

Analysis

Natural Gas and Russia–Turkmenistan Relations

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Abstract

On 1 January 2009, Russia began paying “market prices” for natural gas from Turkmenistan. Although the exact price to be paid is not known and “market prices” is a fuzzy concept, this development comes after years of intractable price quarrels and represents a clear break with the past. This article examines the international context of this turnaround in energy relations between the two countries, as well as the linkages to the most recent Russian–Ukrainian gas crisis, which, not incidentally, also started on 1 January 2009. The article argues that whereas Turkmenistan has remained closely tied to Russia in the energy sector, its broader foreign policy has consistently sought to remove itself from Moscow’s sphere of interest. Thus Russian–Turkmenistan relations combine close cooperation and detachment to a degree that is almost paradoxical.

Not-So-Great Game

Turkmenistan is Central Asia’s biggest natural gas producer, with an annual output of 72 billion cubic meters (bcm) in 2007. Due to several factors – its small five-million population, southern latitude, widespread poverty, authoritarian regime and lack of industrialization – Turkmenistan can export as much as 75 per cent of its gas. By comparison, in 2007 Uzbekistan produced 65 bcm, but with a population of 27 million and a stronger industrial sector, only 15 bcm remained for export. Kazakhstan, with a population of 15 million, produced only 13 bcm, of which it consumed 10.6 domestically. Thus Turkmenistan’s status as Central Asia’s pre-eminent natural gas exporter is unlikely to be challenged any time soon. Most of Turkmenistan’s gas is exported via Russia, and quarrels over the price of this gas have occurred at least biannually since the collapse of the USSR.

Turkmenistan’s natural gas exports to and via Russia were for many years complicated by the involvement of several different private-company intermediaries, the inclusion of barter in pricing arrangements and the complexity of the three-way relationship involving Russia, Turkmenistan and Ukraine, which is the end-user of most of Turkmenistan’s gas exports.

So great have the opportunities for profit been in this tangle that the intermediary company Itera, founded and run by people originally from Turkmenistan, has become one of the largest private companies in Russia.

Multi-Vector Pipelines

Turkmenistan’s former president Saparmurat Niyazov chafed whenever Russia exerted heavy pressure on him to keep prices down. When the terms became too frustrating for the reclusive dictator, Niyazov would start

considering, and loudly discussing, alternative pipeline options that might enable him to bypass Russia’s transit monopoly. After Niyazov’s death at the end of 2006 and the rise to power of Gurbanguly Berdymukhamedov, this tendency has intensified. A map of prospective export pipelines from Turkmenistan resembles the country’s multi-vector foreign policy: the potential pipelines point in all directions. Several different pipeline options have been mooted:

- Western, Azerbaijani, Georgian and Turkish actors promote the construction of the Trans-Caspian Gas Pipeline in order to give Turkmenistan the ability to sell gas to the West independently of Russia. The pipeline would cross the Caspian Sea to Azerbaijan, where it would follow the route of the Baku–Tbilisi–Erzurum pipeline and be extended onwards to Europe. During 2007 and 2008 a blitz of Western actors visited Turkmenistan to promote this project as well as to gain access to gas fields that might feed into the pipeline. In the course of the nine months after the death of Niyazov in December 2006, Turkmenistan received 283 official delegations (and Berdymukhamedov carried out nine state visits abroad). The West is so interested in Turkmenistan’s gas that the country’s profound authoritarianism does not seem to be a significant obstacle. However, concrete results have been few. Instead, Turkmenistan has continued negotiations with Russia and Kazakhstan on re-building the Pri-Kaspiskiy pipeline, which would reinforce Russia’s control over Turkmenistan’s exports. However, actual work on this project has not started either.
- Unocal (merged with Chevron in 2005) leads an international consortium that has promoted the TAPI pipeline, intended to go from Turkmenistan via Afghanistan to Pakistan and possibly India. Until

around 2007 this option looked increasingly sensible from a Turkmenistani perspective, as it largely dodged the question of Russian–Western rivalry in Central Asia and did not threaten to undermine Gazprom’s control over exports to Europe. The deteriorating situation in Afghanistan has, however, made it much less likely that TAPI will be built in the foreseeable future – unless, that is, the NATO countries and international financial institutions should suddenly be willing to take on the entire financial risk of the project.

- In 1994 Turkmenistan and Iran agreed to build a Turkmenistan–Iran–Turkey–Bulgaria pipeline with an annual capacity of 28 bcm. This, and several subsidiary options for routing onwards from Iran and Turkey, have never been realized, due to the active American resistance. Instead, the USD 190 million Korpeje–Kord–Kuy pipeline from Turkmenistan to Iran was completed in 1997 and includes a 25-year contract for 5–6 bcm per year. Turkmenistan was thus the first, and for several years only, Central Asian natural gas exporter to build a pipeline that circumvented Russia. On the other hand, the small volumes involved and the fact that the gas goes to Iran’s isolated north-eastern market means that it does not pose a threat to Russia.
- The pipeline from Turkmenistan to China currently nearing completion is the longest in the world. It spans 7,000 km, of which 188 are in Turkmenistan, 530 in Uzbekistan, 1,300 in Kazakhstan and over 4,500 in China. With an annual capacity of 30 bcm, this project is more significant than the only other post-Soviet pipeline built by Turkmenistan, the Korpeje–Kord–Kuy pipeline to Iran discussed above.

Russia Offers to Pay More

Perhaps as a result of the looming Turkmenistan–China pipeline and the threat of other pipelines, Russia unexpectedly changed tack during 2007 and 2008. It went from using its virtual transit monopoly on Turkmen gas for the extraction of maximum profits, to a more conciliatory approach in which it offers market prices for Turkmenistani gas. The aim no longer seems to be to maximise Russian profit on Turkmenistan’s exports. Now the grand objective is rather to undermine Western efforts to cobble together enough supply to make the Trans-Caspian Gas Pipeline viable. In this picture, Turkmenistani exports to China are far from the worst thing that could happen to Russia, because they will further weaken the resource base for the Trans-

Caspian Gas Pipeline while also removing incentives for Turkmenistani “adventurism” with Western partners, since another stable source of income is already secured in China. Why should Turkmenistan take the risk of irking Russia by building a trans-Caspian gas pipeline directly to the West when China (and Russia through its increasingly generous pricing) already provides the country with a handsome income?

In addition, both China and Russia have a strong track record of refraining from public criticism of authoritarianism in countries such as Turkmenistan. Russia is not only uncritical about the domestic political situation in Turkmenistan, it has also largely refrained from speaking up for the ethnic Russian minority in the country. Since this minority, numbering about 200,000, has been subject to discriminatory measures far more severe than those inflicted upon the ethnic Russian population in the Baltic states (which received extensive attention from Moscow), it is tempting to interpret this as a consequence of Russia’s interest in Turkmenistani natural gas. It also sends a clear signal to Turkmenistan: as long as you sell your natural gas to us, rather than directly to Western actors, we will not intervene in your domestic affairs at all. Unlike countries such as Ukraine, Georgia and Kazakhstan, Turkmenistan does not share a border with Russia and is also therefore less worried about Russian interventionism.

From the perspective of an authoritarian regime such as that in Ashgabat, clearly both Russia and China have something to offer as energy partners. In this perspective, Turkmenistan’s continued reliance on Russia and gradual diversification to China make sense. On the other hand, Turkmenistan also clearly keeps its authoritarian and semi-authoritarian partners at arm’s length, not least through its accentuated neutral foreign policy. Turkmenistan joined the Non-Aligned States in 1995 and thus achieved recognition by the UN Assembly of its neutrality, seeing this as a means of removing itself from the influence of competing great powers – including Russia. In an overview of the number of treaties signed between the various post-Soviet states and Russia, Kathleen Hancock found that Turkmenistan, along with Georgia, Ukraine and the Baltic states, had signed fewest treaties, and therefore classified it as belonging in the category of states that are “resistant” to Russia in the international arena. By contrast, Kazakhstan, along with Belarus, had joined the most treaties and were categorized as having “friendly” relations with Russia. Although this study is from 2006, while Niyazov was still in power, there

have not been any dramatic changes in Turkmenistan's accession to international treaties with Russia or other countries in recent years. Its foreign policy under Berdymukhamedov has become significantly more active, but still very much multi-vector.

Thus Turkmenistan is not as closely tied to Russia as its continued reliance on Russia as a transit country and prickly unpredictability in negotiations with Western partners over the Trans-Caspian Gas Pipeline might indicate. Hancock's survey, however, covers treaties in all sectors. The main pillar of Turkmenistani-Russian relations is trade in natural gas. And as far as natural gas exports are concerned, Turkmenistan does remain closely tied to Russia. The overall picture is thus one of a balance between continued strong relations with Russia (and expanding cooperation with China) in the energy sector, and at the same time maintaining a clear distance from Russia in overall foreign policy.

Russia and Turkmenistan: Tango for Three

Observers frequently note that Russia is dependent on cheap supplies from Central Asia, and Turkmenistan in particular, in order to maintain its gas balance, its export commitments and its profits from exports to the EU. Russia's situation presumably exacerbates the geopolitical competition between the West and Russia over the states in the South Caucasus and Central Asia. The competition becomes one not only over military bases, Russia's historical sphere of influence and valuable resources, but a struggle for Russia's own energy security and survival. Without Central Asian gas, it is thought, Russia might not have sufficient energy to cover either its export commitments or its domestic consumption. But is this really the case?

Central to finding an answer to this question is Ukraine. The bumpy relationship between Russia and Turkmenistan and the equally volatile relations between Russia and Ukraine need to be understood as part of an integrated trilateral relationship with natural gas as one of its centerpieces. Until 2006, much of Ukraine's gas imports were based on direct trade with Turkmenistan, often involving multiple shady companies and messy barter agreements in which Ukraine paid partly in cash and partly in kind for Turkmenistani gas. Often neither the cash nor even the Ukrainian-produced goods were delivered in full.

The agreement reached after the January 2006 Russian-Ukrainian gas crisis put an end to the direct trade between Turkmenistan and Ukraine. The new setup was based on Gazprom buying gas from Turkmenistan and selling it to only one of the shady

middleman companies (RosUkrEnergo), which ultimately sold it to Ukraine. As we now know, this arrangement did not improve the situation, but instead transformed it into a question of Russian-Ukrainian bilateral relations. The defining aspect of the energy component in these relations is that it is a dual monopoly: Russia enjoys a monopoly on exports to Ukraine, while Ukraine has a stranglehold on around 80 percent of Russian gas exports to the EU. Thus, in energy relations between the two countries, two different forms of pipeline power are pitted against each other: producer power and transit power. The January 2009 natural gas crisis was the most serious confrontation between these two forms of pipeline power ever, anywhere in the world.

The severity of the 2009 crisis as compared to previous spats reflected the mutual desperation of both countries. Ukraine, whose post-Soviet economic survival was hardly possible without massive and painful restructuring in the first place, has been devastated by the global financial crisis. Russia too is suffering badly. As a commodity exporter with ambitious debt-fuelled plans using the stock prices of Russian raw material companies as collateral, Russia has experienced a cascade of problems due to the financial crisis. That is one reason why Gazprom and its biggest shareholder, the Kremlin, have been so adamant about passing on the rising price of Turkmenistani natural gas to the Ukrainian end-customers.

The volumes of gas involved are indicative of the importance of the Turkmenistan-Russia-Ukraine relationship for the greater Eurasian gas balance. Russia produces a total of around 607 bcm of natural gas per year. Turkmenistan exports 48 bcm to Russia, and Ukraine imports a total of 55 bcm from Russia. Thus Russia's imports from Turkmenistan correspond to 87 percent of Russia's exports to Ukraine. The remainder of Russia's exports to Ukraine is more than compensated by Russia's imports from Kazakhstan and Uzbekistan, totaling 16 bcm.

Until 2006, when Turkmenistan and Ukraine formally traded directly with each other and Russia made its profits from chaotic middleman operations, the Turkmenistan-Russia-Ukraine energy chain could relatively easily be distinguished from the issue of Russia's energy balance and its export commitments to the EU. When the relationship was streamlined after the January 2006 gas crisis, Turkmenistan's exports became part of the greater Russian and Eurasian picture. Although there have not been shortfalls of gas in Russia so far, if that should occur, Russia will be dependent on

Central Asia to fill the gap. The fact that Turkmenistan's exports make up only seven percent of Russia's gas balance (or ten percent along with those of Uzbekistan and Kazakhstan) means that it will not be the main factor in any future supply crunch. However, since a possible shortfall in Russian supplies may be only a few percent, those ten marginal percent may be decisive for how Russia manages to deal with the situation.

Russia's decision to pay more for Central Asian gas can be understood partly as a measure to fend off Western competition in Central Asia, and partly as a means of keeping Central Asian gas under its control in order to deal with any future problems with the gas balance. If Russia were to continue selling gas cheaply to Ukraine, it would have to pay the cost of this measure itself. It is therefore paramount for Russia to pass on the bill to Ukraine.

An interesting aspect of the triangular relationship between Turkmenistan, Russia and Ukraine is that Russia previously used the same transit power vis-à-vis Turkmenistan as Ukraine uses vis-à-vis Russia. In this perspective, the proposed Trans-Caspian Natural Gas Pipeline is to Turkmenistan what Nord Stream is to Russia: a way of sidestepping an expensive and risky transit country. The difference between the Turkmenistan–Russia and Russia–Ukraine relationships is that Russia is far bigger and more powerful than Turkmenistan, whereas Ukraine is far smaller and weaker than Russia. This also means that now that Russia has relaxed the use of its transit power in relation to Turkmenistan, it may be able to force Ukraine to follow suit.

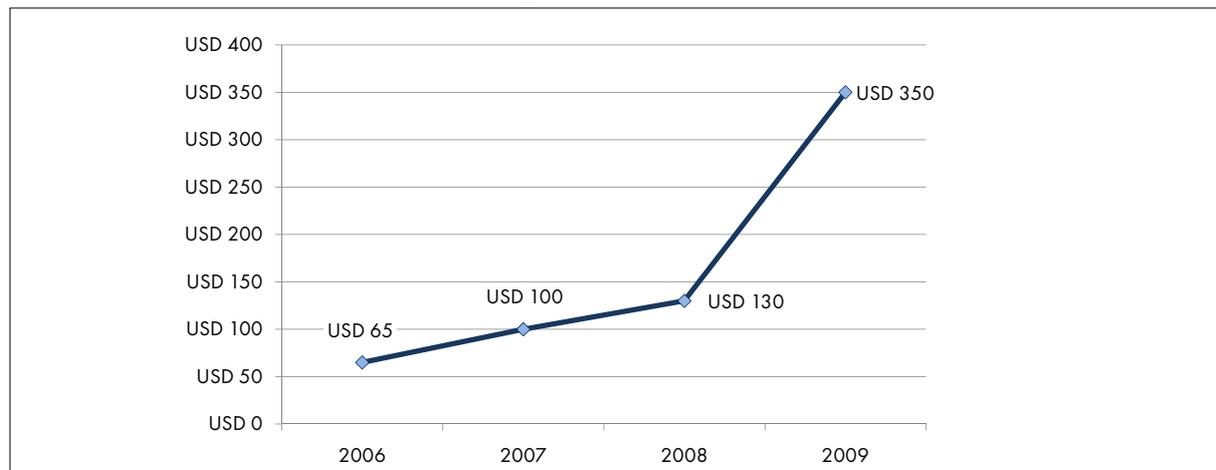
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Further reading

- M. K. Bhadrakumar, "Russia Takes Control over Turkmen (World?) Gas," *Asia Times*, 30 July 2008), http://www.atimes.com/atimes/Central_Asia/JG30Ag01.html.
- Kathleen J. Hancock, "Escaping Russia, Looking to China: Turkmenistan Pins Hopes on China's Thirst for Natural Gas," *China and Eurasia Forum Quarterly* 4, no. 3 (2006): 67-87.
- International Energy Agency (IEA), *Perspectives on Caspian Oil and Gas Development* (Paris: IEA, 2008).
- Simon Pirani, Jonathan Stern, and Katja Yafimava, *The Russian–Ukrainian Gas Dispute of January 2009: A Comprehensive Assessment* (Oxford: Oxford Institute of Energy Studies, 2009).

USD per 1000 m³ of Natural Gas Paid by Russia to Turkmenistan



Sources: based on projections in Mayer, C., "Turkmenistan Emerges as a Serious Natural Gas Player", Penny Sleuth, 2009, <http://www.pennysleuth.com/turkmenistan-emerges-as-serious-natural-gas-player/>, Closson, S. and Perovic, J. "Hope Won't Keep Europe Warm", RFE/RL, 8 January 2009, http://www.rferl.org/content/commentary_Hope_Wont_Keep_Europe_Warm/1367913.htm and International Energy Agency (IEA), *Perspectives on Caspian Oil and Gas Development* (Paris: IEA, 2008).

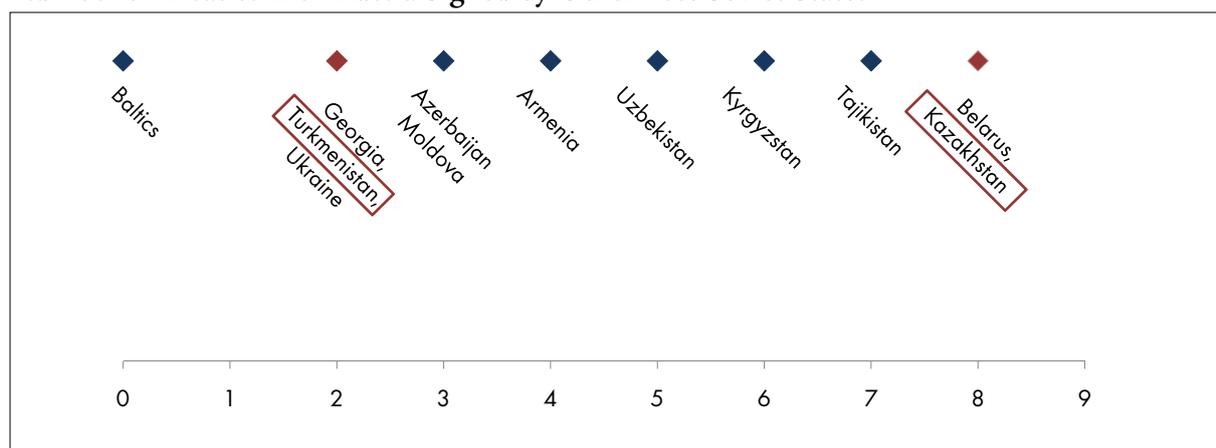
The Importance of Central Asian Natural Gas for the Eurasian Gas Balance (in Billions of Cubic Meters)

Russia's total production	607 bcm*
Turkmenistan's exports to Russia	48 bcm*
Kazakhstan's exports to Russia	5 bcm*
Uzbekistan's exports to Russia	11 bcm*
Ukraine's imports from Russia	55 bcm**
Russia's exports to the EU	148 bcm*

NB: * figures for 2007, ** figures for 2008

Sources: Russia's total production and Russia's exports to the EU: BP Statistical Review of World Energy (London: BP, 2008): 24 and 30, respectively; Turkmenistan, Kazakhstan, and Uzbekistan: International Energy Agency (IEA), Perspectives on Caspian Oil and Gas Development (Paris: IEA, 2008): 10; Ukraine: Simon Pirani, Jonathan Stern, and Katja Yafimava, The Russian-Ukrainian Gas Dispute of January 2009: A Comprehensive Assessment (Oxford: Oxford Institute of Energy Studies, 2009): 6.

Number of Treaties with Russia Signed by Other Post-Soviet States



Source: Hancock, K., "Bringing Economics back in: How Relation-Specific Assets Shed Light on Russia--Turkmenistan Economic Relations", paper presented at the annual meeting of the International Studies Association, San Diego, California, 22 March 2006: http://www.allacademic.com/meta/p_mla_ap_a_research_citation/0/9/9/2/3/p99238_index.html : 1.

The articles in this issue of the Russian Analytical Digest were written as part of the research project "RUSSCASP – Russian and Caspian energy developments", financed by the PETROSAM program of the Research Council of Norway. The project is carried out with the Fridtjof Nansen Institute, the Norwegian Institute for International Affairs and Eon Pöyry as consortium partners and also includes other institutions and researchers.