

Russia's gas weapon

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LONDON Gazprom rising

For Russia watchers, Gazprom's recent announcement that it plans to move into the United States, with designs to take a 10 percent market share for liquefied natural gas by 2010 and increasing that up to 20 percent as soon as production permits, should have come as no surprise.

The move is part of a long-term strategy that is being skillfully executed by the Russian state-owned energy giant with the full backing of President Vladimir Putin.

While this news is significant and represents a new direction for the company, it is by no means overly ambitious for the new-look Gazprom. Because of a recent decision in the Russian Parliament, Gazprom is now allowed to sell shares to foreign investors, though the majority of shares will remain in the hands of the Russian state. That will enable Gazprom to raise capital abroad and form partnerships with major players in the energy sector.

Plans are being drawn up for a Gazprom consortium to ship gas extracted from the Barents Sea to the United States. Current suitors include the likes of ConocoPhillips, Chevron and Norway's Statoil.

Given that demand for liquefied gas is expected to increase in the United States, it seems a sound idea for all concerned. But should America feel comfortable with this level of dependence on a company owned by the Russian state?

An analysis of Russia's motives is in order, and Putin's very personal approach to Gazprom, one of Russia's largest assets, tells much of the story.

In mid-November, Putin appointed the chairman of Gazprom, Dmitri Medvedev, a trusted ally and friend from their days together in St. Petersburg, to the post of deputy prime minister of Russia.

With a senior politician at the head of Gazprom (indeed, Medvedev may yet emerge as the favorite for the 2008 presidential election), the company's role as a powerful foreign policy tool was assured.

Both Putin and Medvedev are pragmatic politicians, prepared to borrow and adapt Western methods when they suit their objectives, though neither has genuine free market instincts.

Gazprom's move to sell shares to foreign investors is based solely on a need to raise capital, which is essential if it is to expand. It is therefore prepared to meet the market just a little less than half way, offering up to 49 percent to foreign investors. But it is most definitely not prepared to risk losing its ability to operate as an arm of the Russian state.

One of Russia's aims is greater geopolitical stability, which neither Putin nor Medvedev believe can be achieved unless Russia is able to reassert her preeminence - let's not forget that Putin, in an address to the Russian nation in April 2005, said that the collapse of the Soviet Union was one of the "greatest geopolitical catastrophes of the 20th century." So Russia is now playing one of the few good hands it has.

With the United States as the sole superpower and now a major influence in central Asia, the Baltics and Ukraine, Russia is not going to let what remains of her former empire

leave the fold without a fight.

Gazprom has recently signed an agreement with Kazakhstan's state-run natural gas transit company, KazMunai, giving it control over all gas exported from Kazakhstan, Turkmenistan and Uzbekistan. Any country that wishes to purchase gas from Central Asia will be vetted, with commercial agreements dictated by Moscow.

Whereas the agreement with KazMunai might be viewed as purely logistical, Russia's precipitous moves to increase the price that Ukraine pays for gas by as much as 400 percent as of January looks more like an effort to put pressure on President Viktor Yushchenko and the "orange revolution" that brought him to power.

Medvedev has not minced his words - if an agreement cannot be reached with Ukraine, he has threatened to turn off the tap. With 75 percent of Ukraine's supplies being of Russian origin, and 29 percent of Europe's total gas supply (rising to 50 percent for some former East bloc countries) coming through pipelines in Ukraine, the effects could be catastrophic.

Russia is not likely to pull the plug at this stage, since that might jeopardize longer term plans for Gazprom and would be a careless move at a highly critical moment for the company. Even so, the threats should not be disregarded.

So how wise is it to cultivate a dependence on Gazprom in the United States and Europe? I think that's a question investors should be quite capable of answering for themselves.

(Ziba Norman is director of the Transatlantic Institute, a foreign policy research organization based in London.)

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