The dynamics of natural gas supply coordination in a New World
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Document Version
Publisher's PDF, also known as Version of record

Publication date:
2010

Link to publication in University of Groningen/UMCG research database

Citation for published version (APA):

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Chapter 11

The geopolitical boundary solutions to strategic collusion

11.1 Introduction

At the firm level, Gazprom can end up in different European gas market outcomes as a quasi-monopolist, a dominant or non-dominant firm, involving varying degrees of over- and under-supply. From an economic perspective, such scenarios may lead Russia to invest strategically or not. At the level of the Russian government, Gazprom’s decisions are guided by factors which go beyond economic rationale when it comes to geopolitical forces. The case studies in Chapter 9, together with Chapter 10, pertain to the economic fundamentals of the problem; this chapter is designed to add another dimension to the real-option game and toolbox-based approach, namely the additional geo-strategic and geopolitical complexities that come into play because of Russia’s position in the international political system and how it perceives that system.

As was explained in Chapter 3, shifting Russian perceptions of US intentions and actions in and around Russia’s periphery in zero-sum terms influence Russia’s course of action. An important question is whether Russia can truly wean itself off of its zero-sum view of the outside world and move towards one involving relative advantage and interdependence where both rivalry and cooperation exist. Developments described in Chapter 3 show that regionally, within the post-Soviet space, Russia perceives the world in zero-sum terms. However, with regard to gas-consuming, Russia faces its interdependence with other geo-strategic players (e.g., EU countries and the US), home to important gas export markets. Russia is also interdependent with other gas-exporting countries.

As was argued in Chapter 3, US geo-strategic ambitions are based on a drive to secure a diversification of gas flows in and away from the Eurasia gas ellipse. For Russia such a US ambition comes as a geo-economic threat, and if successful, the US could undermine Russia’s ability to secure its gas interests both in the post-Soviet space (in terms of volumes for Russia’s own needs) and in European gas markets (in terms of lost income). Ultimately this could have adverse consequences for Russia’s economic security. The geopolitical dimension of gas flows can be appreciated by perceiving Eurasia as one vast chessboard in which the various geo-strategic players jostle for potential gas flows from the Euraisan gas ellipse.
Based on what we know from chapters 2 and 3, the US will counterbalance Russia geo-strategically in Eurasia. Russia’s perception of the US as a geo-strategic competitor may induce Russia to compete geo-strategically with the US. The impact at the political level of Russia’s strategic investments on market structures in European gas markets offers Russia a means to compete geo-economically and geopolitically with the US in the rimland. From an economic and geopolitical point of view, the option to compete with other gas-exporting countries may seem warranted, especially if Russia wants to compete with the US for influence in Europe. What then are the implications of the above for cooperation between gas-exporting countries? Russia faces an important dilemma: is it going to compete with other gas-exporting countries or not, given its geopolitical inclinations?

If avoiding gas market oversupply is an important motive for cooperation of some sort amongst gas-exporting countries, then the question remains: What form of cooperation is most desirable and feasible for Russia, given the nature of regional and interregional gas market(s)? The answer to this question should be held in the light of Russia’s perceptions of the outside world. What form of horizontal energy diplomacy, so to speak, is then most suitable from a Russian point of view, given its position in and perception of the international political system?

11.2 Western challenges to Russia in the Eurasian gas ellipse

Aiming to secure its position by influencing the emerging geo-strategic dimension to gas flows as a result of the changing international political system, the US seeks to create spheres of influence in Eurasia. It does so in order to prevent one single power or coalition of land powers from dominating the Eurasian continent. This is done either in the form of military and economic alliances or by establishing key regimes which are politically receptive to US policies in the rimland.

Before assessing the impact of Russia’s perception of the international political system on its possible cooperation with other gas-exporting countries, we must acknowledge the geographical scale at which the West seeks to undermine Russia’s position in the Eurasian gas sphere. From a realist and geopolitical perspective, the US will not sit by idly and allow Russia to strengthen its hand in Eurasia (by extension of what was discussed in Chapter 2). A Russian ability to aggregate and/or guide gas flows in Eurasia, and the effect of Russia’s pipelines on

550 The term used here is ‘Euro-Atlantic’ in this context because today, there is not only a US drive to ensure Europe’s gas supply diversity (also refer to Chapter 1), there is also an EU-level drive, in part encouraged by the US.

552 As early as 1992, the US Defense Planning Guidance had as one of its main objectives the prevention of the re-emergence of a new rival to the US. The guidance went on to argue that in order to achieve this objective, the US would have to prevent any hostile power from dominating a region whose resources would be sufficient to generate global power [Clarke and Halper 2005].
geopolitical relationships between the US and its Eurasian allies, comes as an important challenge to US power in Eurasia. It upsets the balance of power in Eurasia: Russia would be able to gain control over concentrated economic-strategic resources in Eurasia and expand its geopolitical influence in the rimland (e.g., in Europe).

Recently, however, the Obama Administration appears to have softened its stance on Russian gas in Europe. Bressand [2010], for example, argues that "the Obama Administration’s effort to ‘reset’ relations with Russia has reduced the divergences of views between key continental European countries and the US regarding the risks associated with dependence on Russian gas. Washington’s all-out opposition to the Nord and South Stream pipelines has been replaced” by an effort "to engage Russia constructively,” as stated by Richard Morningstar, the US Special Envoy for Eurasian Energy [Wall Street Journal Europe, 2009]. Be that as it may, the current geo-strategic posture of the US conveys that it seeks to directly control the rimland, especially the Eurasian ‘middle ground.” This region provides the main gateways to central Eurasia (i.e., Central Asia and its surroundings) and is wedged between Eurasia’s major powers, Europe, Russia, China and India. The US drive to diversify gas flows from the Eurasian gas ellipse and to curb the dependence of its European allies on Russian transit is a geo-strategic given for Russia, whatever its desired course of action. While Russia aims to increase its options (i.e., export routes for gas flows), the Euro-Atlantic community seeks to reduce Russia’s and increase its own, with the US is an important driving force.

Gateways enable a diversification of gas flows from the Eurasian gas ellipse while also ‘servicing’ US allies in Europe with non-Russian gas, and breaking Russia’s monopoly of influence in the region. The establishment of greater control over the transport of oil from the Persian Gulf region and the Eurasian middle ground, as well as EU and NATO expansion, provide the US with a firm foothold in the rimland. The rimland can be used as a staging ground for a further diversification flows from the Eurasian gas ellipse.

There are two areas of interest for the US within the Eurasian gas ellipse: the Central Asia and Persian Gulf regions, which contain the vast bulk of conventional gas reserves in the ellipse outside Russia. In Central Asia, key to the US strategy in the resulting ‘pipeline politics’ has been drawing up pipeline routes through pro-US countries in the rimland and skirting the territory of possible or actual geo-strategic rivals such as Russia and Iran (e.g., the SCP and BTC pipelines), by using the aforementioned gateways. What began as the ‘new great game’

333 The Eurasian middle ground corresponds with a region inside the rimland lying between Europe, parts of the Middle East, Russia and East Asia, i.e., southern Central Eurasia, Iran, Iraq, Afghanistan and Pakistan.
334 Gateways are discussed in Chapter 2.
335 For any eventual US hegemony in Eurasia, the tying in of the Ukraine and the Caucasus countries is vital, being important pivots, both in terms of energy corridors and as areas for force projection [Brezinski 1997].
during the 1990s, i.e., a competition for access to oil and gas in the post-Soviet Caspian Sea region, has grown to become a geo-economic competition for gas flows from the Eurasian gas ellipse, refer to Map 11.1 below.

11.2.1 Gas flows from the Caspian Sea/Central Asia regions

The main geo-economic prize for the US in undermining Russia’s economic security is Central Asia, specifically the Caspian Sea region (c.f., the heartland) upon which Russia relies for gas volumes (see Chapter 6). The region’s central geographical position provides it with a unique capability to supply pipeline gas to Russia, Europe, Asia and the Middle East [IEA 2009b]. As was explained in Chapter 6, this region plays a pivotal role in Russia’s gas supply portfolio. Since 2001 the region has been firmly fixed in a US-NATO effort to ensure a long-run Western presence in Central Asia [Zhiznin 2007]. US and NATO forces are likely to remain for the long-term to keep options open in this regard [OSCE 2006].

From Russia’s perspective a US strategy aimed at diversifying gas flows from the Caspian Sea region can undermine Russia’s economic security as ‘diverted’ gas flows, originating from Central Asia and the Caspian Sea would no longer flow to the Russian domestic market. The domestic gas market, as was mentioned in Chapter 3 is an important obligation for Gazprom because it is a political priority for Moscow, while in addition Central Asian gas flows allow Russia to export volumes to European gas markets. This in turn compels Russia to develop its domestic gas resources in Yamal, for example, an investment which is likely to also require exports to Europe and elsewhere by pipeline or LNG. Oversupply could again result because of the sheer size of volumes likely to be made available from investment in Yamal’s resources. Hence gas flows in Eurasia are ‘driven’ as much by geo-economic forces as they are by geopolitical ones.

Traditionally Central Asia’s energy holdings are restricted to Russia according to the US perspective, they could not exercise effective economic or foreign policy independence, and the US thus supports the independence of the Caspian Sea littoral states [Blank 2007]. With the advent of China in the region, this situation has changed. For the US (and the Euro-Atlantic community), equal access for western firms therefore relates strongly to the larger objective of safeguarding these states’ independence, sovereignty and prospects for secure development. In the case of the Caspian Sea/Central Asia region, securing upstream access has no value unless viable alternative export routes are developed to transport gas flows. In the US view, control of

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536 The new great game involves a complex interplay between the Central Asian and Caspian Sea countries, neighbouring countries such as Iran, Turkey, Pakistan as well as extra-regional powers such as Russia, India, the EU, the US [Amineh 2003] and more recently, China. For more on the evolution of and details concerning the ‘new great game’ see Amineh [2003], Olcott [2006], CIEP [2004], Dekmejian and Simonian [2005] and Klevemann [2005], amongst others.
transport routes themselves is important to its own power base in Eurasia. US policy is thus geopolitically tainted rather than purely commercial.\textsuperscript{537}

The Azerbaijan–Georgia–Turkey corridor, which was spearheaded by US ties with Azerbaijan, is the first exit corridor established by the US after the fall of the Soviet Union. Case study 1 in Chapter 9 touched upon the complexity of this case and the role of the US in facilitating this corridor. Brzezinski refers to Azerbaijan as "the cork in the bottle containing the riches of the Caspian Sea basin and Central Asia" [Brzezinski 1997, p. 47].\textsuperscript{538} It became the centre of a wider post-1991 US campaign to secure oil and gas flows, which by-passed enemies such as Iran and would break Russia's standing monopoly on these flows [CIEP 2004].\textsuperscript{539} Turkey, a NATO member, and Georgia, also both played a pivotal geo-economic role in facilitating the construction of the BTC and SCP pipelines.\textsuperscript{540}

During the 1990s, the US became a strong proponent of the trans-Caspian gas pipeline, which would act as an extension of the trans-Caucasus pipelines into Central Asia [Dekmejian and Simonian 2003; Aminieh 2003; CIEP 2004].\textsuperscript{541} The US has been keen to persuade President Berdymukhamedov of the benefits of a gas pipeline to carry gas across the Caspian Sea to European markets [MEES 2007b].\textsuperscript{542} In 2008, the US stressed the importance of diversifying Europe's gas imports because "Gazprom is rapidly gaining control of both the supplies and the transmission lines and they will soon encircle Europe," emphasising the importance of the

\textsuperscript{537} The symbolic and political value of the corridors, transiting across countries in a region still bearing the marks of the Soviet era, outweigh the economic costs involved [OSCE 2006]. However, the US government has had to pressure IEFs to invest in pipelines they do not wish to invest in, because of the costs and risks involved; the IEFs require a stable investment climate in order to achieve their commercial objectives and secure their investments [CIEP 2004].

\textsuperscript{538} Indeed, Azerbaijan's location is important because the "independence of Central Asian states can be rendered nearly meaningless if Azerbaijan becomes subordinated to Moscow's control." Azerbaijan's own and very significant oil (and gas) resources can also be subjected to Russian control, once Azerbaijan's independence has been nullified," and Brzezinski goes on to note that, as far as Russian influence is concerned, "[a]n independent Azerbaijan, linked to Western markets by pipelines that do not pass through Russian-controlled territory, also becomes a major avenue of access from the advanced and energy-consuming economies to the energy rich Central Asian republics. Almost as much as in the case of Ukraine, the future of Azerbaijan and Central Asia is also crucial in defining what Russia might or might not become" [Brzezinski 1997, p. 47].

\textsuperscript{539} Indeed, the driving force behind US policy in the region is anti-monopoly while the driving force behind Russian (and Chinese) policy is quintessentially monopolistic in nature [Mann 2006]. The objective of US policy-makers is not only to obtain oil and gas from Central Asia but also to control the flow to oil and gas markets in the West and in Southeast Asia [CIEP 2004].

\textsuperscript{540} This corridor helps explain American enthusiasm for Azeri membership of NATO, which would further help embed Azerbaijan in a pro-US nexus in the Caucasus from Baku to Turkey, creating a solid transit link for the corridor itself and forestall the formation of a possible Russian-Iranian alliance or strengthening thereof, whether of an energy-related, economic or political nature [OSCE 2006].

\textsuperscript{541} The legal status of the Caspian Sea, the broader geopolitical complexities of the region and Russo-Iranian cooperation as well as the role of Blue Stream (as was discussed in Case study 1 in Chapter 9) have all so far combined to impede any further progress on the trans-Caspian route.

\textsuperscript{542} In 2007, the US was even willing to finance trans-Caspian feasibility study, following Russian moves to secure Azeri and Turkmen volumes earlier that year.
trans-Caspian option along with Nabucco as alternatives to South Stream [PIGR 2008j]. Tense relations between Azerbaijan and Turkmenistan over their shares of the Caspian Sea have also aided in stalling any discussion about the pipeline. The trans-Caspian corridor, together with the trans-Caucasus corridor, could offer long-term prospects for increased European dependence on Caspian Sea/Central Asian gas and reduce European dependence on Russian gas [MEES 2008e].

While the trans-Caspian gas corridor, starting with the SCP, offers one way out for Caspian gas, the TAPI pipeline offers another way, albeit speculative at this stage (also see Chapter 6). The TAPI has been back on the table since the Taliban’s ‘removal’ from power in 2001, with the US keen to promote the TAPI pipeline as a means of enabling Central Asia to reduce its economic dependence on Russia. The pipeline is an alternative to the rival IPI project (see Chapter 6), as the US also seeks to isolate Iran [PIGR 2008i]. Iran (under a pro-US regime) and Afghanistan offer interesting prospects for bringing oil and gas from the Caspian region to the Indian Ocean, and to potentially important US allies outside the NATO alliance such as Pakistan and India. The call among US policy-makers and military planners in 2009 for more US and NATO troops [Financial Times 2009g] supports the view that the US is determined to maintain its position in the region by supporting an important pro-US regime in Afghanistan.

At stake for the US is an important foothold in between Central Asia (in the heartland) on the one hand, and Pakistan and India (in the rimland) on the other; a geo-strategically vital area of influence. For the US and its NATO allies, the perceived geo-strategic stake is high in the quest to maintain a long-term presence in the energy-rich Central Asian region (and within the Eurasian gas ellipse), where Afghanistan offers long-term prospects for a US presence on the crossroads between Central Asia, the Middle East and East Asia [Jalalzai 2003].

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543 Azerbaijan and Turkmenistan enjoy improved relations as of late, particularly since the advent of Niyazov’s successor in Turkmenistan [MEES 2008e].
544 Resolving the legal status of the Caspian Sea would form a crucial, initial step in this process.
545 The establishment of the Baku-Tbilisi-Ceyhan (BTC) pipeline and the South Caucasus Pipeline (SCP) bear witness to this strategy.
546 An important potential geopolitical pivot for the Soviet Union, Afghanistan lies roughly placed on the imaginary border between the Heartland and the rimland, immediately to the South of the Soviet Union in the rimland. This provides Afghanistan with immense geo-strategic importance for any foreign power and has indeed long been the site of geopolitical competition. The Soviet Union did not invade Afghanistan merely for an ideological cause; the geo-strategic stakes were high too. Remarkably, Yuri Andropov, Head of the KGB at the time of the Soviet incursion in Afghanistan, believed the US was planning to use Afghanistan and a pro-US Iran and Pakistan as part of broad new front against the Soviet Union in the south and to push into Central Asia from that region [Brezinski 1997]. Conversely, the US believed the Soviet Union was bent on using Afghanistan as a platform for eventual domination of the Persian Gulf (in and of itself a weakening of American influence in the Rimland).
547 While the battle to defeat the Taliban rages on for the US and its NATO allies, energy interests continue to play an important role in the background. The US has already established permanent bases in Afghanistan and many in US policy circles see US and NATO presence as permanent [Lutz 2006].
Support activities of Russian
At member state level: provide
Stoking an 'energy security'
Joint ventures with European
Possibly discourage Russia’s
Exploring downstream activities in
Re-integrate security presence in CIS
From Caspian to Europe/Turkey
CDC as an EU instrument to
Cooperation between China and
At member state level: provide
From Central Asia via Russia to
Support pro-US regimes
Pursuit of possible deal with
Support for Nord and South
(“serving” upstream
“serving” European allies with
Financial support through IFIs
Perhaps from Azerbaijan to
Support pro-Russian regimes
“Buying” Russian and Chinese gas
Russian support for Gazprom in
Limit and/or contain dependency
Gas flows serving
Russian interests
Gas flows serving
Euro-Atlantic interests
Gas flows serving
Chinese interests
US military facility/base

Eurasia and North America:
Main political, economic and
security alliances

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<td>Pro-US regime</td>
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<td>‘Rogue’ state (vis-à-vis the US)</td>
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Other symbols

Gas flows serving
Chinese interests

Map 11.1 Geopolitical spheres of influence, forces and gas flows

Notes:
- Scheme & overview
- Map only includes relevant institutions and topics for this dissertation

Source: own analysis, institutions’ websites; expert interviews

A PDF version of this map is available at <http://www.clingendael.nl/ciep> for magnification purposes only

World Map Template: © by Le Monde Diplomatique

A PDF version of this map is available at <http://www.clingendael.nl/ciep> for magnification purposes only
11.2.2 Gas flows from the Persian Gulf: Iraq and Qatar

For the US, the Persian Gulf region in general, and Qatar in particular, is an immense source of potential gas flows. By pipeline (e.g., Iraq) and LNG (e.g., Qatar) these two countries act as a potential counterweight to Russia’s pipeline gas dominance of European gas market(s). In addition, flows from Iraq and the Persian Gulf to Europe could also help service other US allies in the rimland. The American on-the-ground military presence safely lodges Qatar in the US sphere of influence (which does not preclude Qatar from cooperating with other gas-exporting countries or companies). With the decreasing need in the US for LNG imports, there is less emphasis on maintaining energy security in the Gulf for LNG tanker traffic. Nevertheless, oil supply security, the potential geopolitical threat of Iran, and long-run interests in the Eurasian middle ground provide the US with sufficient reason to keep Qatar within its sphere of influence as a geo-strategic lynch-pin for US Central Command (CENTCOM). Exxon Mobil’s close partnership with QP certainly goes hand-in-hand with a strong US military presence in Qatar, protecting it from regional rivals such as Iran.

Despite post-2003 instability in Iraq, it is now in the US sphere of influence. With considerable Iraqi gas reserves, the playing field has been levelled for foreign investments (also see Chapter 7), notwithstanding difficult upstream conditions for the firms in question. In ‘rimland’ terms, the 2003 Iraq war fits into the wider geo-strategic vision the US has of controlling the Persian Gulf region and securing the most important oil reserves for the long-run. Besides the political developments in Iraq, geopolitical forces in the region at large should also be taken into account. From a geo-economic point of view, Iraqi gas flows to Europe have become plausible since the removal of the Hussein regime in 2003. In the geo-economic competition for the Eurasian gas ellipse, this has tilted the playing field in favour of the Euro-Atlantic community in the long run.

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548 In the case of the Persian Gulf, transport is less of an issue since LNG is free of transit issues, though the Strait of Hormuz bedevils tanker traffic from the Gulf. Iran’s position vis-à-vis the Hormuz Strait is one of the reasons why Iran forms an important bottleneck for US policy in the region and a major security threat.

549 Iraq offers potential gas for Europe in the longer run, as Matthew Bryza explained: “the US, Turkey and government of Iraq have a trilateral working group […] that aims to lay the foundations for investment in Iraq’s gas sector to get its [gas] production going and complement Azerbaijan’s production for a project like Nabucco, or the Turkey-Greece-Italy pipeline” [AGC 2008b].

550 For the US, Iraq and the possibilities for privatisation of some of the largest untapped oil reserves in the world, could also potentially undermine OPEC’s ability to regulate the oil market In the long run [Boon von Ochusée 2006]. Regime change in Iraq became necessary in the US calculus for geo-strategic reasons as well, centring on concerns about preserving Israel’s power base in the Middle East, securing access to oil reserves and flows and containing Iran’s regional ambitions [Noreng 2008]. As former US president Carter notes: “[T]here are people in Washington […] who never intend to withdraw military forces from Iraq and they’re looking for ten, 20, 30 years in the future […] the reason that we went into Iraq was to establish a permanent military base in the Gulf region, and I have never heard any of our leaders say that they would commit themselves to the Iraqi people that ten years from now there will be no military bases of the United States in Iraq” [CNN Larry King Live 2006].

551 Consider the ability of Iran to affect Iraq’s stability and sovereignty, as well as the geopolitical roles of neighbouring countries such as Saudi Arabia and Turkey with regard to Iraq.
11.2.3 The role of the EU and the European powers

During the 1990s it was the US which became an important geopolitical and geo-economic factor in Eurasia and, specifically, in the post-Soviet space. The expansion of the EU to include 27 member states in 2004, and a neighbourhood policy that now overlaps with Russia’s near abroad policy, has already made the EU a new player in the post-Soviet space. Hence, alongside the US, the EU has become a more independent actor with soft but relatively few hard powers. EU-level initiatives, such as the ‘Southern Corridor’ and the CDC (see Case study 2, Chapter 9), which run parallel to US drives to create alternative gas flows from the Caspian Sea region to Europe as discussed above, bear witness to Europe’s efforts to formulate an external gas strategy. The EU was hitherto mostly concerned with internal developments such as absorbing new member states (which the EU still struggles with today) and the development of an internal gas market. European views however have become more receptive to rhetoric about over-dependence on Russian gas and this catalysed a ‘security’ debate over the matter after the 2006 Russia-Ukraine gas row [Saunders 2008].

The Southern corridor: Gas from both the Gulf and Caspian by pipeline to Europe

While the US advocates its own gas transport corridors, the EU also toys with import route diversification schemes, primarily embodied on paper by the so-called ‘southern corridor’ and the CDC. With EU expansion, and new possibilities for gas exploration and production in Iraq, the geo-economic significance of Iraq and the Caspian Sea increased. The so-called ‘southern corridor’ is the EU’s latest pet project to tie in gas flows from Azerbaijan via the Caucasus (Shah Deniz, phase II), and from the Persian Gulf region. A vast arc of gas resources can thus be accessed by the EU, with the main conduit potentially being the Nabucco pipeline. So far this pipeline lacks a gas reserve base. Ideally, the Nabucco would bundle supplies from all these countries. While Nabucco has been on the drawing board for a number of years, the notion of Iraqi gas supplying Europe is new (as discussed above and in Case study 2, Chapter 9). Interconnections between Nabucco and the AGP are also on the drawing board. EU energy ambitions have come to lead a life of their own in spearheading the discussion over gas from the regions mentioned above, transcending US influence there.

11.3 Towards strategic and ad hoc collusion

From the section above, and given what we know about Russia’s gas interests in the post-Soviet space and in Europe, it is clear that Russia faces a geo-strategic challenge from the US. In Russia’s view, the US seeks to undermine Russia as a geopolitical power in Eurasia. The analysis carried out in chapters 8 through 10 point to the economic underpinnings of deciding whether or not to compete, in which Gazprom’s perspective was taken. Various forms of coop-

\[\text{Saunders 2008}\].
eration between gas-exporting countries at a firm level and other related aspects were discussed in Chapter 10. Yet another leap is needed to arrive at the issue of whether or not Russia, at the government level, is willing to cooperate with other gas-exporting countries. This hinges on Russia’s perception of the outside world.

11.3.1 Competition versus cooperation: Russia’s ideas

Russia may ultimately proceed with investing strategically, and thus compete with gas-exporting countries at large, because of the following main points:

1) Scenarios in which Gazprom ends up with a greater market share and thus a greater income, in and of themselves enhance Russia’s economic security. This security buttresses Russia’s state coffers and enhances its relative advantage in the international political system. This is a particularly attractive option if Russia perceives the structure of the international political system in Hobbesian terms.

2) The resulting increased gas import-dependency of its European markets (as a result of the realisation of an aggressive investment policy), and the countries through which and to which its gas pipelines are laid (and the gas which flows through them), offer Russia further political currency with the relevant governments on the receiving end of the value chain. Positioning itself as aggregator of gas resources in Eurasia provides Russia with geopolitical strength vis-à-vis the US. Proceeding with its strategic investments along the entire gas value chain, including the mid-stream pipelines discussed in Chapter 9 may, in Russia’s perception, strengthen its position as a geo-strategic player.

From a geo-economic perspective, the SSEE market is the most sensitive sub-regional European market for Russia, given the points above. It is imperative that Russia keeps out potential flows from Iraq, Iran and the Caspian Sea region, because the gas reserves of the ellipse could lead to important market share losses, particularly if transported by pipeline. As Case study 2 has demonstrated, the South Stream is endowed with a special geo-strategic, rather than only economic-strategic value by making such pipelines obsolete when built on time.

From competition to cooperation

The development of the interregional gas market and separate regional gas markets bear witness to the increasing interdependence of gas-exporting countries’ export ambitions. As illustrated in Chapter 10, if other gas-exporting countries also decide to invest strategically, gas market oversupply can result. Rather than being strengthened, Russia’s economic security would be weakened, as would its aspiration of resurrecting its position as a geopolitical player. Gas market oversupply could jeopardise Russia’s domestic economic situation, which it has tried hard to stabilise during the 1990s. Russia may wish to gain a greater market share, but the threat to its economic security, because of the prospect of gas market oversupply, should
compel it to seek cooperation with other gas-exporting countries if it wishes to protect its economic security.

Russia is dependent on gas markets (and other geo-strategic players) for gas export revenues. Additionally, Russia must take this world of interdependence into account. Chapter 3 illustrated that at a global level, Russia is aware of its interdependence with other geo-strategic players. The Russian energy diplomacy within the GECF and the Troika further highlight its preparedness to cooperate with other gas-exporting countries. Russia’s identity as a great power will determine the shape and form such cooperation may take later on in time, as will be argued below. Because Russia increasingly perceives the world in terms of relative advantages, cooperation with other gas-exporting countries is an attractive option for Russia, both at the country and at the firm level.

11.3.2 Barriers to binding, open and explicit cooperation
If Russia chooses to cooperate because it successfully perceives and acknowledges its interdependence with other gas-exporting countries, then what shape is likely to be most suitable according to the Russian perspective? At face value, cooperation may seem desirable to avoid oversupplies. However, Russia may perceive formal, binding commitments to cooperate as an option that could undermine its policy independence [Finon 2007]. As Stern notes, the impetus Russia has given to the GECF and its joint foundation of the Troika with Iran and Qatar compels a reassessment of earlier dismissals of the GECF as an organisation lacking any substance [Stern 2009]. As discussed in Chapter 7, Russia has taken a more active role in the GECF and co-founded the Troika in the period 2006-2008. Ultimately, how these organisations will evolve and develop in the future, depends on how Russia behaves as a great power. The fact that Russia’s is the biggest (conventional) gas reserve-holder in the world definitely plays an important role in this respect.

For Russia, cooperation with important gas-exporting countries in and outside the gas ellipse translates into political power because of Russia’s ability to gain influence vis-à-vis the US in the rimland. Such cooperation also enhances Russia’s bargaining position vis-à-vis the EU. The possibility of organising political cooperation and cohesion through common interest in a comparatively new dossier, i.e., in the sphere of an expanding but uncertain, interregional gas market, offers Russia additional international political clout. International, horizontal energy diplomacy may therefore prove to be expedient, as long as it does not affect Russia’s sovereignty. A number of barriers to open and formal cooperation à la OPEC persist. Depending on gas market and political developments, cooperation in the interregional gas market may
develop tacitly\textsuperscript{552} or become more explicit. Below it is argued why, from a Russian perspective, cooperation is likely to remain ad hoc:

1) \textit{Cost of maintaining long-term binding commitments}

From a theoretical point of view, lasting and formal collusive outcomes are notoriously unstable, especially because binding commitments are required (see Chapter 4). In the interregional gas market, very long-term commitments would be needed to sustain effective collusion across all regional and interregional projects [Finon 2007]. Parallel behaviour and tit-for-tat signalling also offer means to collude, short of full cartelisation. The geopolitical complexities involved, as discussed above, also make binding commitments difficult to achieve. In addition, if Russia were to play the role of a swing supplier in a more liquid European gas market, it would have to bear the significant costs inherent to being a balancing supplier just as Saudi Arabia does in the oil market.

2) \textit{Policy independence}

A Russian desire to maintain its policy independence and its self-perception as a great power may incline it to refrain from full, formal cooperation (rather than merely as a regional, less comprehensive power such as Saudi Arabia as far as the world oil market is concerned) [Finon 2007]. Russian leaders prefer to adopt an independent energy policy without limiting their choices by joining a collective grouping [Bahgat 2009]. Russia’s arm’s length cooperation with OPEC (and, at times, its tendency to expand production when OPEC withholds volumes), as well as its refusal so far to join the oil cartel points to Russia’s desire to steer an independent course [Nefte Compass 2009].\textsuperscript{554} Consider how Russia has attended OPEC meetings as an observer, and informally attempted to influence deliberations, without actually being a member and without carrying the burden of being a swing supplier [Finon 2007]. Russia has also tried to strengthen its influence on OPEC’s decision-making by promoting bilateral relationships with individual OPEC member states [Elass and Jaffe 2009].\textsuperscript{555}

\textsuperscript{552} As opposed to formal forms of cooperation such as OPEC, tacit collusion is more politically expedient and better suits the rather divergent nature of interests between the various gas-exporting countries, also refer to Chapter 4 for a definition of tacit collusion.

\textsuperscript{554} It is worthy to note that during late 2009, Russia is reported to have exceeded oil production levels it agreed upon with OPEC amid a period of dampening oil prices in 2008-2009, with the structure of the Russian oil market also being an important factor to take into consideration (also see Chapter 3) [Gulf News 2009]. Besides, unlike many OPEC countries, which have only one NEF and thus have more direct and simple control over their oil sectors, Russia has two government-controlled National energy firms in its oil sector while the remainder is outside the control of the state. On other occasions as well, Russia preferred to act unilaterally in deciding upon oil production vis-à-vis OPEC, free riding on the back of efforts to restrain production by the oil cartel (e.g., in 1999 – 2000). Russia’s behaviour with regard to OPEC in oil market is telling. This behaviour points to a Russian desire to act independently of what courses of action other oil and gas producing and exporting countries recourse to, notwithstanding the economic circumstances.

\textsuperscript{555} Russia monitors OPEC specifically to prevent adverse impacts on its decisions on Russian crude exports and maintain price stability [Lee 2007].
From a historical point of view, OPEC agreements have only been truly successful from a supply point of view on a limited number of occasions [Van der Linde 1999]. The advantage of the Troika is that it includes very few members able to possibly influence the geography of the interregional gas market in the very long-run (beyond 2020-2030). With few very large (potential) players in the interregional gas market, it is easier to collude and make agreements on strategic investments than it is in cases involving a greater number of members in other oligopolistic settings. Even a slight increase in the number of players tends to vastly increase coordination difficulties and encourages cheating. Through pipeline-for-LNG swaps in the short run, and agreements of a more long-term nature (see Chapter 10), Russia and Qatar alone can have a considerable impact on the structure of the interregional gas market by calibrating their activities in Asia-Pacific region and Europe, leaving the US as a residual LNG market.

Russia’s self-perception as a great power that pursues its own goals and objectives independently of other countries goes hand-in-hand with its self-perception as the largest conventional gas reserve-holder. Possible cooperation with other gas-exporting countries fits into a wider framework for Russia, in which the power it derives from its position as a powerhouse in the gas world is can be used as a bargaining chip in other dossiers. Russia requires room in its policy-making in the gas sphere in order to have the freedom of manoeuvre to gain or make concessions on other matters of importance to its international standing.

3) Diverging interests of the top three gas reserve-holding countries

The membership of the GECF is large and therefore politically cumbersome [Jaffe and Soligo 2006]. This may point to a motive for Russia to set up the Troika: maintaining its ties in the sphere of potential cooperation with the limited number of the world’s top gas reserve holders. In and of itself, this points to Russia’s ostensible preference for tacit collusion. With such a small grouping, formal agreements are less necessary than is the case when many actors are involved. Whatever the shape and form of collusion that best suits the rigidity of the interregional gas market in the long run, with Russia as an important actor herein, relations between Russia and Iran and between Russia and Qatar (i.e., within the Troika) are of crucial importance in the long run. Relations with Qatar may well be strongly influenced by that country’s relationship with the US, thus possibly complicating or acting as barrier to Russia’s scope for cooperation with this small sheikdom.

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556 After a meeting between Russian and Qatari gas delegations, Gazprom issued a statement saying it had discussed the ‘high potential’ for LNG deals with QP, as well as pipeline gas sales to Europe and Asia [WGI 2010d].

557 Bilateral Russo-Iranian cooperation (also see Chapter 6) is more of a tactical nature than a form of long-term strategic congruence or a hard alliance [Amineh 2003]. It is difficult to establish whether Iran and Russia may act as rivals or partners on a permanent basis, they likely to remain loosely partnered. Given the geopolitical and geo-economic relationship of Russia and Iran alone, as well as their sway over Central Asia, a hotly contested region for involving ‘pipeline politics’ (also see below), cooperation between these two countries predisposes collusion in the interregional gas market to geopolitical as well as geo-economic forces.
Both countries’ interests may diverge widely: Qatar’s reserves are very high relative to its population size, and the need to maintain output to generate revenue is not as urgent as in Russia’s case. In addition, Qatar’s heavy reliance on LNG exports provides it with much more flexibility than Russia, which for now mostly relies on pipeline gas exports [Bahgat 2009]. For Russia, Iran may act either as a rival or as a potential partner, the line between cooperation and competition between Russia and Iran may prove to be very thin depending on market or geopolitical circumstances [Lee 2007] (also see Chapter 6). There is no guarantee both countries may not seek to compete for gas flows and markets in the future [Finon 2007]. Qatar also sees Iran as an important security threat to the Gulf at large as well as to itself, while both countries also still have to resolve issues concerning the shared North Field (i.e., South Pars for Iran). Further complicating matters are the many common interests that Qatar has with the US.

4) Dependence on gas earnings and security of demand
Russia remains as dependent on markets for its gas earnings as these remain on Russia for gas supplies. In dealing with the US and Europe as well as China, i.e., other great or emerging powers, Russia’s tacit alignment with other gas-exporting countries may be more politically expedient than explicit and formal cooperation. Explicit, formal cooperation may constrain Russia’s foreign policies on other dossiers. Russia is therefore not likely to engage in open cooperation with other gas-exporting countries at the expense of relations with European customers, who may perceive any ostensible attempts by Russia to collude ‘against’ consumers with apprehension. These consumers could pursue strategies which may undermine gas demand in Russia’s gas export markets. In other words, security of gas demand is an important priority for Moscow.

5) Market division and long-term contracts
The carving up and division of markets through the establishment of long-term contracts, which lock in customers, suits gas industry dynamics and fit the nature of the gas trade, which does not require explicit or more formal collusion. The rise of new business models for LNG and pipeline gas challenges the solid underpinnings of these long-term contracts. A tacit agreement between Russia and Iran for the latter to supply Asian markets and stay out of the European gas market is a workable example of tacit market division, wherein the geographical location of suppliers and markets play a key role. Of course, as Case study 1 has shown, this is also the result of Russia’s deterrence of Iranian gas flows to Turkey and beyond.

6) Gas market development and pricing
As has been argued in Chapter 10, overcapacities over time eventually translate into price competition. With the collapse in gas demand observed in 2008-2009, the LNG gas glut is placing extensive pressure on long-term oil-indexation [Stern 2009a]. In the long run devel-
opment of the interregional gas market, and congruent with industrial organisation theory as far as the shift in competition in capacities to prices, issues such as pricing may well become more pressing in a steadily more global gas market. Here, some level of more formal collusion can be imagined, where Russia would require more formal commitments and binding agreements with other gas-exporting countries. For the time being, Russia and other gas-exporting countries wish to stick to oil-indexation, regardless of the volumes of flexible supplies in the form of LNG and pipeline gas, which now exert downward pressure on oil-indexed contracts.

Towards strategic collusion

Given the barriers to open, explicit cooperation listed above, Russia’s nature as a great power and the obvious need for some type of coordination mechanism to avoid oversupplies (also see Chapter 10), what form of cooperation does Russia prefer? Until the interregional gas market fully matures, which is a long-run prospect, Russia will prefer ad hoc collusion with other gas-exporting countries, relying on tacit bilateral agreements and coordination through the GECF and/or Troika. Such tacit collusion can occur on capacity schedules, by mutually postponing investments, or by sharing them. Russia may in some scenarios even desire to compete rather than cooperate. The previous chapter argued that a bandwidth of scenarios exists. The upshot is that Russia will not commit to formal and binding agreements à la OPEC, and yet binding agreements are key to a cartel’s success if it is to survive, i.e., agreements must be stable. Russia will opt for so-called ‘strategic collusion’, which involves collusive behaviour or parallel behaviour on coordinating capacities, for example, falling short of outright cartelisation because it is not a permanent outcome.

11.3.3 Russia’s integrated gas strategy in Eurasia

The geo-strategic underpinnings of the US presence in the rimland, and its geo-economic potential to affect gas flows from the Eurasian gas ellipse, call for a comprehensive integrated Russian gas strategy. A Russian strategy should be ‘integrated’ in the sense that Russia’s foreign policy is to be integrated with and complementary to firm-level policies, i.e., at the level of its national champions. It lays beyond doubt that China’s presence in the region is now also a ‘fait accompli’, and it too seeks to establish a long-run sphere of influence, particularly in Central Asia. Also of great importance is the potential of China (and other Asian economies) as both a market for Russian gas and as a rival geo-strategic player in the Eurasian gas ellipse that seeks to monopsonise gas flows from both the Central Asian and Persian Gulf regions. Russia is likely to use institutions such as the Shanghai Cooperation Organisation (SCO) and the

Ironically, OPEC and other oil producing and exporting countries that also export gas can (see Map 8.1) can manipulate gas prices in long-term contracts by propping up oil prices (taking into account a time lag between oil prices and gas prices, however). Thus by effecting oil prices, the OPEC countries can indirectly influence gas prices in long-term contracts [Hallouche 2006], while according to Zhiznin [2007], OPEC countries wish to avoid over-exporting LNG in order to prevent a decrease in oil prices [Zhiznin 2007].
CSTO as a nexus of political and economic cooperation in the energy sphere vis-à-vis China, especially in Central Asia and perhaps beyond.\textsuperscript{39}

11.4 Conclusion

From a Russian perspective, the US attempts to suffocate Russia’s gas and other interests in Eurasia. This is Russia’s heritage from the 1990s: a Hobbesian view of the world in which Russia is compelled to compete geo-strategically with the US. Strategic investments provide Russia with geopolitical power and are geo-economic tools that provide Russia with geopolitical currency in the rimland. However, the risk of regional gas market oversupply thus also arises.

Russia hence faces a dilemma: it seeks to defend its position in Eurasia, having to compete geo-strategically with the US yet must take into account its interdependence with geo-strategic players and other gas-exporting countries in a steadily more globalised world. In the former case, losses to the US are seen in zero-sum terms, particularly in the post-Soviet space when it comes to geopolitical influence as well as gas interests. In the latter case, room is made for economic and strategic cooperation with other gas-exporting countries because Russia does not necessarily perceive the world in zero-sum terms vis-à-vis the US. In this case, Russia desires to avoid the domestic economic instability resulting from considerable gas market oversupplies abroad.

Coordination is to be pursued between Russia and other gas-exporting is unlikely to resemble explicit OPEC-type collusion or cartelisation of the interregional gas market. Given Russia’s self-perception as a great power and its geopolitical perception of the outside world, strategic collusion within the GECF or within the Troika or a combination of both is more likely. Such collusion is strategic in that it serves a certain purpose for Russia, but is never a permanent given for Russian policy, and is likely to hinge more on key bilateral relations with key gas-exporting countries. Moreover, Russia wishes to maintain room for manoeuvre in its policies outside the gas sphere, requiring it to keep its options open in its commitments to other gas-exporting countries.

Economically and strategically it may be beneficial for Russia to cooperate with other gas-exporting countries but its identity as a great power and its geopolitical aspirations prevent Russia from making any binding commitments. Even though it has taken greater interest in playing a leading role within the GECF in recent years, and is one of the drivers of the Gas Troika initiative, formal cooperation is unlikely to suit Russian interests, as Russia is a power

\textsuperscript{39} Depending on geopolitical relations mainly between Russia, China and the US, the SCO could be used as a forum for Russia and China to defend their common Eurasian interests against the US. A Kissinger-style US foreign policy of playing off Russia against China could diminish the likelihood of such a partnership between these two Eurasian powers.
with the desire to maintain policy independence. In addition, the interests of gas-exporting countries differ widely: while Russia’s preference for long-term contracts and oil-indexation encourage Russia to take an independent stance on issues such as pricing.

In the bid for the control of gas flows, the Eurasian gas ellipse will become a field of increased competition in the longer term, particularly if the US pursues its goal of servicing its European NATO (and other) allies. The struggle to influence the playing field in the Eurasian gas ellipse adds a geopolitical character to possible gas market coordination that neither standard cartel theory nor the real-option game model can capture. What is more, as discussed above, Russia’s decision whether to compete or not with other gas-exporting countries hinges to a large extent on its perception of the international political system. The decision on Russia’s part not to compete with other gas-exporting countries—and by extension successful collusion—is subject to geopolitical, rather than merely economic boundary solutions.