

Nabucco vs. South Stream – Rivalry over Balkan Gas Pipelines

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Over recent months, Russia has noticeably intensified its efforts to prevent the building of infrastructure for the export of Caspian natural gas to Europe. This refers particularly to the Nabucco pipeline, which is regarded as a strategic project for the European Union. Nabucco constitutes a serious challenge to Russian energy interests. Moscow's visible agitation is mainly a result of the increasing feasibility of the EU project, which is a consequence both of the growing availability of natural gas sources and a clear intensification of EU & US activities concerning the project. The agreements signed recently with Bulgaria, Serbia and Hungary facilitating implementation of South Stream, which is an alternative project to Nabucco, emphasise the intensification of the Russian policy. Such Russian actions are targeted not only against Nabucco but also, more extensively, against the unity of EU member states in their approach to energy issues. Their effects, at the moment, can be seen in the fields of politics and propaganda; they have resulted in deepening doubts about the possibility of completion of the Union's strategic project and building political support for the South Stream project, which is promoted by Russia. Nevertheless, it seems that – contrary to Moscow's efforts – Nabucco is still the most realistic project, and the European Union (with US support) will continue its efforts to make its implementation successful.

Nabucco, a strategic project for the EU and the USA

Nabucco is a strategic gas pipeline project for the European Union, which is expected to contribute to the diversification of sources and routes of natural gas supply and, consequently, to improving energy security in Europe. The project is an element of a broader US-European idea of building an independent from Russia East-West gas export corridor. Such a corridor would enable European access to gas from Caspian Sea region (Azerbaijan and Central Asia) and also from the Middle East (Iran, Iraq and Egypt). The Nabucco gas pipeline is planned to run through Turkey, Bulgaria, Romania and Hungary to Austria (to the gas hub in Baumgarten), from where gas will be further distributed to other EU member states.

The Nabucco gas pipeline, which was listed among the priority infrastructure projects of the EU's TEN (Trans-European Networks) programme as early as 2003, has gained significantly in importance since the Russian-Ukrainian gas crisis in 2006. As part of the common Energy Policy for Europe concept, which was presented in early 2007, it became the most

important EU gas pipeline project enabling diversification of supplies. A special European coordinator was appointed to facilitate more rapid implementation of the project.

Nabucco also plays a major part in the US policy on Eurasia. Washington has for many years promoted building oil and gas export routes from the Caucasian and Central Asian states, designed to omit Russian and Iranian territories. This is part of its strong commitment to developing the Caspian states (increasingly independently from Russia and more strongly linked with the West) and of European energy security (by reducing dependence on energy imports from Russia and the Middle East). Since the successful launching of the Baku–Tbilisi–Ceyhan oil pipeline in 2006, the completion of the Caspian gas export route to the EU has become one of the priority goals of US energy policy in the region.

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Nabucco makes progress

Opportunities (chances) for securing natural gas supplies for Nabucco have become more numerous over the past year and a half. Since 2006, further sections in the emerging East-West export corridor have been built to enable the export of gas from Azerbaijan which already flows

to Turkey via the Baku–Tbilisi–Erzurum (BTE) pipeline, opened in 2006.

The reality of Caspian gas exports to the EU has been confirmed by the launch of another section in the East-West corridor, the Turkey–Greece inter-connector pipe, which is an element of the Turkey–Greece–Italy project (TGI, see the map). Increased estimates regarding the reserves of the Azeri Shah Deniz gas deposit give hope for even greater supplies from Azerbaijan than originally planned. At the same time, the European Commission's efforts to enable gas supplies from Middle East and North African countries have noticeably intensified. Initial agreements on supplies of Iranian gas to Nabucco were signed in 2007. Additionally, negotiations on buying gas from Egypt and Iraq have been set on track; it will be possible to implement the deals when the so-called Arab Gas Pipeline is extended to reach Turkey – as envisaged. Last but not least, the change of government in Turkmenistan and the new Turkmen leader's greater openness to the West have enabled the resumption of negotiations on possible Central Asian gas supplies to Nabucco (using the planned trans-Caspian gas pipeline or via Iran).

Work on the project development phase has been accelerated over recent months. At the beginning of 2008, the German RWE joined the consortium of companies engaged in Nabucco (see Appendix), which will not only bring financial benefits (the costs of the project will be shared by a larger number of companies) but is also expected to guarantee an outlet for part of the gas involved. RWE has been chosen after rather keen competition (with the French Gaz de France among the rivals), which proves that the project is attractive to European companies. In the first months of 2008, the European Commission allowed the exemption of the Austrian section of Nabucco

Nabucco

Route: Turkey – Bulgaria – Romania – Hungary – Austria

Length: 3300 km

Flow capacity: 31 billion m³

Project cost: € 5 billion

Consortium: Nabucco Gas Pipeline International GmbH; shareholders Botas, Bulgargaz, Transgaz, Mol, OMV and RWE

Raw material sources (planned): Azerbaijan, Central Asia (Turkmenistan and Kazakhstan), Iran, Iraq and Egypt; no supply contracts have been signed

Implementation progress and future prospects of the project:

- 2002 – memorandum of understanding on the project signed
- 2004 – consortium established and feasibility study carried out
- 2008 – final investment decision expected to be made
- 2010 – building work planned to commence
- 2013 – building work planned to be completed and supplies launched

from the EU Gas Directive requirements of third party access (TPA) to the pipeline's transport capacity. Moreover, the British company Penspen has been appointed to coordinate engineering work.

The unresolved issues

However positive such solutions may be, many issues crucial for building Nabucco have not yet been resolved, which means that the implementation of the project is still not a foregone conclusion. The weightiest argument used by the project's opponents (Russia among others) is the lack of guaranteed supplies necessary to fill the pipeline. The Nabucco consortium has not yet signed any supply contracts with gas producing countries. It is still uncertain whether, when and how gas from Central Asia will be delivered to Nabucco. Possibilities of supplies from Iran are limited due to the country's complicated geopolitical situation. Moreover, misunderstandings with Turkey concerning gas transit through its territory have not been resolved (Turkey does not want its role to be limited to that of a transit state; instead it wants to actively participate in the re-export of gas). Doubts have also appeared about the real demand for gas from Nabucco in Southern and Central European countries, since the market is saturated by existing supplies (mainly from Russia). All this makes the decision to build the pipeline quite difficult and causes delays in the project implementation schedule. The final decision on investment is expected by the end of this year and the planned dates for commencing the construction work and opening the pipeline have both been postponed by one year.

Nabucco vs. Russian interests

One of the key factors which complicate the implementation of Nabucco is the fact that its existence per se is contrary to the interests of Russia, which is the largest exporter of gas to Europe. The Russian Federation wants to reinforce its position on the European market, to limit access for its competitors and to maintain its control over gas exports from the Caspian region. Meanwhile, Nabucco is intended to supply independently from Russia gas non-Russian sources (including Azerbaijan and Central Asia). These supplies will be aimed at Russia's traditional markets in Southern and Central Europe, Hence the Russian attempts to impede the completion of Nabucco in its originally designed form. The signs of increasing feasibility of the project implementation (especially the Western successes in Azerbaijan) and the intensified activity of EU and US diplomacy in Central Asia, which have appeared over the past year or so, give impetus to such Russian attempts. The activation of Russian policy has become noticeable not only in the European countries, where the planned outlet markets and/or transit territories of the new gas pipeline are located, but also in the Caspian region, which is expected to be the main source of gas for Nabucco.

Russia has been trying to play on the problems linked to the project implementation and to turn them to its profit. Talks with Central Asian

TGI

Route: Turkey–Greece–Italy, the route will consist of the existing Turkey-Greece inter-connector pipe and planned Greece–Italy sea pipe (going through the bed of the Ionian Sea)

Length: Turkey–Greece: 296 km,
Greece–Italy: 807 km

Flow capacity:

- section to Greece: currently 7 billion m³, max 11.5 billion m³
- section to Italy: 8.5 billion m³

Project costs: € 1 billion (including € 350 million for the maritime section), the project is co-financed by the EU

Consortium:

- Turkey–Greece inter-connector: DEPA and Botas, each holding a 50% stake
- Greece–Italy inter-connector: Poseidon Company (DEPA and Edison, each holding a 50% stake) for building the maritime section; DEPA is responsible for the land section in Greece

Gas sources: in 2007, Turkey re-exported Azeri gas to Greece; according to plans, gas from the Caspian region and the Middle East will be fed to the pipeline

Implementation progress:

- 2001 – Turkish-Greek memorandum of understanding on the project signed
- 2002 – agreement on building the Turkey–Greece inter-connector pipe signed
- 2005 – building of the first section of the gas pipeline (Turkey–Greece) started
- 2006 – agreement on building the Greece–Italy gas pipeline signed
- 2007 – the Turkey–Greece inter-connector pipe opened
- 2008 – the Greece–Italy inter-connector pipe building planned to commence
- 2011 – section going to Italy planned to be completed

countries and agreements signed (on increasing the capacity of existing export pipelines as well as building new ones connecting Central Asia and Russia, among other provisions) are intended to limit the availability of gas which could be exported to the West independently of Moscow. In turn, subsequent long-term contracts for Russian supplies, with Southern and Central Eu-

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ropean states (Romania, Bulgaria, Hungary, Austria and the Czech Republic), which were signed in 2006, lessen the demand for gas from alternative sources. New proposals to build other gas pipelines running from the Russian Federation to Southern and Central European countries, competing with Nabucco, have been made over the last two years. South Stream is the project which is currently promoted most strongly.

The case of South Stream

Russian activities related to South Stream perfectly illustrate the methods which Russia has been using in an attempt to defend its interests and torpedo any initiatives which do not comply with them. The project, which was announced by Gazprom and the Italian company ENI in June 2007, is currently in the preliminary phase. South Stream gas pipeline is planned to stretch from Russia across the Black Sea bed to Bulgaria, where it would split into two, with the southern pipe going to Greece and Italy, and the northern one going to Hungary and other Central European countries. This means that South Stream would supply the same markets as the pipes of the emerging East-West export corridor (both the Turkey-Greece inter-connector, which was made available in late 2007, and Nabucco) and is a counter-proposal to the concept of the export of Caspian gas to Europe independently of Russia. In fact, the Russian project is significantly less advanced than both Nabucco and the TGI gas pipeline (the later is already being built). The South Stream's feasibility study has not yet been carried out. Its precise route (in particular, the section going through the Black Sea) and its total costs are unknown. Consequently, even though the project has been initiated by the world's largest gas producer (Russia), which guarantees a resource base, it is difficult at the moment to clearly determine the economic profitability or likelihood of its construction.

As a result of the intensive actions taken by the Russian Federation, over recent months, South Stream has received political support from a number of Balkan and Central European countries, including those also engaged in Nabucco; agreements have been signed with Bulgaria, Serbia and Hungary to set conditions for carrying out of South Stream in their territories and a similar agreement is expected to be signed with Greece. Russian-Austrian co-operation has been enhanced (inter alia with Gazprom taking over a 50% stake in the Baumgarten hub). Although such agreements do not settle the future of the project, they give the impression of increasing progress and, in line with other Russian actions, seem to pose a threat to the implementation of the Nabucco project.

South Stream

Route – initial idea: from Russia through the Black Sea bed to Bulgaria, then two pipes:

a) to Serbia (or Romania), Hungary and Austria
b) to Greece and Italy, possible branch pipes;

Length: 900 km (maritime section)

Flow capacity: 30 billion m³

Project costs: initial estimates: between € 7 and 10 billion

Consortium: n/a; ENI and Gazprom established South Stream company to carry out a feasibility study for the project

Implementation progress and future prospects of the project:

- mid-2007 – memorandum of understanding between ENI and Gazprom signed
- November 2007 – company which expected to carry out the feasibility study for the maritime section by the end of 2008 established
- 1st quarter of 2008 – agreements on building the gas pipeline signed with Bulgaria, Serbia and Hungary
- 2013 – building work planned to be completed and supplies launched.

Reactions to the Russian activities

The Russian activities aimed at undermining the practicability of Nabucco, mainly the recent agreements with countries participating in the project, have met with a decisive reaction from the USA, for which the struggle for Nabucco is an element in the Russian-US rivalry for the future of the Caspian gas exports. Diplomats from the US State Department have warned against a 'gas pipeline war' in Europe. Their public statements for the media and during foreign visits to various countries in the region have emphasised Washington's support for Nabucco and the commercial value of the project, and have promised more active engagement in resolving the problems which inhibit the implementation of the pipeline. The European Union has reacted with more reserve. However, the moderate tone chosen by EU officials does not mean that the priorities in the energy policy have changed. Although Brussels has officially recognised the possibility of the coexistence of the two projects, it has emphasised Nabucco's significance for the Union and thus clearly demonstrated the will to continue activities aimed at building the pipeline. At the same time, it has shown its understanding of the interests of both EU member states and the key supplier of gas to the European Union (Russia), and has left some room for compromise.

The effects of the rivalry for Nabucco

1. Russian energy policy in Southern and Central Europe has achieved some important results. Russia has taken intensified actions and skilfully gained support from both individual EU member states and the Italian ENI company. Thus it has managed to create the South Stream project in a relatively short time and give it quite a high profile.
2. The recent Russian actions linked to South Stream are significant in the fields of politics and propaganda. Russia has managed to cast more doubts on the practicability of implementation of the EU project among politicians and in global public opinion, especially by signing agreements with countries which are also participating in Nabucco (Bulgaria and Hungary). Moreover, the agreements have cemented relations between these countries and Russia.
3. Russia has succeeded in breaking the political consensus on Nabucco which has existed up to now in the EU (some member states have supported an idea which is in competition with Nabucco, although it is Nabucco which has been determined as the EU strategic project). This is another project, after Nord Stream, which Moscow has successfully used to increase disunity in gas-related issues within the EU. This may inhibit the development of an EU energy strategy and the achievement of a uniform stance on Europe's gas relations with Russia.
4. However, in practice, none of the countries which have supported the Russian South Stream project have given up the idea of Nabucco or of diversifying energy sources. Considering the lower cost of the EU project, greater progress in preparatory work and conformity with EU priorities, the implementation of Nabucco still seems – for the time being – to be more likely than the building of South Stream.
5. The rivalry linked to Nabucco and the general concept of an East-West corridor for export of Caspian (and Middle Eastern) gas independently from Russia will intensify in the near future.

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Map. European and Russian gas pipeline projects

