeed, within Europe, other countries are recognising that they have to try to catch up with Germany and form their own bilateral arrangements with Gazprom and Russia. ENI in Italy is well advanced with swaps, contracts and pipeline deals. Others are likely to follow. Europe is indeed being divided - the risk is that, in energy terms, it might be ruled too.

2007: Germany's twin presidencies

This conflict between national and European approaches towards Russia and Gazprom will come to a head in 2007. Germany then has the twin presidencies of the European Union [23] and the G8 [24]. Germany will preside over the commission's liberalisation plans, including possibly the proposal for ownership unbundling of networks within companies such as Ruhrgas, the development of the energy green paper proposals and the EU's post-2007 PCA or other arrangements with Russia.

At the G8, it will also have to broker the US-Russian energy relationships, and in both presidencies it will need to take the climate change agenda forward. Finally, to make matters even more complex, Germany will have to prepare the ground for resolving the EU constitutional issues, which are likely to make any further shift of powers to the commission in areas such as energy even harder to sell.

While all this European and global activity is going on, Germany will at the same time be continuing its own bilateral summits and arrangements with Russia. Thus, 2007 will be a testing year for Germany and the EU. There are wider political ramifications too. In the past, Germany has sought to bury its national interests in the European project. Indeed, that was part of the motivation for the creation of the European Economic Community (EEC) in the first place [25].

At reunification, François Mitterrand and Helmut Kohl strove to permanently anchor an enlarged Germany within Europe, and steps such as monetary union were part of that process. Now there is a further test - whether Germany can lead [26] Europe through its presidency towards a *European* energy policy, and the foreign-policy elements that accompany it, or whether it will let energy remain a national competence and allow Europe to drift into greater dependency without the necessary safeguards.

The first test will come in January 2007 when the commission tables its energy package [27]. Germany (and France) may want to defend their national champions from ownership unbundling and water down the commission's proposals.

The next test comes with the EU summit in March 2007, and the question of how to build on the 2006 energy green paper. The challenge here will be to focus on the completion of the European networks, and to move regulation towards a more European approach to their development and operation.

Then there is the question of strategic gas storage (which German companies oppose - along with many other large incumbents).

And finally there is the development of mutual support arrangements (which need the physical grid connections to be delivered).

Europe's opportunity

The worrying recent developments have opened up considerable opportunities. Recognition of the reality of Vladimir Putin's Russia [28], and in particular the rational monopoly strategy that Gazprom is pursuing, should disabuse most of the notion that Russia is about to open up its gas pipes to others. Recognition, too, of what is going on in Georgia and the Caspian, and the implications for southern non-Russian pipeline supplies, should alert Europeans to the importance of European foreign policy [29].

To meet this series of new challenges, Europe needs more than a set of national responses, however much these might be in individual member-states's narrow interests. That Germany is in the driving seat, both as Gazprom's hub [30] and with the presidencies, provides a timely chance to prepare Europe for its future energy dependency, and to better align its internal energy market reforms with the external challenge.

But at stake is much more: if Germany fails to go down the European path, it will be a break with one of the deep political objectives of the EU, and it will show the sceptical voters of Europe that the EU cannot deliver in an area of such vital interest. Energy is where a significant part of the case for greater European integration may be won or lost.

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