

# ENERGY POLICY



## RUSSIA'S ENERGY GEOSTRATEGY IN THE BALTIC SEA REGION

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*This article explores Russian energy policy in the Baltic Sea region in the context of the world energy market globalization. The study focuses on the three Baltic States — Latvia, Lithuania, and Estonia — which have a similar geographical location and history. The dynamic development of the region as a whole is strongly influenced by the stability of energy supply in each state. The article analyses the role Russia plays in the energy policy of the region from both geopolitical and geostrategic viewpoints. The author identifies the main characteristics of the Russian energy policy in these countries, and provides with a forecast for energy policy development in the region.*

*A geostrategic approach dictates any successful energy policy in the Baltic Sea region to bring in line Russian interests with those of the European states.*

**Key words:** energy policy of Russia, Baltic Sea region, geostrategic approach to the study of energy

We live in a world that is undergoing yet another major socio-political and economic transformation. Risks of various kinds — nuclear, environmental, financial, military, terrorist, biochemical, and informational — accumulate and are becoming the key decision-making factor. We are surrounded by those risks, and the risk, in turn, seeps inside. However, the mere presence of risks doesn't spell 'catastrophe', but rather the anticipation of one [1, p. 47—48].

In order to foresee catastrophe in the 'world risk society' (U. Beck), one must study the traditional research fields, security, and world politics in combination with energy issues. The subjects of treaties and diplomatic contacts established

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on the Eurasian continent bring to the fore the issues of energy resource trade and energy transport projects thus giving an impetus to the joint constructive development of a non-confrontational type.

This study focuses on the countries of the Baltic region — Latvia, Lithuania, and Estonia, which share geographical location and have common history. The aim of this work is to research Russian energy policy in the countries of the Baltic region against the backdrop of world energy market globalization. To achieve this aim, we have put forward a set of objectives:

- to describe contemporary world energy market;
- to carry out a geopolitical and geostrategic analysis of Russia's role in the energy policy of the Baltic region states (Latvia, Lithuania, Estonia);
- to identify the features of Russian energy policy in the countries of the Baltic region;
- to examine the prospects of development of Russian energy policy in the region.

The countries of the Baltic region are tied together by common history — rich in conflicts but driven by shared interests. The Hanseatic League of the 14<sup>th</sup>—15<sup>th</sup> centuries serves as a good example. Despite the disputes between its member states, the trade between them was flourishing. During the Great Northern War (1700—1721) Sweden and Denmark — being at war with each other — still continued the joint use of the Nidingen lighthouse to ensure safe navigation in the Kattegatt strait. Shortly before WWI, Swedish companies *Ericsson* and *Nobel Industries* carried out a number of major commercial projects in Russia, although at the time Russia was a military threat to Sweden [2].

It is worth noting that *Nobel Industries* (the *BraNobel* company in Russia) contributed to the development of Baku oilfield and thus influenced the history of Russian oil industry. Among the Nobels' contributions to the development of oil industry in Russia is the construction of the first Russian oil pipeline. Another achievement is the creation of the oil tank fleet; the Nobels were also pioneers in the field of railway transportation of petroleum products. These are just a few examples of what can be achieved through collaborative constructive development of a non-confrontational type. There is much historic evidence that the Baltics Sea has often been a unifying rather than dividing factor for the region, which should serve as a good lesson for policy makers of the present day.

Today, as before, the rapid development of the Baltic Sea states largely depends on how stable the energy components of each country are. This relates to the globalisation of energy security, which rests on the principles of long-term, reliable, and green energy supply at adequate prices suitable for both exporting and importing countries.

In the early 21<sup>st</sup> century the shape of the world energy market started to change. European countries are forming a common gas market. World exporters compete fiercely for short-term and long-term contracts. The rapid development of Pacific Rim region (notably, China, Japan, India) accompanied by an increase in its energy consumption requires new energy sources

and capacities. The increase in LNG trade has become an important global trend in the energy market. The leaders in the field are the USA and Canada. The new gas production and processing technologies allow the USA to profitably produce shale gas. Shale gas production is a labour intensive and environmentally hazardous process. However, the US still anticipates the so-called 'shale gas revolution', and in 2011 alone it increased its shale gas extraction to 214 billion m<sup>3</sup>. According to the International Energy Agency, global gas production will grow by 50 % until 2035; while non-traditional (first of all, shale) gas will account for two-thirds of this growth. The USA is the leader in shale gas production [3].

Russia is becoming increasingly integrated in the world energy market as it contributes to the operations of all command centres of world energy security. The global nature of energy problems, their politicisation, and the increasing role of Russia in the world energy arena made energy one of the crucial elements of Russian foreign policy.

The topic of energy security is now a top priority in the framework of Russian energy dialogue with its major buyers — most importantly, the European Union and its individual member states such as Germany, the UK, France, the Netherlands, and Italy. The lack of an operational legal framework is a major obstacle in the EU-Russia energy relations.

In October 2012, a meeting of the Commission for Strategic Development of the Fuel and Energy Sector and Environmental Security took place in Moscow, during which a draft of the Russian energy security doctrine was discussed. Among the priorities the draft puts forward are: secure supply of energy resources to customers; innovative development of fuel and energy industry; increased energy efficiency of all sectors of national economy; non-discriminating access of Russian exporters to external markets; and a stronger standing of the Russian Federation in the world energy markets. There is a need for swift and adequate reactions to changes in the energy market configuration. According to the speech delivered by Vladimir Putin at the meeting, 'it is essential to consolidate the principles of intergovernmental cooperation in the energy sector with the EU countries and the EU as a whole, to develop a set of measures that will improve the competitiveness of the Russian electricity sector, and not only to keep our traditional markets, but also to expand to new markets in the near future' [4].

The geostrategy of modern Russia should take into account the 'new dimensions' of energy unions, whose efficiency can eventually ensure Russian leadership in world energy politics. In the near future, the EU will not be able to forego Russian gas through replacing it with alternative energy sources. The structure of the EU's gas import is as follows: Russia — 32 %, Norway — 34.6 %, Algeria — 14.5 %, other countries — 14.7 % [5].

Europe does have gas resources of the North Sea, but these are depleting. Experts estimate that after 2010 at least 60 % of European gas needs will be satisfied through import. As early as 2015, European demands for gas will increase by a third. Gas fields in the Netherlands and the UK are almost ex-

hausted; Norway's contribution to meeting the EU needs is on decline, and that of Russia is on the rise; the share of Algeria — a supplier of gas to Spain, Portugal and, to some extent, to Italy — will remain at the same level. At the moment, Russian gas accounts for 24 % of European energy needs. The EU countries encounter difficulties in developing a single concept relating to Russian gas supply, since the degree of their dependence varies greatly. For instance, the Baltics and southern states fully depend on Russian gas; the Nordic countries, Poland, and Germany are classified as “heavily dependent”, while Spain and England hardly depend on Russian gas at all. The latter insist on looking for “alternatives” to Russian gas.

Russian energy policy relies on the assumption that Latvia, Lithuania, Estonia, and partially Poland act predominantly as energy importers. The problems of the Baltic States' energy dependence is deteriorated by that they spend approximately 13 % of GDP cost on energy import, which is explained by the low energy efficiency of industry in these countries. Russian monopoly on gas supply to the Baltic Sea states has existed since the Soviet times, yet back then the RSFSR was a friendly republic, whereas today, through the prism of politics, Russia is seen as an external threat to the energy security. Global political risks and changes in the sphere of international security make the countries of the region look for the alternative ways to stabilise energy supply. The political aspects are accompanied by discontent with high prices for Russian energy resources, which makes these states seek energy sources elsewhere.

A liquefied natural gas (LNG) terminal is expected to be put into operation in the Polish city of Świnoujście in 2014; with LNG delivered from Qatar. Starting from 2010 the Baltic States have been discussing the construction of LNG terminal for their region. However in 2011 Latvia proposed another project, a Poland—Lithuania gas pipeline, which would grant the other countries access to German pipelines going through Poland. The unsolved economic problems within the region and the lack of a unified energy policy result in the EU's lack of motivation to co-finance the project [6].

In the field of nuclear energy, Russian policy is based on the challenges faced by the country. In 2009 the EU closed down the Ignalina NPP in Lithuania for environmental reasons. Lithuania, Latvia, Estonia, and Poland reached a decision to construct the Visaginas NPP with Japanese technology (however, in 2011 Poland withdrew from the project). Poland and Estonia have now announced their intention to construct their own NPPs. In the meantime, Lithuania has signed a 10 year energy supply contract with *Inter RAO UES*, and the construction of the Baltic NPP in the Kaliningrad region and the joint NPP project with Russia and Belarus in the Grodno region can ensure electricity supply, perhaps, on more advantageous terms than the domestic capacities of various industries of these countries [7; 8]. In this case, Russian project might receive support Poland, since an increase in natural gas transit through Belarus and Poland, for example, has already had a beneficial effect on Russian-Polish relations [9].

In 2006, *Gazprom* made a transition to market-based pricing for the Baltics, which made the prices double and then even triple. Simultaneously,

*Gazprom* acquired significant holdings of shares (around 30 %) of Baltic gas transportation companies. Gas pricing depends on the degree the country is integrated in *Gazprom* business, as well as the import capacity (as a result of its increase in 2011, Latvia and Estonia received a 15 % discount). In terms of relations with the EU countries the main challenge to Russian energy policy is the Third Energy Package adopted in 2009 [10; 11]. The philosophy behind this legislation rests on two principles. The first principle — ownership unbundling — suggests that an agent cannot simultaneously produce energy resources and transport them to the EU countries. The second one — TPA (third-party-access) suggests that third parties can also use the transportation infrastructure — gas pipelines — alongside the supplier and the consumer. Of course, these two principles pose a threat to the energy security of Russia and, first of all, *Gazprom*, which transmits gas to European countries; moreover, the emergence of new investors within a developed infrastructure can cause additional complications.

The Baltic States hastened to meet the EU requirements for splitting gas supply and transportation, as well as to emphasise the need for fair pricing.

According to the Energy strategy adopted in Russia in 2009, *Gazprom* and other energy companies with state backing aspire to maintain stable relations with traditional markets but use a geopolitical approach for advancing national interests, since economic security largely depends on successful energy export. Whether a transition from the geopolitical to a geostrategic (integrative) approach will be possible in this region is still an open question. The outcome will largely depend on whether the Baltic countries are able to abandon the position of “the last Western outpost” and assume that of “a bridge between the East and the West”. The signs of a geostrategic (integrative) approach are present in Russian energy policy regarding Poland. However, there are still complications in relations between Russia and the Baltics caused by the concerns about the declining role of transit countries in delivering Russian energy resources to Germany and other states of Western Europe. These complications are mostly connected with the development of oil transit via the ports of Primorsk and Ust-Luga on the Russian territory and the continuation of the Russian *Nord Stream* project.

In 2011 and early 2012, there was a certain increase in the volume of oil transhipped at Russian sea terminals. This happened for two reasons: first, there was a decrease in oil production at some fields; secondly, we saw the growth of oil processing within the country at national refineries. However, the export of crude oil through seaports is very likely to remain the principal area of Russian foreign trade, and modernisation and construction of sea oil terminals will continue.

An increase in oil export to the Baltics is ensured through the growth in oil shipping via the port of Primorsk (BTS-1), as well as putting the oil terminal in the port of Ust-Luga into operation. Experts believe that it will increase the surplus of Russian capacities ensuring export to the West. The check points on the Russian territory (Primorsk,

Novorossiysk, Ust-Luga, etc.), firstly, ensure the transit of Russian oil to Europe and, secondly, contribute to the energy security of the Russian Federation [12; 13].

Perhaps, the settling of disputes and the achievement of consensus by all countries of the region will require Russia to pay greater attention to energy cooperation in the framework of the Council of Baltic Sea States working under Russian presidency since July 2012. Successful energy policy in the region requires Russia to harmonize its interests (a geostrategic approach) with those of Western Europe — the consumers of Russian resources. We can clearly see the need for that since yet another rift in relations between Russia and the Baltics stems from the adoption of the European energy legislation. At the same time, not all Western European experts believe that there is a need for an urgent liberalisation of energy markets because that can result in Russia pursuing a stricter gas supply policy. It is, after all, rather difficult to find an alternative to Russian gas, so any negative dynamics may adversely affect the Baltics [14; 15]. Russia should take into the account the integration of these countries into the European transmission networks in accordance with the plan of the European Commission and the Baltic region states of 2009, because earlier the transmission systems of the Baltics were integrated only with those of Russia and Belarus. The optimal solution for the Russian Federation would be to launch the Baltic NPP as soon as possible and get involved with the Baltic Energy Ring project, which is aimed at bringing together all countries of the Baltic Sea region.

Russian energy policy in the Baltic Sea region can be described through the following categories: involvement, integration, and innovation. In our opinion, these are not three different approaches, but rather three components of Russian current geostrategy, including the energy dialogue between Russia and the EU.

In the globalized world, with transnationalisation of international politics, the geopolitical paradigm should be replaced in several key aspects with a geostrategybased on the integrative principle of 'selective involvement' designed to qualitatively transform the entire sphere of social relations and transnational interaction. It should also generate strong transcontinental and internal regional streams and networks, interconnections and relevant forms of governance [16].

Perhaps, a new geostrategic method of research (geostrategy) will help Russia find a strategy for optimal and systematic integration into the world telecommunication and information space and develop a predictable and well-coordinated energy policy.

At the moment the entire Eurasian continent is embracing a new hot topic — that of 'energy bridges', oil and natural gas transit routes. They are the subjects of modern geopolitical games. Today, information communications and energy bridges form a new global space, which serves as a site for emerging geopolitical and geoeconomic competition. Integration processes create new 'large spaces' that clash the states together and create new hot-spots of geopolitical tension. Energy interdependence will increase, as well

as consumption of energy; the struggle for control over energy resources and the national selfishness of states and regions in ensuring energy security will thus intensify. In the divided world there was a clash between two superpowers (the USA and the USSR), whereas in the age of globalisation, there is competition not only between the developing superpowers, but also *inside* them. It would be more advantageous for Russia not to exploit contradictions, but to encourage the neighbouring territories of the EU, Central Asia, and China towards integration. Against the background of major political and economic differences, energy security is a common ground for harmonising the interests of these power-wielding agents.

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**RUSSIA'S  
ENERGY POLICY  
IN THE BALTIC REGION:  
A GEOECONOMIC  
APPROACH**

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*This article analyses certain issues of implementation of Russian energy policy in the Baltic region from the geoeconomic perspective. The purpose of the study is to explain Russian energy policy in the region as dependent solely on the import capacity of its partners. Russian energy policy is viewed as one of the most important activities of the state and its business structures. As such it aims to achieve both general economic goals (generation of profit, market domination) and more specific geoeconomic tasks. At the same time, the policy follows the traditional rules of consumer/producer market game. Russian energy resources are delivered to an energy deficient region, where the demand and need for them is stable. The study is based on the author's geoeconomic methodology, which extensively uses geographical and general scientific methods. This work aims to develop a geoeconomic paradigm in the framework of social geography. It will be of interest to anyone who aims to analyse the true motives behind Russian current energy policy.*

**Key words:** Russian energy policy, Baltic region, hydrocarbon resources, geoeconomics, geoeconomics of energy sources

The pipelines stretching across the territory of Russia help to connect unique mineral and raw material resources (including hydrocarbon) and power generating capacities with their end users, i.e. industrial centres and other consumers in the pivotal geoeconomic centre, the European Union (EU). Because of the volume of its market (with population nearing 150 million people and a GDP of about 5 trillion USD) and its geographical proximity, the Baltic region has always been a point of special interest for Russia. The energy streams between Russia and the Baltic region are studied by applied geoeconomics.

Geoeconomics, a research branch within the field of social geography, studies the formation of structural elements of global geoeconomic space [1; 2]. Such

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