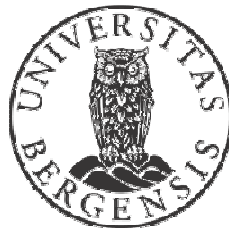


**Russian Energy Aggression 2000-2008:
A Multiple Case Study of Russian Energy Aggression
During Vladimir Putin's Presidency**

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”Aside from military defence, there is no project of more central importance to national security and indeed independence as a sovereign nation than energy security”
-Henry Kissinger-

Abstract

This thesis seeks to explain what triggered cases of Russian energy aggression during Vladimir Putin's presidency. Previous studies on the subject have largely focused on single cases or a small sample of cases, whereas this thesis has performed a comparative multiple case study on 13 cases of Russian energy aggression in seven former Soviet Union republics (Belarus, Estonia, Georgia, Latvia, Lithuania, Moldova and Ukraine). The thesis addresses the research question through an analysis of three hypotheses. The hypotheses are concerned with whether economic interests, political considerations, or interest in energy infrastructure triggered the cases of Russian energy aggression.

The comparative analysis shows that although all three hypotheses to a varying degree explain two or more cases of Russian energy aggression, the relative merit of the hypotheses shows that interest in energy infrastructure is the strongest explanatory variable. Nine out of 13 cases are primarily or secondarily explained by Russian interest in energy infrastructure. The dissolution of the Soviet Union left Russia in a situation where it no longer controlled the distribution network of oil and gas exports to Europe. The importance of oil and gas revenues for the Russian economy increased throughout Putin's presidency, which led the Russian state to exert energy aggression on neighbouring countries through state-controlled companies in order to acquire ownership in their oil and gas infrastructure.

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List of Abbreviations

CEO	Chief executive officer
CFE	Treaty on Convention Armed Forces in Europe
CIS	Commonwealth of Independent States
ECT	Energy Charter Treaty
EU	The European Union
FPC	Foreign Policy Concept
FSU	Former Soviet Union
IPAP	Individual Partnership Action Plan
MAP	Membership Action Plan
NATO	North Atlantic Treaty Organization
NGO	Non-governmental organisation
NSC	National Security Concept
OPEC	Organization of Petroleum Exporting Countries
OSCE	Organization for Security and Co-operation in Europe
RFE/RL	Radio Free Europe/Radio Liberty
UN	United Nations
USSR	Union of Soviet Socialist Republics

Units of Measure

bcm	billion cubic meters
mcm	million cubic meters
tcm	thousand cubic meters

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Bergen, 4 October 2009
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Map 1: Russia and the European former Soviet Republics



Source: http://www.lib.utexas.edu/maps/commonwealth/cis_europe_pol_2003.jpg [Map Segment].

Chapter 1: Introduction

1.1 Theme and Motivations

The purpose of this thesis is to analyse cases of Russian energy aggression during Vladimir Putin's presidency. The research question is *what triggers Russian energy aggression?*

Russian energy aggression is in this thesis understood as Russian energy cut offs of oil and gas supplies and threats of oil and gas cut offs¹. The research question will be answered by a multiple case study analysis.

After Vladimir Putin became president of the Russian Federation on New Year's Eve 1999, Russian energy policy has had a markedly different outlook than that of his predecessor Boris Yeltsin. This thesis is built on an analysis of 13 cases of Russian energy aggression in seven countries, all former Soviet Union republics (FSU). These are Belarus, Estonia, Georgia, Latvia, Lithuania, Moldova and Ukraine, which are considered as 'Russia's sphere of influence' by Putin. Common to these countries are their dependency on Russian oil and gas supplies, with little or no energy resources of their own. Their energy dependency on Russia comes as a result of the Russian Republic's role as the hub for oil and gas supplies to the other republics in the Soviet Union. The FSU states are as a result connected to the Russian pipeline system, with limited diversification possibilities. The upturn in oil and gas prices during Putin's presidency has radically changed Russia. While Russia was weak politically and economically under Yeltsin's presidency, the increased energy revenues have led to a strengthening of the Russian state domestically and internationally. Russia under Putin has acted far more assertively and aggressively in promoting her interests. One of the tools available to the Russian state has been to use oil and gas deliveries as a foreign policy leverage, where the state-owned pipeline monopolies Gazprom and Transneft have had an important role. Putin has himself stated that Gazprom is "a powerful lever of Russia's economic and political influence in the world" (President of Russia 14 February 2003).

1.2 Purpose of the thesis

The purpose of this thesis is to generate new knowledge regarding Russian energy aggression. Whereas previous studies have largely focused on single cases or a small sample of cases², this thesis will perform a multiple case study of a large sample of cases of Russian energy

¹ Clarification of terminology: while both gas and natural gas is used in the literature, I have chosen to use gas in this thesis.

² I discuss previous studies in section 2.2.2.

aggression in order to see if there is a pattern in what triggers it³. The thesis takes the form of a hypotheses-generating study in the sense that no theories have previously been developed on the subject. Without any established theories that may serve as a starting point for this analysis, this thesis will attempt to establish some preliminary hypotheses. By analysing the hypotheses, which will be presented in chapter two, the thesis seeks to identify independent variables that may explain the cases of Russian energy aggression. The thesis will also discuss the relative merit of the hypotheses in chapter eight. By discussing the ranking order of the hypotheses, the thesis also contains an element of hypotheses-testing.

1.3 Why Study Russian Aggression?

Russia has the world's largest gas reserves, and is currently the second largest exporter of oil. Oil and gas resources are among the basic commodities in any society. When oil and gas supplies are disrupted, it has important consequences for the countries that are subject to the disruption. The importance of stable oil and gas supplies gives the exporter a leverage that can be exploited vis-à-vis the inflicted countries, which is seen in Putin's own admission that Gazprom is a powerful lever for the Russian state. Considering the importance of Russia's role as an oil and gas exporter, it is therefore important to gain more knowledge regarding the factors that trigger Russian energy aggression. Is it economic interests, political considerations, or an attempt to acquire energy infrastructure in the inflicted countries? These questions are the basis for the hypotheses that I will return to in chapter two.

1.4 Contributions of the Thesis

First of all, the main contribution of this thesis is to generate new knowledge regarding Russian energy aggression during Vladimir Putin's presidency. Due to the lack of a comparative multiple case study analysis of a large sample of cases of Russian energy aggression, there is insufficient knowledge regarding this topic. Second, the thesis can also serve as a starting point for an analysis of case of Russian energy aggression beyond Putin's presidency. January 2009 saw a repeat of the Russian-Ukrainian gas dispute of January 2006, less than a year into Dmitry Medvedev's presidency. The relevance of the thesis' contribution is also greater as Vladimir Putin has continued to serve as Prime Minister in Medvedev's government.

³ Not all cases of Russian energy aggression are included. I will deal with this question in chapter two.

1.5 Outline of the Thesis

Chapter two will discuss the multiple case study method that is applied in the thesis. Besides defining the case study method and discussing how this thesis is comparative in nature, it will also discuss what type of case study the thesis is based on and the strengths and weaknesses of the method. Chapter two will also outline and discuss three hypotheses that will serve as the starting point for the analysis later in the thesis. Chapter three will provide the reader with an empirical knowledge of the Russian oil and gas sector. The chapter will begin with an outline of how Vladimir Putin established the power-vertical and his view on energy policy. Next, I will outline the development in ownership and control and the renationalisation of the Russian oil and gas sector, and then turn to an outline of the Russian pipeline system and the importance of oil and gas revenues for the Russian state. Next, chapter four will outline three policy documents that can contribute to the understanding of Russian energy aggression. The three policy documents are the 2000 Russian National Security Concept, Russia's Foreign Policy Concept, and the Energy Strategy of Russia for the Period up to 2020.

Chapter five covers the major issues that concern Russia's relationship with the seven countries that have been subject to Russian energy aggression. The purpose of the chapter is to provide the reader with a more intimate knowledge of issues that may have triggered the cases. Next, the 13 cases of Russian energy aggression will be outlined in chapter six. The focus will be on how the cases of Russian energy aggression unfolded, and on which proposals and statements were made during the negotiations. Chapter seven will then turn to the hypotheses presented in chapter two, and analyse the 13 cases of Russian energy aggression based on the information in the preceding chapters. The purpose of chapter seven is to see if there is a pattern in what triggers the cases of Russian energy aggression. Finally, chapter eight will summarise and present the main findings of the analysis. The chapter will also discuss the relative merit of the hypotheses, and discuss the limitations of the findings and elaborate on future studies on the subject.

Chapter 2: Research Design

2.1 Introduction

The main purpose of this chapter is to outline and discuss various aspects of the case study method and to outline and to outline and discuss the three hypotheses in the thesis. The chapter will begin by defining the case study method, and will then discuss how this thesis is comparative in nature. Next, I will clarify what type of study this thesis is. I will also discuss the strengths and weaknesses of the case study method, and then briefly discuss the thesis' data sources. Finally, the last part of the thesis will present the variables in the thesis, and then outline and discuss the hypotheses.

2.2 The Case Study Method

Gerring defines a case study as “an intensive study of a single unit for the purpose of understanding a larger class of (similar) units” (2004: 341). A case is here understood as a “spatially delimited phenomenon (a unit) observed at a single point in time or over some period of time” (Gerring 2007: 19). Whereas a case study entails an intensive study of one case, this thesis includes seven different countries that have been subject to Russian energy aggression; hence it is a *multiple case study*. The multiple case study shares the same characteristics as the case study, but is different from a cross-case analysis. Gerring notes that the distinction between case study and cross-case study is a matter of degree: “The fewer cases there are, and the more intensively they are studied, the more a work merits the appellation “case study” (Gerring 2007: 20).

2.2.1 The Case Study Method as a Comparative Method

Ragin notes that comparison provides a basis for “making statements about empirical regularities and for evaluating and interpreting cases” (1987: 1). Comparison enables us to identify similarities and differences that are vital to understanding, explaining, and interpreting historical outcomes and their significance. The comparative method may be narrowly defined as analytical strategies that are used in situations with few cases and potentially many explanatory variables (Østerud, Goldmann and Pedersen ed. 2004). While the case study method is not considered as one of the comparative methods per se⁴, Lijphart stresses the importance of the case study method as a comparative method, which brings me to the reason behind the comparative nature of this thesis. First, while the cases are initially

⁴ Lijphart (1971) identifies the comparative method, the experimental method, the statistical method and the case study method as the basic methods of establishing general empirical propositions.

analysed separately in order to see what triggered the cases of Russian energy aggression, the cases are also analysed together in order to see if there is a pattern in what triggers Russian energy aggression. Furthermore, after having concluded the analysis of the hypotheses, chapter eight will discuss the relative merit of the hypotheses in order to reveal which of the hypotheses has the greatest explanatory power with regards to Russian energy aggression.

2.2.2 What Type of Case Study?

This thesis has come to fruition due to a lack of a comparative analysis of a large sample of cases of Russian energy aggression during Vladimir Putin's presidency. The common practice so far has been single case studies or small sample case studies, and no theories have been established that attempts to explain energy aggression. Goldman (2008) and Lucas (2009) look at how Russia has used the energy weapon towards neighbouring countries. However, Goldman's and Lucas' approach is not comparative in nature, and their focus is primarily on recent cases of Russian energy aggression. Larsson (2006) focuses on Russia's foreign energy policy, with a special focus on Russia's reliability as an energy supplier⁵. Since Larsson's report was written in 2006, it only encompasses seven out of the 13 cases included in this thesis. The Russian-Ukrainian gas dispute in January 2006 has been subject to the greatest attention in the literature⁶. Furthermore, Bruce (2005) has studied Russia's gas relationship with Belarus, and emphasises Gazprom's interest in BelTransGaz as an explanatory factor for the cases of Russian energy aggression towards Belarus in 2002 and 2004⁷. The respective authors' views on the cases of Russian energy aggression will be discussed as I turn to the analysis in chapter seven.

Although the case study method cannot provide the basis for a valid generalisation or the rejection of an established generalisation, Lijphart (1971) states that "case studies can make an important contribution to the establishment of general propositions and thus to theory-building in political science" (1971: 691). Lijphart operates with six ideal types of case studies, where one of them is the hypothesis-generating case study⁸. Lijphart states that the

⁵ Larsson does not only focus on oil and gas supplies, but also how Russia's electricity monopolist United Energy System has been used in a similar way to Gazprom and Transneft.

⁶ Goldman, Larsson and Lucas discuss the Ukrainian case, and note the connection between Ukraine's supply disruption and Ukraine's 'defection to the West' and Gazprom's interest in Ukraine's pipeline system. Moreover, several single case studies have also analysed the dispute, such as Stern (2006) and Koren and Bukkvoll (2007).

⁷ Main (2006) and Stern (2007) also analyse cases of Russian energy aggression towards Belarus.

⁸ The other five case studies are atheoretical case studies, interpretative case studies, theory-confirming case studies, theory-infirming case studies, and deviant case studies.

objective of hypothesis-generating case studies is “to develop theoretical generalizations in areas where no theory exists. Such case studies are of great theoretical value” (1971: 692).

This thesis will contain an element of hypothesis-generating in the sense that no theory has been developed on the literature of energy aggression. The lack of theories on the subject explains why no theory chapter is included in this thesis. A more fruitful approach will be to discuss and clarify hypotheses. I will discuss in section 2.5 how the hypotheses have been established. Those hypotheses will attempt to identify independent variables that may explain Russian energy aggression. Moreover, since the thesis in chapter eight will discuss the relative merit of the hypotheses, it can also be said to contain an element of hypothesis-testing. The thesis will not be hypothesis-testing in the meaning of testing already established theories on new empirical data, where hypotheses are either rejected or found significant. Instead, it will be hypothesis-testing in the sense that the thesis will discuss the hypotheses’ ranking order in order to see which of the hypotheses have the greatest explanatory power. When the analysis suggests more than one hypothesis may explain the case of energy aggression, I will operate with primarily and secondarily explanation. Although the thesis includes a relatively low number of cases, and cannot compare to large-N hypothesis-testing studies, the thesis’ findings will have a high validity with regards to explaining what triggered cases of Russian energy aggression in Vladimir Putin's presidency. This will be a first step towards evaluating Russian energy aggression based on what the 13 cases have in common, which in turn will allow me to draw a conclusion on the thesis’ research question.

2.2.3 Strength and Weaknesses of the Case Study Method

Gerring has identified ten trade-offs that are inherent in case studies relative to large-N cross-case studies. However, I will only discuss eight of them due to the uncertain nature of the last two trade-offs⁹. The eight trade off are divided into two categories: four concerning research goals, and four concerning empirical factors. The respective trade-offs are summarised in Table 1 on the next page, and will now be discussed in relation to this thesis.

The first trade-off concerns whether the thesis is a *hypothesis-generating study or hypothesis-testing study*. I have already discussed in section 2.2.2 that this thesis contains an element of both hypothesis-generating and hypothesis-testing. However, it would be wrong to categorize

⁹ Gerring openly admits the uncertain nature of the two last trade-offs. The trade-offs concerned are *causal complexity* and *state of the field*. They are identified as two additional factors where the affinity is indeterminate with regard to the case study method or the cross-case study method.

my approach as a clear example of either approach. Gerring notes that many of today’s classic studies were born from the introduction of a new idea which has since been subject to rigorous analysis, although the initial study may not cover all relevant aspects. Gerring argues that case studies have a natural advantage in exploratory studies, while large-N studies allow for more rigorous testing of already established hypotheses. Hence, while the thesis has an exploratory nature in the sense that it will analyse Russian energy aggression on the basis of three preliminary established hypotheses, it will also contain an element of hypotheses-testing as it discusses the relative merit of the hypotheses.

Table 1: Case Study Method

Affinity		
Research Goal	Case Study	Cross-case Study
1. Hypothesis	Generating	Testing
2. Validity	Internal	External
3. Causal Insight	Mechanisms	Effects
4. Scope of proposition	Deep	Broad
Empirical Factors		
5. Population of Cases	Heterogeneous	Homogeneous
6. Causal Strength	Strong	Weak
7. Useful Variation	Rare	Common
8. Data Availability	Concentrated	Dispersed

Source: modified version of table 3.1 in Gerring (2007: 38).

The next trade-off concerns *external and internal validity*. High internal validity is achieved when the findings have a high validity for the sample under study, while high external validity is achieved when the findings can be transferred to a larger population. Since this thesis is concerned with explaining a large sample of cases of Russian energy aggression under Vladimir Putin's presidency, it can be said to have a high internal validity for the sample in question, but a low external validity as the findings cannot be generalised to all cases of energy aggression.

The third trade-off deals with *causal insight*. Gerring notes that “Case studies, if well constructed, may allow one to peer into the box of causality to locate the intermediate factors lying between some structural cause and its purported effect.” (2007: 45). Gerring does not exclude the possibility that case studies can be used to discover causal effects, but concedes that case studies are commonly used to uncover causal mechanisms. This is also the case of this thesis, as it describes the causal mechanisms in play as it questions what triggers Russian

energy aggression. The fourth trade-off concerns the *scope of the study*, whether the study is extensive or intensive. The case study method implicitly involves an intensive study of the cases. Ultimately, Gerring asserts that this trade-off concerns “knowing more about less, or less about more” (Gerring 2007: 49). This thesis is limited in time as only cases of Russian energy aggression during Vladimir Putin’s presidency are included. Moreover, a lack of literature on a small sample of cases of Russian energy aggression early in Putin’s presidency renders them difficult to analyse, and they are as a result not included in the thesis. Only those cases that are possible to analyse have been included¹⁰. Although not all cases are included in the thesis, the great majority of cases are. Furthermore, the sample of cases is large enough to make a vital contribution to the understanding of Russian energy aggression.

The next four trade-offs deal with empirical factors. The fifth trade-off addresses the nature of the *population of cases*, whether they are heterogeneous or homogeneous. Gerring notes that the population of cases largely comes down to a trade-off between numbers of observations and number of variables. The larger the population of cases, the less likelihood they are comparable due to their heterogeneous nature. The population of cases in this thesis is homogenous, as the cases have been selected on the dependent variable. No ‘negative cases’ of Russian energy aggression is included, as it would be impossible to define what a negative case of Russian energy aggression is. The thesis’ approach resembles in this manner the approach in most different systems design (MDS), which is based on Mill’s method of Agreement. The method of agreement identifies all instances of a phenomenon, and attempts to determine which of the causal variables is constant all in all cases. The method suffers from multiple causation, as it fails to explain when several factors may explain the outcome in the dependent variable (Ragin 1987 and Landman 2003). The sixth trade-off concerns the *causal strength*, whether the relationship between variables are deterministic or probabilistic. Deterministic is here understood as X is assumed to be necessary and/or sufficient for Y’s occurrence. Probabilistic, in turn, relates to events where X is assumed to lead to the occurrence of Y. The nature of this thesis is of the latter variant. The findings can hardly be said to be of a deterministic character due to the complexity of the cases and numerous variables. I will instead argue that the thesis’ findings are probabilistic as it is *likely* that the variables I have identified have triggered the cases of Russian energy aggression.

¹⁰ The lack of literature on the cases can be primarily explained by the lack of interest for earlier cases of Russian energy aggression.

The seventh trade-off deals with *variation of evidence* from available cases. Gerring notes that case studies are common where evidence and previous knowledge are rare. The lack of established theories and the lack of comparative literature on a large sample of cases of Russian energy aggression make the case study the most useful method of analysis for this thesis. The eighth and final empirical trade-off concerns *data availability*. The case study method is best suited when the available data is rich and where it is not possible to code the data into single numbers such as in large-N studies. If the case study contributes to new knowledge and clarification of the topic at hand, this may in turn make a large-N study more plausible at a later stage. This is the case for this thesis, as I have already established the lack of literature on the subject.

2.3 Data Sources

The data sources for this thesis are threefold: books and articles, reports and papers, and internet resources. The majority of the literature is derived from internet articles, most importantly from internet journals like Eurasia Daily Monitor and RFE/RL, due to the large amount of information that has been needed to sufficiently cover the 13 cases of Russian energy aggression. The internet articles have been invaluable in terms of providing facts regarding coverage of political events and as a source for statements and other pieces of information that are important for the understanding of the cases. Another aspect with regards to the sources is the linguistic limitations. Since I do not possess knowledge of the Russian language, I have had access to primary sources in Russian. I have as a result had to rely on translated versions of the three policy documents that I outline in chapter four. Nor have I had access to academic articles and news sources in Russian, which means that I have had to rely on Russian-based English-written sources like Eurasia Daily Monitor and RFE/RL.

2.4 Observations and Variables

This thesis rests on an analysis of 13 observations (N=13) in seven countries. Observations may also be referred to as the units of analysis, which in this thesis are specific *cases of Russian energy aggression*. I have already noted that Russian energy aggression is defined as cut-offs of oil and gas supplies and threats of cut-offs of oil and gas supplies. The cases of Russian energy aggression are limited in time, as only cases identified during Vladimir Putin's presidency are included in the thesis. The countries were selected on the basis of whether or not they were targeted by Russian energy aggression. Based on this procedure, some cases were omitted from the thesis. I have already noted that the thesis is non-exhaustive since not all cases of Russian energy aggression are sufficiently covered in the

literature for them to be analysed. Consequently, I have omitted an incident in Georgia in January 2006, when two Georgian pipelines were blown up by TNT explosions. The literature on the incident is inconclusive, although several analysts seem to agree that it is not a case of Russian energy aggression. I have also omitted Armenia from the analysis. While Armenia was offered a lower gas price in return for energy infrastructure, Gazprom's offer was not combined with a supply threat, hence the exclusion of Armenia from the analysis.

As I now have identified the units of analysis, it is time to turn to the variables in the thesis. Gerring notes that "A single observation may be understood as containing several dimensions, each of which may be measured as a variable" (2007: 20). Landman defines variables as "those concepts whose values change over a given set of units" (2003: 17). Variables are divided into dependent and independent variables. The dependent variable refers to what the researcher is trying to explain, which in this thesis is what triggers Russian energy aggression; hence, the *dependent variable is Russian energy aggression*. Independent variables are those factors which supposedly explain the dependent variable. The purpose of this thesis is to identify which of the independent variables that can explain what triggers Russian energy aggression. I will now present the independent variables. The background for why they are included will be dealt with as I outline and discuss the hypotheses:

1. Economic interests.
2. Leaving Russia's sphere of influence.
3. Interest in energy infrastructure in targeted states.

2.5 Hypotheses

I will now present the three hypotheses in this thesis that will serve as the starting point for the analysis in chapter seven. With each of the three hypotheses, I will begin with a discussion of how the hypotheses were conceived. Common for all three hypotheses is their inductive nature, as the hypotheses have not based on already established theories. Next, all three hypotheses will also be discussed in a context in order to provide the reader with more information regarding the background of the hypotheses.

2.5.1 H₁: *Russian companies will exert energy aggression due to economic interests*

H₁ is based on explanations used by Russian state officials and Russian energy company officials to explain cases of Russian energy aggression. The hypothesis states that Russian companies will exert energy aggression due to economic interests, and the argument in this hypothesis is that Russian energy aggression occurs in cases where Russian companies are not

successful in defending their economic interests. Economic interests are here understood as a stop to subsidising countries with cheap gas by introducing market principles, collecting energy-related debts, and using energy aggression as a pretext for seeking lower tariffs and taxes in transit countries. Russia had since the dissolution of the Soviet Union provided the FSU states with markedly cheaper gas than Western European countries. Russia's practice of subsidising FSU states changed in 2004, when Gazprom stated it wanted to change to a market based pricing system¹¹. Russia's new policy became particularly evident in 2005 when the FSU states' gas contracts for 2006 were negotiated. Alexei Miller stated in December 2005 that Gazprom applied market principles to "all foreign partners without exception" (RFE/RL 12 December 2005). Moreover, Transneft has also opted to stop oil exports citing too high costs using the FSU states' oil terminals. Transneft halted Ventspils Nafta's oil shipments in 2002-2003 on the pretext of too high tariffs using the terminal.

2.5.2 H₂: *Russia will exert energy aggression towards countries that leave its sphere of influence*

H₂ is conceived on the basis of what Russian policy documents state and what Russian officials have said with regards to foreign policy interests. The argument in H₂ is that countries that 'leave Russia's sphere of influence' will be punished by Russian energy aggression. Before I turn to the reasoning behind this hypothesis, I will clarify what is considered Russia's sphere of influence and how 'leaving Russia's sphere of influence' shall be perceived. Russia's Foreign Policy Concept (FPC) states that the Commonwealth of Independent States (CIS) is Russia's highest foreign policy priority, and Putin stated in 2003 that "we see the CIS area as the sphere of our strategic interests" (President of Russia May 16, 2003). Countries that leave Russia's sphere of influence are understood as CIS states seeking political/economic, and/or military cooperation with other countries than Russia, or countries that fail to make any progress in establishing a closer relationship with Russia. Leaving Russia's sphere of influence is also understood as countries seeking to decrease their economic dependency on Russia, particularly by joining the EU.

Russia is especially wary of FSU states seeking a closer relationship with NATO and the United States, as they are considered security threats to Russia. Russia's National Security Concept (NSC) is above all concerned with Russia's eastward expansion, which by 2004 had

¹¹ Market based pricing system is here understood as the same price as Western European countries pay.

brought three FSU states into the organisation¹². Viktor Yushchenko, who was elected Ukrainian president in December 2004, expressed an interest Ukrainian NATO membership, after which Russian authorities warned Ukraine that it would have consequences for her relationship with Russia. Russia's Foreign Minister Sergei Lavrov said that while Russia would not obstruct Ukraine's right to choose its own partners, Ukraine could not rely on privileged economic relations with Russia (RFE/RL 4 January 2005). Moreover, the FPC states that NATO's guidelines do not coincide and sometimes contradict Russian security interests. The United States is also considered a security threat due to its unipolar actions at the international stage, and for overstepping its boundaries and meddling in other countries' affairs. Russia has been particularly critical of the United States' support to the coloured revolutions in Georgia and Ukraine, and for providing military support to Georgia. The FPC also emphasises a good-neighbourly-belt around Russia, which is considered important for Russia's political stability (Ministry of Foreign Affairs of the Russian Federation 2000 and President of Russia 10 February 2007). The FPC states that "Russia must be prepared to utilize all its available economic levers and resources for upholding its national interests" (Ministry of Foreign Affairs of the Russian Federation 2000). Russia's greatest economic leverage is its oil and gas resources, which is further increased by many of the FSU states' dependency on Russian oil and gas deliveries. No country can function without adequate energy supplies, which renders control over energy resources a powerful leverage.

2.5.3 H₃: Russian companies will exert energy aggression in order to acquire energy infrastructure

H₃ has been generated on the basis of Russia's dependency on independent countries for its oil and gas exports to Europe. H₃ states that Russian companies will exert energy aggression in order to acquire energy infrastructure. Energy infrastructure is here understood as oil and gas pipelines, oil refineries, and terminals used for oil exports. The Russian economy has experienced a strong growth during Vladimir Putin's presidency, which can be largely explained by Russia's increased revenues from oil and gas exports during his tenure, above all oil and gas exports to Europe. Although gas exports to Europe only constitute one-third of Gazprom's gas exports, roughly two-thirds of Gazprom's revenues come from the European market. If we take a look at Map 2 on p. 23, we will see that oil and gas exports to Europe have to be transported through pipelines in independent countries, or be shipped through oil terminals in the Baltic States. The pipelines that serve as Russia's main export channel for oil

¹² The Baltic States became members of both NATO and the EU in 2004.

and gas exports to Europe were formerly part of the unitary pipeline system owned by the Soviet Union. However, the dissolution of the Soviet Union saw the newly independent countries acquire ownership of pipelines and other forms of oil and gas infrastructure on their soil. This has left Russia in a situation where it does not control the distribution network, nor does Russia possess enough refining capacity of its own.

Being dependent on foreign countries for energy exports is considered problematic for Russia. Russia's energy strategy highlights Russia's export ability as important for Russia's economic safety. Moreover, it calls on "state and private entities to exert pressure on regional states to ease Russia's access to the international markets" (Stulberg 2007: 98). The dramatic upturn in oil and gas prices after the turn of the century has proved extremely important for the Russian economy. While the oil price at the time of the Russian financial crisis in 1998 was 11.19 \$/barrel, it had increased to 106.95 \$/barrel at the end of Vladimir Putin's presidency in 2008. However, these prices are on the international market, and both Russian oil and gas is sold at below market price in Russia¹³. Hence, export safety is vital for the Russian economy. The pipelines have also been a source of blackmail and theft for Russia. Overland argues that "the country where the pipeline is located will ultimately have the power to do things with the pipeline" (RFE/RL 10 January 2007). By acquiring the distribution network, including oil terminals, Russia secures its oil and gas exports to Europe as no foreign countries may disrupt the exports. Moreover, Russia's oil revenues would increase if a larger share of Russia's oil production was refined by Russian oil refineries. Vahtra notes that "By acquiring upstream assets, refineries and sales outlets abroad, Russian companies have achieved better control over foreign markets and demand, processing oil in their own refineries and selling the products via their own petroleum stations" (2005: 14).

¹³ See section 3.6.3 for detailed information regarding Russia's dependency on oil and gas exports.

Chapter 3: The Russian Oil and Gas Sector

3.1 Introduction

This chapter will serve as an empirical background chapter on the Russian oil and gas sector that will provide information which will contribute to the understanding of the analysis in chapter seven. I will start with a discussion regarding Vladimir Putin's achievements as Russian president and his view on energy policy. I will also briefly discuss the presence of the siloviki in Putin's administration. Next, I will deal with the implications of the privatisation of the Russian economy that took place during the 1990s, and the renationalisation process of the energy sector which started with Putin's crackdown on Yukos in 2003. The majority of the cases of Russian energy aggression have taken place *after* the Russian state consolidated its control over the energy sector. I will then turn to the Russian pipeline monopolies, and discuss how pipelines can be used as a power instrument. Twelve out of 13 cases of Russian energy aggression have been executed by exerting pipeline pressure by cutting or threatening oil and gas supplies. Finally, the last part of this chapter will be devoted to outlining the extent of Russia's oil and gas resources, and a discussion of the importance of oil and gas exports for the Russian economy.

3.2 Vladimir Putin

As this thesis is concerned with cases of Russian energy aggression during Vladimir Putin's Presidency, it is natural to provide a brief outline of Putin's policies and his view on energy policy. Putin was a largely unknown entity when he became acting president following Boris Yeltsin's resignation as Russian president on New Year's Eve 1999. Putin was subsequently elected president of the Russian Federation in March 2000. Boris Yeltsin had been elected president of the Russian Soviet Federative Socialist Republic (RSFSR) in June 1991 while Russia was still under Soviet rule. Yeltsin's rule as Russian president was a troublesome period in Russia's history. Russia experienced the August 1991 coup d'état staged by communist putschists, the violent dissolution of the Supreme Soviet and the Congress of People's Deputies (CDP) in October 1993, two Chechen wars (1994-1996 and 1999-2000), and the Russian financial crisis in August 1998 (Sakwa 2002). Russia's standing on the international stage in this period was severely weakened, and the country was no longer a powerful actor. Unable to demonstrate itself as an attractive partner, several of the FSU states turned to Europe for support despite Russian attempts to keep them close to Russia. While Yeltsin's policies and demeanour will be closely linked with the troubled the

Russian state experienced during the 1990s, Putin's presidency will be synonymous with the resurrection of the Russian state in the 2000s. Putin's first move was to strengthen the Russian state. This task was largely completed by 2003, when he turned his attention to the energy sector.

3.2.1 Establishing the Power-Vertical

Vladimir Putin started working in Boris Yeltsin's presidential administration in 1996, and was appointed head of the FSB, Russia's security service, in July 1998. Putin then became Russian Prime Minister in August 1999 after several leading Russian politicians had not been deemed fit by Yeltsin to succeed him as president. Putin soon emerged as the leading presidential candidate, and received high approval ratings¹⁴. After Yeltsin's resignation as president of the Russian Federation on New Year's Eve 1999, Putin served as acting president until the presidential election was held in March 2000. The March 2000 saw Putin elected Russian president with 52.94 percent of the votes. The political landscape when Putin was elected president had a completely different outlook than the one Yeltsin governed in. While Yeltsin had to deal with a severely fragmented Duma, the heavily orchestrated December 1999 Duma elections saw the formation of a parliamentary coalition supportive of Putin. The December 2003 election further enhanced Putin's parliamentary support as his bloc won a two-thirds majority in the Duma. These election results provided Putin with the power to oversee radical changes in Russia (White in White, Gitelman and Sakwa 2005).

Putin's first task as the new Russian president was to strengthen the Russian state. Yeltsin's tenure had seen Russia become a weak and fragile state, domestically and internationally, and Putin considered a strong centre as vital for the restoration of the Russian state. Regional leaders had under Yeltsin gained strong independence from central powers, and Sakwa notes that several regions had by the end of Yeltsin's tenure made sovereignty claims vis-à-vis Moscow. Chechnya is the most prominent case of a Russian break-away region. Russia and Chechnya had already been at war once following Chechnya's declaration of independence in November 1991, and Putin initiated the Second Chechen War in August 1999. Putin also

¹⁴ Sakwa points to several factors for Putin's emergence: the Second Chechen War, which unlike the first Chechen war proved popular in the Russian population; an unprecedented power over policy-making his predecessors did not enjoy as Prime Minister; economic recovery due to higher oil prices; and Putin's appearance as someone who would be able to restore Russia's national dignity (Sakwa 2008).

eliminated unofficial and official asymmetry in federal-regional relations¹⁵, and created seven federal districts led by presidentially appointed representatives which serve as an administrative layer between the federal centre and the regions¹⁶. Putin has also adopted a bill which allows the Russian president to dismiss regional leaders that violate regional laws, and used the Beslan tragedy in 2004 as a pretext for a new law whereby regional leaders now will be appointed by the president¹⁷. The Russian media has also been subject to pressure from Russian authorities. Following Putin's crackdown on the oligarchs, which I will discuss in section 3.3, the Russian state and state-owned companies acquired ownership in all three nationwide television networks (Goldman 2008).

3.2.2 The Putin Thesis and Putin's view on the role of Energy

Vladimir Putin wrote in 1996 a PhD dissertation titled "Mineral Raw Materials in the Strategy of Development of the Russian Economy" while studying at St. Petersburg State Mining Institute¹⁸. Although Putin is credited with writing the thesis, Olcott questions whether Putin himself has written the dissertation as he at the time was a senior official in Yeltsin's administration¹⁹. However, as Olcott argues, "Whether or not Putin wrote it himself, he obviously authorized its publication in his name and so subscribed to its contents. He endorsed the contents with knowledge of his political future" (2004: 17). Putin's thesis emphasises the role of the state in the energy sector, and argues that "state planning must be at the core of Russia's resource management" (Olcott 2004: 17). Putin further writes that "the state has the right to regulate the process of the acquisition and the use of natural resources, and particularly mineral resources" (Olcott 2004: 19). Private companies must consequently act within the framework provided by the state, or risk losing their assets if they do not. While Putin's thesis provides support for private ownership and seeks a level playing field between private owners, Putin argues there should not be a level playing field between the state's interests and private interests. The state's interests should always be the most important, and the state should act in society's interest.

¹⁵ Unofficial asymmetry is the adoption of constitutions and legislations that violate the Russian constitution and federal law by regional authorities. Official asymmetry was legislation sanctioned by Yeltsin that violated the Russian constitution and federal law (White, Gitelman and Sakwa 2005).

¹⁶ Stoner-Weiss regards this as problematic, as "it meant placing appointed presidential representatives higher in the political-administrative hierarchy than elected governors and presidents of regions" (2006: 109).

¹⁷ Although regional legislatures must approve the candidate, the president can appoint the regional head for a period up to six months and dissolve the regional legislature by decree if the presidential nominee is rejected two times. So far no presidential nominees have been rejected by regional legislatures (Sakwa 2008).

¹⁸ Putin's actual dissertation is not publicly available, but Putin published an abstract of the thesis in 1999.

¹⁹ Olcott notes that "In both Soviet and Russian practice, it is common for others to write in the name of leaders (2004: 17).

Although the thesis emphasises a strong presence by the state within the natural resource sector, Putin does not want full state control, but argues instead in favour of a mixed system with state and private ownership (Olcott 2004 and Goldman 2008). Putin links the strong state presence in the mineral sector with Russia's financial stability, and argues that control over Russia's natural resources is vital to achieve this task. Putin also sees natural resources as a guarantor for Russia's international position, and proposes to use energy to advance the country's interests. Putin also argues that Russia's interests are best served by a restructuring of the economy: "The process of restructuring the national economy must have the goal of creating the most effective and competitive companies on both the domestic and world markets" (Goldman 2008: 97). Putin spends the last part of the thesis on the creation and strengthening of national champions within the oil and gas sector. National champions are large companies that should put the promotion of the state's interests over profit maximization. The state should preferably own more than 50 percent in these companies, but could with the right type of guidance and pressure be predominantly privately owned (Goldman 2008 and Olcott 2004).

Several statements made by Putin further clarify his view on the importance of energy for Russia's economy and the role of the state within the energy sector. Putin stated at a National Security Council meeting in December 2005 that "The present and future prosperity of Russia depends directly on the place we occupy in the global energy context" (Legvold 2008: 14). Putin made the same kind of acknowledgement of energy as the engine in Russia's economic renaissance in January 2006: "Our welfare at present and, to a degree, in the future directly depends on the place we will take in the global energy context" (Financial Times 3 January 2006a). Likewise, Putin stated in 2006 that "if our European partners want us to let them into *the holy of holies of our economy, namely the energy sector*, [...] we expect something in return regarding the most critical and important areas of our development" (President of Russia 25 May 2006a – italics added).

3.2.3 The Siloviki

The most influential faction in Vladimir Putin's presidential administration was the siloviki. The siloviki are politicians and businessmen who commonly have a background from the KGB/FSB or the armed forces²⁰. Several leading Russian politicians and businessman are

²⁰ Bremner and Charap (2006) also note that people from outside the security and armed forces are called siloviki. They are in these cases termed siloviki because they share similar political views and a common policy agenda.

considered siloviki. Igor Sechin served as Deputy Chief of Putin's administration, and is the CEO of the state-owned oil company Rosneft; Igor Ivanov served as Russian Foreign Minister until 2004; Sergei Ivanov served as Russian Defence Minister until 2007; and Sergei Bogdanchikov, the former CEO of Rosneft, serves as Director General of Gazprom Neft. Members of the siloviki also head several critical law enforcement agencies and serve as board members in state-owned companies like Gazprom and Transneft (Bremner and Charap 2006 and Van Bladel 2008). Khrystavenko estimates that 26 percent of the Russian elite are siloviki, and that the figure had increased during Putin's two terms as president (RFE/RL 20 December 2006).

Bremner and Charap (2006) have identified five core values of the siloviki, but I will only present two of them due to the scope of the thesis. Bremner and Charap argue that the siloviki are economic nationalists who see Russia's natural resource as the property of the Russian people, and that the state should control every aspect of resource exploitation. Van Bladel argues that the siloviki seek to create large national companies that will "serve as the main engine driving the economy and as a lever to back up a more assertive foreign policy" (2008: 79). The second value concerns the siloviki's view of Russia on the international stage. Bremner and Charap argue that the siloviki seek the restoration of Russia on the international stage. NATO and the United States are considered external security threats to Russia that "actively undermine Russia's sovereignty and ultimately would like to force the collapse of the Russian state." (2006: 89). The siloviki also want Russia to regain the respect the Soviet Union had, and seek to reintegrate the FSU states with Russia as much as possible. Van Bladel argues that "It is in the sphere of foreign policy that the *siloviki* want to achieve the most domination. Since they see a growing number of rivals threatening the country from all sides, they rely on the Soviet idea of strengthening the heartland by creating a buffer zone around the country. [...] The *siloviki* want to have influence over the Near Abroad and CIS countries, if not by exerting military power, then by supplying raw materials, regulating visas, maintaining military personnel and bases, and controlling ethnic groups on the territory of the Russian Federation" (Van Bladel 2008: 79-80).

3.3 Ownership and Control

Property rights in Russia have been troublesome for the past twenty years. Boris Yeltsin initiated as Russian president a large privatisation process which saw most of the oil companies end up in the hands of a new group called the oligarchs. The privatisation process

of the 1990s was reversed in Vladimir Putin's presidency, and the Russian state now has a strong presence in the oil and gas sector. Balmaceda argues that the increased state control of the oil and gas sector has "greatly increased President Putin's ability to use energy as a means of political pressure both within and outside the FSU" (2008: 7).

3.3.1 Rise and Fall of the Oligarchs

Boris Yeltsin handed Anatoly Chubais the task to carry out the privatisation reform of state-owned companies in November 1991. Chubais initiated the first voucher privatisation scheme, which enabled a few individuals to acquire a majority of the vouchers and turn them into ownership control of various companies. This new class of powerful, economic magnates has been colloquially known as the oligarchs²¹. A second privatisation round was executed by Yegor Gaidar, who initiated the loans-for-shares scheme due to the financial difficulties the Russian state found itself in²². The loans-for-shares scheme was intended to provide the Russian state with the necessary funds to pay its bills, while the banks that supplied the funds were given collateral in state-owned petroleum companies. As the Russian state was not successful in increasing tax revenues, it was not able to retain ownership rights of the shares. The shares were sold on rigged auctions by oligarch-controlled banks so that the banks themselves or an accomplice of the banks could buy the shares for below market price. Sibneft, the fifth largest oil firm in Russia, was in 1995 sold for \$100 million to Roman Abramovich. Sibneft was in 2005 sold to Gazprom for \$13.1 billion. Another example is Mikhail Khodorkovsky's purchase of Yukos for \$309 billion, which shortly after had a market value of \$15 billion (Goldman 2008 and Victor 2005). When Putin became president in 2000, it is estimated that the wealth of the 25 richest persons in Russia far outstripped the economic power of the Russian state (Olcott 2004).

The oligarchs had under Yeltsin's presidency been allowed to operate freely in return for political support²³. Putin, however, did not accept their meddling in state affairs, and assembled 21 of the country's oligarchs to a meeting in July 2000. Putin said during the meeting that the oligarchs would be left alone if they kept out of politics, but warned them that they would risk repercussions if they did not. Putin had prior to the meeting made an

²¹ The vouchers were distributed to Russian citizens. However, as ordinary citizens did not know what to do with the vouchers, they were sold on the cheap to those interested. Many of the oligarchs have a background as government officials who knew the vouchers' value.

²² Only three million out of 70 million Russian citizens paid their taxes to the full extent after nearly a decade of private ownership (Goldman 2008).

²³ Boris Yeltsin was re-elected in 1996 after extensive support from oligarchs, among them Boris Berezovsky, despite single digit support in the months leading up to the election date.

example of Vladimir Gusinsky, who in June 2000 was arrested for embezzlement of funds, and later fled the country (White et. al. 2005)²⁴.

3.3.2 The Yukos Case

Russian authorities started in 2003 on a process of re-establishing state control of the Russian oil and gas sector. The aggressive demeanour of the Russian state started with the actions taken against Mikhail Khodorkovsky, who at the time was the richest person in Russia and the CEO of Yukos, Russia's largest and most successful oil company. Khodorkovsky was arrested on 25 October 2003 on charges of tax evasion, grand theft, fraud, forgery, embezzlement and extortion. He was found guilty and sentenced to prison in Siberia for nine years (Goldman 2008). Most analysts argue that while Khodorkovsky and Yukos undoubtedly were guilty of several of the charges, other reasons led to the imprisonment of Khodorkovsky. Vahtra writes that "During the time of privatizations of large industrial companies in the beginning and mid-1990s, hardly any individual involved in the deals would get clean records from the processes in light of present legislation" (2004: 26). Khodorkovsky main 'crime' was to get involved in areas Putin see as the Russian state's dominion. One of them was challenging Transneft's pipeline monopoly. Khodorkovsky proposed to build an oil pipeline to China and another pipeline to Murmansk, where large deepwater tankers could dock and transport petroleum to the United States. He was also on the verge of selling a substantial stake in Yukos to Chevron or Exxon-Mobil, two American oil companies²⁵. Khodorkovsky was also directly involved in politics, as he and other Yukos executives supported opposition parties in the Russian Duma, such as the pro-Western party Yabloko. Khodorkovsky also used financial inducements to members of the Duma to gain support on several legislative issues²⁶.

Yukos was charged with failing to pay \$33 billion in taxes. The Russian state proceeded to auction off Yukos' assets to cover the charges. Yukos' most priced asset, the main production unit Yuganskneftegaz, was in December 2004 sold for \$9.35 billion, which Lucas (2008) argues was barely half the \$17 billion it had been valued at in 2004. Yuganskneftegaz's buyer was an unknown entity called Baikal Finance Group, which proved to be a front company for the state-owned oil company Rosneft. Yukos' remaining assets, valued at \$26 billion, were put up for sale in 2007. The value of the assets meant that Yukos could not be bankrupted.

²⁴ Boris Berezovsky also fled Russia in 2001. Like Gusinsky, Berezovsky also owned a television network that was critical of Putin's policies.

²⁵ The contract was more or less ready to be signed with one of the companies, according to Goldman (2008).

²⁶ Goldman notes this support "was one of the main reasons for the defeat of two government efforts to increase taxes and environmental restraints on the oil companies" (2008: 113)

The debt was instead recalculated to \$26.6 billion by Russian authorities, just enough to bankrupt Yukos. Goldman notes that the subsequent auctions were as rigged as the ones during the 1990s, and most of the assets were bought on the cheap by Rosneft and Gazprom (Goldman 2008). Putin achieved several things by reining in Khodorkovsky and Yukos. First of all, Putin made a clear example that no one is safe. Putin did not only attack Khodorkovsky and Yukos, he also attacked Russia's richest person and the most successful oil company in Russia. Hence, the Russian state had set the rules. Several Russian companies were taken over by state-owned companies or state-friendly companies in the aftermath of the Yukos case. The Russian state also gained more loyalty from companies. Lukoil's CEO Vagit Alekperov stated that "we are not trying to separate our [company] interests from national ones" (Wenger, Perovic and Orttung 2006: 31). The Yukos case also enabled the Russian state to gain a substantial ownership within the oil sector which it had lost during the privatisation process of the 1990s²⁷. The Russian state knew that targeting Yukos would have financial repercussions due to the perceived attack on property rights. Larsson claims Russia experienced a \$5.9 billion outflow during the second half of 2003, while there was a \$4 billion inflow during the first half.

3.4 Re-nationalisation

The Yukos case in October 2003 marked the beginning of a new era within the Russian oil and gas sector. Prior to the Yukos case, the Russian state only had a weak presence in the oil sector through ownership in Rosneft and Transneft, and did not have a controlling stake in Gazprom. Yakovlev argues that the strengthening of the power-vertical "not only consolidated the state, but also consolidated federal bureaucracy and strengthened its position in relation to the regional authorities and big business" (2006: 1044). Yakovlev further argues that the Russian state had by summer 2004 established an absolute dominance over business.

3.4.1 The Russian State's presence in the Gas Sector

The Russian gas sector is dominated by Gazprom, the successor of the Ministry of the Gas Industry. Unlike the Russian oil companies, which were parcelled out in different companies, Gazprom remained intact as one company. This meant that Gazprom continued as the monopoly owner of Russia's gas pipeline system and kept a strong control over the country's gas production. Gazprom was in November 1992 converted to a private joint stock company, but the Russian state kept 38 percent of the shares and remained the largest stock owner with

²⁷ Milov, Coburn and Danchenko (2006) estimate that government ownership in the oil sector had fallen below 10 percent in 2004.

the right to determine management control (Goldman 2008). Putin made his first move to establish tighter control over Gazprom in May 2001, when he replaced Gazprom's CEO Rem Vyakhirev with Alexei Miller, and Viktor Chernomyrdin with Dmitry Medvedev as Chairman of the Board of Directors. Both Miller and Medvedev were former colleagues of Putin from St. Petersburg. The Russian state still did not have a controlling stake in Gazprom, and Goldman notes that "without 50 percent plus one share state ownership, there was always the possibility that a foreign group could accumulate enough stock to take control" (2008: 83). Subsequently, strengthened by the financial upturn in the 2000s, the Russian state increased its ownership in Gazprom to a controlling stake of 50.002 percent in 2005 (Gazprom 2009 and Goldman 2008). Gazprom's importance to the Russian state can be seen in several speeches made by Putin. Putin stated in Gazprom's tenth anniversary that "Gazprom is a key element in the system of the country's energy security and its export potential. Equally important, it is a powerful lever of Russia's economic and political influence in the world" (President of Russia 14 February 2003). Figures presented by Putin showed that Gazprom contributed to eight percent of Russia's GDP in 2002, and 20 percent of the federal budget revenues. Gazprom's tax contributions had by 2008 doubled, and Gazprom still accounted for 20 percent of the federal budget revenues.

3.4.2 The Russian State's presence in the Oil Sector

Unlike the Ministry of the Gas Industry, the Ministry of the Petroleum Industry was broken up in a myriad of private oil production companies. The Russian state did not, however, privatise Transneft, the owner of the Russian oil pipeline system. Rosneftegaz, the first joint stock company, was created in September 1991. Lukoil then split from Rosneftegaz later in November 1991, before further splits saw the creation of Surgutneftegaz, Yukos and Rosneft in 1992 and 1993. New companies in turn emerged from those companies, and most of them were taken over by former state officials. One of them is Lukoil, which is owned by the former acting Minister of the Petroleum Industry, Vagit Alekperov (Goldman 2008). Only 16 percent of Russia's oil production was produced by state-owned companies when Vladimir Putin became Russian president in 2000. Rosneft's acquisition of Yuganskneftegaz and other Yukos assets increased the Russian state's share in the oil sector substantially. Liuhto (2008) notes that the Russian state's ownership in oil companies increased from 32 percent in 2004 to 47 percent in 2007. Liuhto explains the increase by several takeovers of oil companies by Rosneft and Gazprom. Gazprom also bought Sibneft in 2005 for \$13.1 billion, which was the fifth largest oil company in Russia (Liuhto 2008 and Victor 2005).

3.5 The Russian Pipeline System

Russia has the largest pipeline system in the world, with more than 200,000 kilometres of oil and gas pipelines. The Russian pipelines are an inheritance of the Soviet pipelines that were situated on Russian soil. The Soviet pipeline system was built to serve the Soviet Union as a single unit, and the Russian Republic served as the pipeline hub (see map 2 for a detailed map for Russian oil and gas pipelines). When the Soviet Union collapsed in 1991, the ownership rights to pipelines and other energy infrastructure situated on their soil were transferred to the respective republics. As a result, Russia is dependent on exporting oil and gas through independent countries to reach its European customers (Kandiyoti 2008 and Mohitpour 2008).

Map 2: The Russian Pipeline System



Source: <http://www.eia.doe.gov/emeu/cabs/Russia/images/772861%20%5bConverted%5d.pdf> [Map segment].

3.5.1 State-owned Pipeline Monopolies

The Russian pipeline system is controlled by two monopolist companies: Gazprom controls the gas pipelines²⁸, while Transneft controls the oil pipelines. While the Russian oil companies were privatised and left with little state presence during the 1990s, the Russian state retained 100 percent ownership of Transneft. The Russian state also kept close control of Gazprom, and increased the stake in the company to a majority holding in 2005. Gazprom and Transneft can as pipeline operators decide which companies are allowed access to the pipelines. This is the case for both domestic and international producers of oil and gas, and Gazprom and Transneft can as a result stop oil and gas exports if they decide to. New pipelines are also initiated on their initiative. Both companies have resisted letting go of their monopoly status, and they have argued that a privatised pipeline system will be more problematic than the current system. Vladimir Putin supports their view, and has argued that pipeline priorities should be guided by state interests (Gorst 2004). Gazprom's pipeline monopoly was strengthened in June 2006, when the Russian Duma approved by 385-6 votes that Gazprom should keep its exclusive rights to export gas (Financial Times 17 June 2006). Another bill was approved by the Duma in July 2007 to strengthen Gazprom's and Transneft's protection of their pipelines. The new bill allows Gazprom and Transneft a special exemption from private business' right to bear arms, and permits the two companies to form armed forces of their own (Reuters 4 July 2007).

3.5.2 Pipelines as a Power Instrument

Oil and gas resources are commonly exported through pipelines. However, Larsson notes that the utilization of pipeline ownership can be a powerful leverage: "By controlling the entire oil and gas pipeline (and electricity) grid, the state has a strong lever in controlling energy flows" (2006: 71). Oil and gas differ in how they can be transported. While oil is usually exported through pipelines, by railway or by oil tankers, the only viable option for transporting gas in its natural form is through pipelines in a compressed, but gaseous form. Building gas pipelines has several advantages. It is a well established technology, cost effective, and fairly easy to expand. The major economic cost is building the pipeline, but costs are relatively minor and predictable once the pipeline is built. However, the cost of building the pipelines makes building them only an option in cases where a long-term gas contract is agreed. Pipeline diversification is also not an option for many countries due to the high costs (Ericson

²⁸ Although some local gas pipelines are privately owned, the companies which own those pipelines are in turn subsidiaries of state-owned companies (Larsson 2006).

2009 and Mohitpour 2008). No gas market or market price for gas can be said to exist due to the monopolistic nature of gas deliveries. Ericsson argues that this makes the gas ‘markets’ highly inflexible and political, and that “pipeline networks impose a “lock-in” relationship, where the deep dependence without alternatives imposes non-market bargaining and allows the potential for political leverage” (2009: 37). Liquefied natural gas (LNG) is the only viable option besides exporting gas through pipelines. However, LNG is so far only considered if market access by pipeline is not feasible due to the expensive infrastructure requisites (Mohitpour 2008)²⁹. Currently only seven percent of the gas is transported as LNG. In comparison, oil can be traded in several ways, which makes diversification possible for the importing country.

Balmaceda notes that the energy issue for many of the FSU states literally is “the number one question – it directly affects their daily economic situation, their domestic politics, and their relationship with their main international partners. This is especially so for those eight energy-poor states which remain largely dependent on imports from Russia: Belarus, the three Baltic states, Moldova, Armenia, Georgia, and last but not least, Ukraine” (2008: 1). Wallander argues that oil and gas provide the Russian state with “leverage in political relationship to the extent that oil and natural gas are desirable and even necessary resources for Russia’s neighbours” (RFE/RL 5 December 2005). It is also important to consider the importance of the perceived threat of Russian energy aggression. By exerting energy aggression, Russia shows that it has the capability to do so, which in turn provide leverage in negotiations with other countries besides the inflicted country.

3.5.3 Energy Charter Treaty

Russia has so far refused to ratify the Energy Charter Treaty (ECT). Although Russia signed the ECT in 1994, it has continuously refused to ratify the treaty since. The ECT was launched following the cold war to create cooperation between East and West within the energy sector, with the purpose of creating a multilateral legally binding framework for international energy cooperation. The ECT came into legal force in 1998, and focuses on five broad areas: investment, trade, transit, energy efficiency and related environmental aspects, and dispute settlement mechanisms.

²⁹ Mohitpour argues that “Projects of this type need to be large scale to achieve efficiency and economic viability and can only be supported by extensive gas reserves and the ability to deliver the product into a large, long term market where alternate forms of energy are relative [*sic*] expensive.” (2008: 85)

Russia's refusal to sign the ECT largely comes down to transit clause in the ECT. The ECT's transit provisions "oblige its Contracting Parties to facilitate the transit of energy on a non-discriminatory basis consistent with the principle of freedom of transit." (Energy Charter Secretariat 1994: 15). The transit provision is considered important as "energy resources are increasingly being transported across multiple national boundaries on their way from producer to consumer" (ibid.). Balmaceda argues that if Russia ratified the ECT, it would lose control over the pipeline system. She notes that "full implantation of the Energy Charter could mean that Ukraine could have access to Central Asian gas – even through Russian pipelines – without Russia being able to forbid its transit at will" (2008:35). Putin, on the other hand, stresses reciprocity as the most important reason behind Russia's refusal to sign the ECT: "Full implementation of the energy charter and the additional provisions on transit would mean that we provide free access to oil and gas production and to the transport infrastructure. Of course we cannot help but ask what we are to get in return. And we are told that we will get the same. But as I said, where are their deposits to which they will give us access? Do they have pipeline networks of the kind that Gazprom has? No." (President of Russia 25 May 2006b). Although Russia has not ratified the ECT, it is important to note that several other countries have also refused to sign or ratify the ECT. Of countries that have signed the ECT, Norway has yet to ratify the document. Saudi Arabia and the United States are only listed as observers, and have refused to sign the treaty.

3.5.4 The Transit Problem

The pipelines that transport Russian oil and gas to Europe are situated in independent countries. As a result, Russian companies do not control the flow of oil and gas to its customers, but must instead rely on foreign operators. This is considered problematic by the Russian state because of the importance of the European market for the Russian economy. Russia has also been subject to blackmail from transit countries, which have used pipeline ownership as leverage in negotiations with Russia. Overland argues that "the country where the pipeline is located will ultimately have the power to do things with the pipeline" (RFE/RL 10 January 2007), whether it be to stop the flow or do repairs. Hence, because of the economic importance for the Russian economy, securing oil and gas exports to Europe is a security matter for the Russian state. Gas exports through FSU states account for 95 percent of Gazprom's gas exports. Ukraine and Belarus are the two most important transit countries. Russian gas exports through Ukrainian pipelines account for 80 percent of Russia's gas exports to Europe. Most of the remaining gas supplies are exported through Belarusian

pipelines, and both countries are also important for Russia's oil export (Map 2 on p. 23 shows the pipelines connecting Russia and Europe). Gazprom has several times accused Ukraine and Belarus for siphoning off gas from their pipelines without paying for it. Russia's relationship with Ukraine has been particularly strained because of Ukraine's siphoning during the 1990s and early 2000s (Goldman 2008). Russia has repeatedly tried to acquire ownership in pipeline infrastructure and other types of oil and gas infrastructure in FSU states, but has yet to establish control over the energy sector in the FSU states.

3.5.5 Circumventing Transit Countries and avoiding Competition

Russia's present and future prosperity is directly linked to its ability to export Russian oil and gas to Europe. Although Russian energy producers are keeping an eye on other markets, such as the growing Asian market, creating a pipeline network of a substantial volume will be time consuming and it will require a large amount of capital. The European market, in comparison, is readily available through an extensive web of existing pipelines that connect Russian energy producers with European customers. Gazprom and Transneft have initiated several new pipeline projects in the last few years, with more projects being planned. Common for most of the projects are that they circumvent existing transit countries, which will enable Russia to diversify pipeline exports to Europe and circumvent troublesome countries (most of the planned pipelines are shown on Map 2 on p. 23) Putin has previously stated that "the choice of routes or new pipelines should not be based on political considerations but made after taking into account economic and well as environmental factors" (Larsson 2006: 174). Nord Stream is a planned gas pipelines that will carry gas from Russia to Germany on the Baltic seabed³⁰. Nord Stream will enable Russia to divert gas from the Ukrainian and Belarusian gas pipelines, which will decrease Russia's dependence on the two countries (Lucas 2009). The Baltic Pipeline System 2 (BTS-2) is another pipeline that was approved after the oil dispute with Belarus in 2007. Semyon Vainshtok, the CEO of Transneft, has called the pipeline an "absolutely unprofitable political project" (RIA Novosti 1 July 2008). Vainshtok's statement shows that the pipeline was not initiated because of its profitability. Russia has also proposed to build several other pipelines. One of them is South Stream, which will transport Russian gas through a pipeline under the Black Sea to Bulgaria and then to Italy (Goldman 2008).

³⁰ Underwater pipelines are considerably more expensive to build than land-based pipelines. Nord Stream's expected cost has risen throughout the planning period, from €4 billion in 2004 to €7,5 billion in 2009 (Lucas 2009 and Nord Stream 2009).

Russian authorities have also sought to eliminate the threat from alternative pipelines that bypass Russia or threaten Russia's position as the dominant energy supplier in FSU states. This is especially the case for NABUCCO³¹. Gazprom has made several attempts at tying up NABUCCO's potential customers to Russian gas, offering them increased deliveries and a cheaper and quicker alternative to NABUCCO. The Iran-Armenia pipeline is another example of Russian efforts to avoid competition. Armenia is a close ally of Russia, but the country's weak economy has led to an indebted relationship with Russia. Armenia was like several other countries in 2006 subject to Gazprom's demands for a higher gas price. Instead of an outright increase from \$55 per tcm to \$110 per tcm, Gazprom received a larger stake in ArmRosGaz³². The deal also included the ownership transfer of the Armenian part of the Iran-Armenia pipeline to ArmRosGaz. The Iran-Armenia pipeline diameter was initially planned to be 1420 millimetres, but Gazprom limited the size to 700 millimetres (Eurasia Daily Monitor 19 April 2006). The size reduction "precluded the possibility of this pipeline being used for transit of Iranian gas via Armenia to Georgia and potentially to Ukraine via the Black Sea" (Eurasia Daily Monitor 3 November 2006). Russia has not been successful in eliminating all competing pipelines, as in the case of the Baku-Tbilisi-Erzurum (BTE) gas pipeline. The BTE pipeline has eased Georgia's dependence on Russian gas by providing Georgia the option to import most of its gas from Azerbaijan (Goldman 2008).

3.6 Russian Oil and Gas Resources

This part will outline Russia's oil and gas reserves, the oil and gas price development, and Russia's dependence on revenues from this sector. Oil and gas reserves are here understood as "those quantities that geological and engineering information indicates with reasonable certainty can be recovered in the future from known reservoirs under existing conditions" (BP 2009)³³. In order to understand the longevity of Russia's oil and gas reserves, a reserves-to-production (R/P) ratio is used. The R/P ratio shows the number of years oil and gas reserves will last if the production continues at the same rate as the listed year, and is calculated by

³¹ NABUCCO is a planned pipeline that will transport Central Asian gas from Turkey to Austria, crossing Bulgaria, Romania and Hungary. Gas from NABUCCO can in turn be re-exported to other European nations (Goldman 2008).

³² ArmRosGaz, now ArmRosGazprom, is the transport and distribution network that owns the Armenian pipeline system. Gazprom's ownership in ArmRosGaz was raised from 45 to 58 percent, which gives Gazprom a controlling stake in the company. Together with Itera, an independent Russian gas company, Russian companies own 68 percent of ArmRosGaz (Eurasia Daily Monitor 3 November 2006).

³³ Probable and possible reserves are not included in Table 2 and Table 3 on p. 29-30. However, it is likely that Russia has substantial oil and gas reserves that are yet to be discovered, or that may be possible to extract in the future. This is especially the case for oil and gas reserves in parts of Siberia and in the Arctic.

dividing the amount of reserves remaining at the end of the year with the production in that year (BP 2009).

3.6.1 Gas Reserves

Russia has by far the world's largest proven gas reserves, which according to BP's estimates amount to 25.2 percent of the total proven reserves in the world (see table 2 for more information). Comparatively, Iran has the second largest reserves with 15.7 percent of the world's gas reserves. If we take a look at proven gas reserves by areas in the world, Russia controls 75.2 percent of the of total gas reserves in Europe and Eurasia. Norway has in comparison the second largest reserves in Europe and Eurasia with 1.7 percent of the proven gas reserves in the world³⁴.

Table 2: Gas Reserves and Gas Production

Country	Proved reserves		Production		
	Trillion cubic meters	Share of total in %	Billion cubic meters	Share of total in %	R/P ratio
Russian Federation	44.65	25.2	607.40	20.6	73.5
Iran	27.80	15.7	111.90	3.8	*
Qatar	25.60	14.4	59.80	2.0	*
Saudi Arabia	7.17	4.0	75.90	2.6	94.4
United Arab Emirates	6.09	3.4	49.20	1.7	*
United States	5.98	3.4	545.90	18.8	10.9
Nigeria	5.30	3.0	35.00	1.2	*
Algeria	4.52	2.5	83.00	2.8	54.4
Total Europe & Eurasia	59.41	33.5	1075.70	36.5	55.2
Total Middle East	73.21	41.3	355.80	12.1	*

* More than 100 years

Source: BP Statistical Review of World Energy June 2008

Although the Middle East's proven gas reserves surpasses the gas reserves found in Europe and Eurasia, Russia's gas reserves alone amount to 61 percent of the Middle Eastern gas reserves. Russia's gas production in 2007 amounted to 20.6 percent of the world total. In comparison, the second largest gas producer, the United States, produced 18.8 percent of the world's gas. However, there is a large difference in longevity in the two countries' gas production. While the United States current production can only last for 10 years, Russia can produce the current amount of gas for 73.5 years. Moreover, Russia also has a large surplus of gas which leaves room for gas exports. Table 2 also shows that several other countries lag

³⁴ There is reason to believe Turkmenistan has substantial reserves, but BP has yet to publish statistics which shows the size of Turkmenistan's gas reserves.

behind in gas production compared to their total share of gas reserves³⁵. Although these countries' share of production will increase in the future and provide competition for Russia, Russia's substantial gas reserves will ensure Russia's position as an important actor on the gas market.

3.6.2 Oil Reserves

The oil sector is dominated by Middle Eastern countries. Saudi Arabia's oil reserves amount to 21.3 percent of the proven oil reserves in the world. In comparison, Russia's oil reserves only amount to 6.4 percent of the world's proven oil reserves (Table 3 shows proven oil reserves and oil production). Although Russia's oil reserves are inferior to Middle Eastern reserves, Russia's is the world's leading oil producer together with Saudi Arabia. Russia was in 2006 the world's largest oil producer, as OPEC members, among them Saudi Arabia, cut their production to stimulate oil prices (Larsson 2006). Russia's sustainability as an oil producer is nevertheless much smaller than Saudi Arabia's due to the difference in oil reserves. The R/P ratio reflects Russia's overproduction. While Saudi Arabia can continue present-day oil production for 69.5 years, Russia's oil production will only last for 21.8 years.

Table 3: Oil Reserves and Oil Production

Country	Proved reserves		Production		
	Thousand million barrels	Share of total in %	Thousand barrels daily	Share of total in %	R/P Ratio
Saudi Arabia	264.2	21.3	10413	12.6	69.5
Iran	138.4	11.2	4401	5.4	86.2
Iraq	115.0	9.3	2145	2.7	*
Kuwait	101.5	8.2	2626	3.3	*
United Arab Emirates	97.8	7.9	2915	3.5	91.9
Venezuela	87.0	7.0	2613	3.4	91.3
Russian Federation	79.4	6.4	9978	12.6	21.8
United States	29.4	2.4	6879	8.0	11.7
Total Middle East	755.3	61.0	25176	30.8	82.2
Total Europe & Eurasia	143.7	11.6	17835	22.0	22.1

* More than 100 years

Source: BP Statistical Review of World Energy June 2008

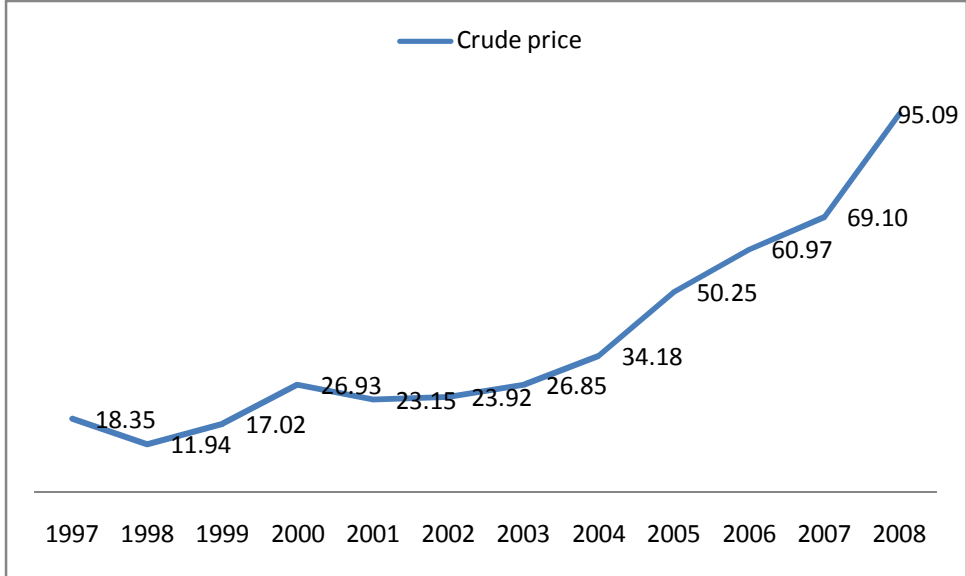
3.6.3 Price Development 1999-2008

Vladimir Putin has as Russian president enjoyed a very favourable development of oil and gas prices. The price for Russian Urals crude oil was at the time of the Russian financial crisis in August 1998 11.19 \$/barrel, and the average for 1998 was 11.94 \$/barrel. The average oil

³⁵ This can be primarily explained by the lack of investments in gas production and pipeline infrastructure.

price for 1999 was in comparison 17.02 \$/barrel, a 43 percent increase from the previous year. The price for Russian Urals had by the time Putin became president on New Year’s Eve 1999 increased to 24.71 \$/barrel. The oil price steadied between 2000 and 2003, but increased dramatically from 2004 and onwards, reaching higher levels each year until the end of Putin’s presidency (the oil price development is shown in Figure 1). The average oil price for 2008 was 95.09 \$/barrel, and was in the week before Putin stepped down as Russian president priced at 106.95 \$/barrel.

Figure 1: Graph Showing Yearly Average Crude Oil Price



Source: Energy Information Administration 2009 (<http://tonto.eia.doe.gov/dnav/pet/hist/wepcuralsw.htm>)

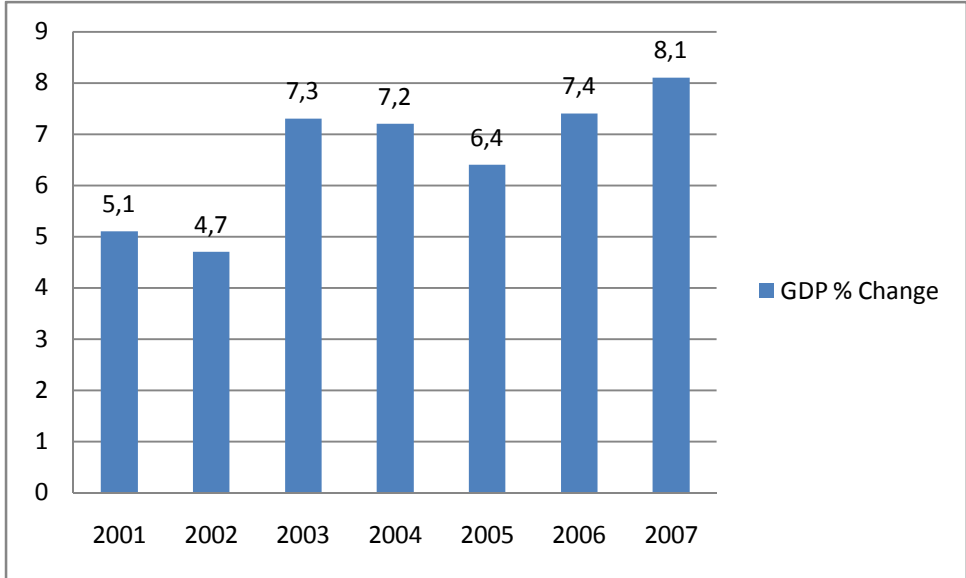
Russia has also benefited from markedly higher gas revenues as the gas price is commonly linked to the development of the oil price. Goldman notes that “Vladimir Putin’s selection as prime minister in August 1999 and four months later his appointment as acting president coincided with the recovery in petroleum prices. The increase in oil prices would probably have triggered an economic recovery even if Boris Yeltsin had still been in power” (Goldman 2008: 170).

3.6.4 The Importance of Oil and Gas for the Russian Economy

75 of the 100 largest companies in Russia in 2005 operated within the oil and gas sector, and Larsson argues that Russia’s dependency on natural resources will continue to grow in the future. Figure 2 below shows that the Russian economy has grown substantially each year during Putin’s presidency, with a record high GDP increase of 8.1 percent in 2007. 2007 also saw a record high average oil price at 69.10 \$/barrel. These figures stand in stark contrast to

the period before Vladimir Putin came to power. Russia experienced between 1987 and 1997 an annual GDP decrease of -7.6 percent, with oil prices significantly lower than the one's recording during Putin's presidency.

Figure 2: Graph showing Russian GDP % Change



Source: World Bank 2008

(http://siteresources.worldbank.org/INTRUSSIANFEDERATION/Resources/macroind_rer_16.pdf)

Data from the World Bank shows that Russia's trade balance has increased by 267 percent from 2001 and 2007, up from \$48.1 billion in 2001 to \$128.7 billion in 2007 (see table 4 on the next page). The same trend is seen in Russia's export of goods, as Russia's exports are 3.5 times larger in 2007 than in 2001. While energy exports have always been important for the Russian economy, their role has increased in Putin's presidency. Energy resources accounted for 51.2 percent of Russian exports in 2001, and had increased to 61.5 percent in 2007. Gazprom is the single largest tax contributor in Russia, and accounts for nearly 20 percent of Russia's federal budgets (President of Russia 11 February 2008 and Goldman 2008).

Table 4: Balance of Payment Indicators

Year	Average Urals crude price (\$/barrel)	Trade Balance (in billion \$)	Export of Goods (in billion \$)	Share of energy resources in export of goods, %
2001	23.15	48.1	101.9	51.2
2002	23.92	46.3	107.3	52.4
2003	26.85	59.9	135,9	54.2
2004	34.18	86.9	183,2	54.7
2005	50.25	118.3	246,3	61.1
2006	60.97	139.2	303,9	63.3
2007	69.10	128.7	354,0	61.5

Source: World Bank 2008

(http://siteresources.worldbank.org/INTRUSSIANFEDERATION/Resources/macroind_rer_16.pdf)

Russia's oil exports in 2005 generated \$113 billion, while gas exports amounted to \$30 billion (Eurasia Daily Monitor 12 May 2005). The enormous impact increased oil prices have had on Russia's energy resources is shown by Pirog, who notes that "a \$1 per barrel increase in the price of Urals blend crude oil for a year results in a \$3 billion increase in Russia's nominal Gross Domestic Product" (2007: 4). Table 5, which shows the development of Russia's gold reserves and the Stabilisation Fund³⁶, further shows the impact increased energy revenues have had on the Russian economy. Russia's gold reserves multiplied 13 times between 2001 and 2007, while the stabilisation fund had in four years accumulated \$156.8 billion.

Table 5: Monetary Indicators

Year	Gold Reserves in billion \$	Stabilisation Fund in billion \$
2001	36.6	
2002	47.8	
2003	76.9	
2004	124.5	18.7
2005	182.2	42.9
2006	303.7	89.1
2007	476.4	156.8

Source: World Bank 2008

(http://siteresources.worldbank.org/INTRUSSIANFEDERATION/Resources/macroind_rer_16.pdf)

The figures presented above clearly paint a picture of the Russian state's dependence on oil and gas exports, and shows a clear connection between higher energy prices and increased revenues for the Russian state. The increased revenues have enabled the Russian state to

³⁶ The Stabilisation Fund was created on 1 January 2004. Revenues from oil and gas exports are saved in the Stabilisation Fund as a buffer for future expenses.

increase the standard of living in Russia, including reducing poverty and raising wages. Yakovlev argues that “The high ratings of President Putin strongly depend on improving standard of living, which in turn is closely related to economic development” (2006: 1050).

Chapter 4: Policy Documents

4.1 Introduction

After having established the empirical background in the previous chapter, we will now have to consider more explicitly the political documents that describe and identify Russia's policies in the spheres of national security, foreign policy and energy policy. The three documents are the National Security Concept (NSC), the Foreign Policy Concept of the Russian Federation (FPC), and the Energy Strategy of Russia for the Period up to 2020. Although the importance of the documents should not be overstated, the policy documents provide insight into how Russian decision-makers view the world. The policy documents have also been approved by Vladimir Putin, which they would not have been if they did not represent the views of Putin and the Russian state on the different policy areas. Only those aspects of the documents that are considered relevant to the thesis' research question will be outlined. When I outline Russia's FPC, I will also supplement the document by providing additional information regarding Russia's hostility towards NATO, the EU and the United States.

4.2 National Security Concept

The National Security Concept (NSC) was signed on 10 January 2000 by Vladimir Putin, and concerns the most important policy directions with regard to the security of the individual, the society and the state against internal and external threats. The document is divided into four parts: Russia in the world community, Russia's national interests, threats to the Russian Federation's national security, and ensuring the national security of the Russian Federation.

The first part of the NSC outlines Russia's view on the world order, and how Russia's position is threatened. The NSC argues that while a large number of states have been strengthened economically and politically, power structures continue to be dominated by Western countries under the leadership of the United States. Although Russia sees itself as one of the great powers, Russia feels threatened by a number of states that seek to weaken Russia politically, economically and militarily. The NSC also states that Russia feels ignored when major issues are solved in international processes. The next part concerns Russia's national interests; Russia's national interest is by the NSC defined as "the combined political, social, international, informational, military, border, ecological security. They are long-term in nature and define the main goals and strategic and short-term goals of the state's domestic and foreign policy" (Russian Security Council 2000). The NSC assigns economic

development the highest priority: “Russia’s national interests may be assured only on the basis of sustainable economic development. Therefore Russia’s national interests in economic [sic] are of key importance” (ibid.). The NSC also states that Russia must seek to strengthen its role as a great power and to develop closer ties to CIS states.

The third part of the NSC identifies several threats to Russia’s national security. A weakening of the Russian economy is considered a threat to Russia’s national security as it can lead to political stability and a weakened economic output, which in turn will affect the standard of living in Russia. Several threats are also identified in the international sphere: the weakening of Russia’s political, economic and military influence in the world; the strengthening of military-political blocs and alliances, above all NATO’s eastward expansion; the possibility of foreign military bases and military presence in neighbouring states close to the Russian border; and the outbreak and escalation of conflicts near the Russian border and on the external border of CIS states. The last part of the NSC is concerned with how Russia can secure its national security. The NSC is in favour of strengthening state regulation, above all strengthening state regulation of the domestic economy. The NSC also states that Russia’s foreign policy should be designed to ensure favourable economic conditions and secure the rights of Russian abroad. Militarily, the NSC argues that “the interests of ensuring Russia’s national security predetermine the need [...] for Russia to have a military presence in certain strategically important regions of the world” (Russian Security Council 2000). The NSC also states that Russia shall assist in settling conflicts and participate in peacekeeping activities.

4.3 Russian Foreign Policy

4.3.1 Foreign Policy Concept

Russia’s Foreign Policy Concept (FPC) was approved by Vladimir Putin on 28 June 2000, and represents the Russian state’s views on the main areas of Russia’s foreign policy activities. The FPC operates with seven main objectives, of which I will outline three, and then goes on to discuss various aspects of Russian foreign policy. The first main objective of Russia’s foreign policy is to protect Russia’s security, sovereignty and territorial integrity. The FPC goes on to state that Russia’s position in the world community must be “fully consistent with the interests of the Russian Federation as a great power, as one of the most influential centres” (Ministry of Foreign Affairs of the Russian Federation 2000). Second, the FPC states that Russia will seek to “form a good-neighbour belt along the perimeter of Russia’s borders” (ibid.), and that it will seek to eliminate potential conflicts and tensions in

neighbouring states. Next, the FPC also emphasises the rights and interests of the large Russian diaspora in FSU states: “The Russian Federation will seek to obtain adequate guarantees for the rights and freedoms of compatriots in states where they permanently reside” (ibid.), and that the relationship between Russia and the other states will depend amongst others on the guarantees of rights of Russian citizens abroad. Besides the main objectives, the FPC is critical of the unipolar structure of the world and the economic and power domination of the United States. Despite its negative view of the United States, the FPC states that Russia is prepared to overcome difficulties in its relationship with the United States. The FPC also highlights the problematic nature of Russia’s weak economic situation as it limits the resources available to support the Russian foreign policy. The FPC states anyhow that “Russia must be prepared to utilize all its available economic levers and resources for upholding its national interests” (Ministry of Foreign Affairs of the Russian Federation 2000). The FPC regards international peacemaking as an effective instrument to resolve armed conflicts, and states that Russia will participate in peacekeeping missions.

The FPC assigns the CIS the highest priority, and states that Russia attaches priority importance to settle conflicts in the CIS. Europe is also considered a foreign policy priority, and the FPC aims to secure greater cooperation with European states and institutions. The most important institution is the EU, which is considered to be one of Russia’s main political and economic partners. Russia does not specifically mention the EU’s enlargement as problematic, but notes that Russia will seek respect for its interests from the EU. While the FPC expresses a favourable view of the EU, NATO is considered much more problematic. The FPC states that “NATO’s present-day political and military guidelines do not coincide with security interests of the Russian Federation and occasionally contradict them” (Ministry of Foreign Affairs of the Russian Federation 2000). The FPC mentions specifically NATO’s new strategic concept which does not preclude the use of force outside NATO’s membership zone³⁷. The FPC is also negative to further expansion of NATO, and states that substantive and constructive cooperation is only possible if respect is shown to both side’s interests.

4.3.2 Russia and the CIS

Vladimir Putin said in his 2005 annual address to the Federal Assembly that “the collapse of the Soviet Union was a major geopolitical disaster of the century” (President of Russia 25 April 2005). Putin has repeatedly stated that the CIS area is Russia’s foreign policy priority:

³⁷ Russia was very critical of NATO’s decision to intervene in Kosovo in 1999 without authorization from the UN.

“These countries are our closest neighbours. We are united by centuries of historical, cultural and economic ties. [...] And to put it directly, we see the CIS area as the sphere of our strategic interests.” (President of Russia 16 May 2003). Russia has created several Russian-dominated organisations with the aim of maintaining Russia’s influence over the FSU states. Although many FSU states are members in the various organisations, few of the organisations have led to any significant collaboration (Nygren 2008).

4.3.3 Russia’s views on NATO and the EU

Russia’s relationship with NATO under Vladimir Putin has been strained. Putin has repeatedly been angered by NATO’s actions, especially with the 2004 NATO expansion which brought three FSU states and five former Central European satellite states into the organisation. In February 2007 at the Munich Conference on Security Policy, Putin claimed that NATO has broken a promise made by former NATO General Secretary Woerner, who promised NATO expansion would not include former Warsaw Pact countries³⁸: “the fact that we are ready not to place a NATO army outside of German territory gives the Soviet Union a firm security guarantee” (President of Russia 10 February 2007). In the same speech Putin questioned against whom the expansion was intended. NATO is also being accused for breaking a promise made in May 1998, which stated that future enlargements of NATO would not cross a ‘red line’ on the geopolitical map of Europe drawn along the borders of the Soviet Union (Adomeit in Rowe and Torjesen). Putin has several times criticized NATO members’ refusal to ratify the Conventional Armed Forces in Europe treaty (CFE)³⁹, and has accused NATO of putting its frontline soldiers on Russian borders (ibid.). Russia suspended its participation in the CFE treaty later in 2007 following the Munich Conference. Russia claims there is no justification for NATO’s continued existence as a military alliance, and argues instead it should be turned into a political alliance. Putin has said Russia would reconsider its position towards NATO’s expansion if it did so.

While Russia’s relationship with NATO is strained, Russia’s relationship with the EU has a more pragmatic nature. Russia recognizes the EU’s importance for Russian trade. Europe is Russia’s principal importer of Russian oil and gas resources, and is Russia’s largest export

³⁸ The Warsaw Pact was a Soviet-led military alliance similar to NATO. Former Warsaw Pact members include Albania, Bulgaria, Czechoslovakia, German Democratic Republic, Hungary, Poland, Romania, and the Soviet Union (Rowe and Torjesen 2009).

³⁹ The CFE treaty was signed in November 1990, and was created to establish a military balance between NATO members and former Warsaw Pact members. The most important feature of the CFE treaty is its limitations on deployment of military equipment in Europe (Rowe and Torjesen 2009).

market. Although Russia has been less critical of the EU's, Russia is not unconcerned with the EU's actions. The EU's enlargement in 2004 made Russian access to Kaliningrad, the Russian exclave on the Baltic Sea (see Map 1, p. viii), more difficult due to the EU's visa regime. Russia is also concerned that the EU's expansion into FSU states will decrease Russia's dominance over the FSU states, especially with regards to their economic dependency on Russian trade. Their dependency has in turn provided the Russian state with political leverage on the FSU states. Moreover, Russian authorities have also been angered by EU members' financial support to the coloured revolution in Ukraine and Georgia, and the EU's perceived attempt to impose European values on FSU states (Light in Rowe and Torjesen ed. 2009).

4.3.4 Russia's views on the United States

After an initial positive tone between Vladimir Putin and George W. Bush, Putin's disillusionment with the United States increased as his presidency progressed. Putin's hostility towards the United States is based on several factors, some of them already mentioned in the NSC and FPC. Putin stated at the Munich conference that the United States has "overstepped its national borders in every way. This is visible in the economic, political, cultural and educational policies it imposes on other nations" (President of Russia 10 February 2007). Russia has been angered by the United States' increased focus and presence in FSU states. The United States provided strong support for the colour revolutions in Georgia and Ukraine, and has funnelled economic assistance to NGOs through the former Soviet Union. The United States has been one of the main proponents for NATO's eastward expansion, and was the driving force behind NATO's decision to intervene in Kosovo and later recognition of Kosovo's independence. The United States has also encouraged the development of pipelines bypassing Russia, which will decrease the FSU states' energy dependency on Russia⁴⁰. Putin has also been incensed by the United States' planned anti-missile system located in Europe, which according to Putin can also be targeted against Russia and not only Middle Eastern countries (Smith 2007 and Nygren 2008).

4.4 Energy Strategy of Russia for the Period up to 2020

4.4.1 General outline

Russia's energy strategy is outlined in a document called 'The energy strategy of Russia for the period up to 2020', and was approved by the Russian government on 28 August 2003. The

⁴⁰ Georgia started in 2007 to receive gas from Azerbaijan through the BTE pipeline, which had been supported by the United States.

intention of the document is to clarify the “Aims, tasks and guiding lines of a long-term state policy and phases of its realization” (MFE 2003). The aim of Russia’s energy policy is “to make most effective use of the natural fuel and energy resources and of the potential of [*sic*] energy sector for economic growth and improvement of life quality” (Ministry of Energy of the Russian Federation 2003). The energy strategy argues that Russia’s energy resources are essential to Russia’s economic growth, and that energy safety is the most important element of Russia’s energy strategy. The energy strategy identifies several factors that may affect Russia’s energy safety. It recognizes Russia’s great dependence on the oil and gas sector and the volatile energy prices, and sees the lack of investments as dangerous due to the high degree of wear on energy infrastructure. The energy strategy therefore calls for an upgrade of the technical infrastructure in order to ensure continued high production.

4.4.2 External Energy Policy

Russia’s energy strategy argues that Russia must change from being a supplier of raw materials to an active participant on the world energy market, and emphasise that strengthening Russia’s position in the energy markets is strategically important. The energy strategy highlights the export ability of the Russian energy sector, as it provides economic safety to the Russian state. In this regard, the energy strategy calls on “state and private entities to exert pressure on regional states to ease Russia’s access to international markets” (Stulberg 2007: 98). Russia’s dependency on energy exports to Europe through foreign countries is highlighted by the energy strategy, which argues that providing the “indiscriminate transit of energy answer [*sic*] the strategic interests of Russia” (Ministry of Energy of the Russian Federation 2003). Russia’s energy strategy acknowledges Russia’s unique geopolitical and geographical position, and sees energy as an important element in Russian diplomacy and foreign policy relations. Fredholm notes that the energy strategy “occasionally uses language reminiscent of military strategy: the state must support the Russian companies in the struggle for resources and markets” (2005: 3). With regards to oil export, the Russian energy strategy favours using Russian ports, and considers export port terminals under foreign control as problematic. The energy strategy states that Russia should seek to transit oil from CIS states through Russia by making use of its existing pipeline system (Fredholm 2005). Furthermore, Western Europe followed by Central Europe is considered the most important market for Russian gas.

Chapter 5: The Sites of Russian Energy Aggression

5.1 Introduction

In order to be able to analyse the 13 cases of Russian energy aggression, we need to know the context in which the cases took place. This chapter will serve as a context-chapter for the 13 cases of Russian energy aggression, where I will cover the most important issues that have dominated Russia’s relationship with the seven countries that have been subject to Russian energy aggression.

5.2 The Baltic States

Since the Baltic States have shared many of the same problems since the dissolution of the Soviet Union, their common historical context will be discussed together. Next, I will also discuss a specific event which concerns Russia’s relationship with Estonia.

5.2.1 Common historical context

The three Baltic States, Estonia, Latvia and Lithuania, gained independence from the Soviet Union in 1991 after 51 years of occupation⁴¹. Due to Josef Stalin’s replacement policies, many ethnic Russians live in Estonia and Latvia. The Russian diaspora in Estonia amounts to 25.6 percent of the population, while Latvia’s Russian diaspora amounts to 29.6 percent of Latvia’s population (Table 6 shows the dispersion of the Russian diaspora). Putin noted in a speech in November 2004 that more than 160.000 Russians in Estonia and up to 500.000 Russians in Latvia were still without citizenship.

Table 6: The Russian Diaspora in FSU states

Country	Population	Ethnic Russians in population (in percent)
Belarus	9.648.533	11.4
Estonia	1.299.371	25.6
Georgia	4.615.807	1.5
Latvia	2.231.503	29.6
Lithuania	3.555.179	6.3
Moldova	4.320.748	5.8
Ukraine	45.700.395	17.3
Russia	140.041.247	79.8

Source: CIA Factbook 2009

⁴¹ The Baltic States were occupied in June 1940. Estonia gained independence on 20 August 1991, Latvia on 21 August 1991, and Lithuania on 6 September 1991 (CIA – The World Factbook 2009).

Putin also emphasised the restricted rights for non-citizens in the two states, as they were not allowed to vote in Estonia's EU referendum. He argued that the two states exert economic and language discrimination on the Russian diaspora. Putin also argued that Russians face restrictions in sports, and that World War II veterans are being oppressed (President of Russia 10 November 2004).

Unresolved border issues that stem back from World War II have been another issue. While Lithuania and Russia resolved their border issues in 1999, no agreement was signed with Estonia and Latvia. The border issue is connected to the Baltic States' view of the Soviet Union as an occupant⁴². Both the Estonian and Latvian Soviet Republics had to surrender land to the Russian Republic following World War II, and this dispute was revived when they received independence in 1991 (BBC 27 March 2007). Socor argues that Russia has used the unresolved border issues as leverage to extract concessions on other issues, such as the two countries' citizenship rights and language policy. While Latvia and Russia ratified their border treaty in March 2007, Russia refused to ratify the Russian-Estonian border treaty in June 2005 (Eurasia Daily Monitor 2 May 2005 and Eurasia Daily Monitor 23 June 2005)⁴³.

Although these issues have soured the relationship between Russia and the Baltic States, the biggest issue has been the Baltic States' accession to the EU and particularly NATO. EU and NATO membership was a driving force in the Baltic States' foreign policy since independence in 1991, and was finally achieved on 1 May 2004. Besides several principal disputes with the EU⁴⁴, Lithuania's EU membership made Russian access to Kaliningrad more difficult due to the EU's visa regime for Russians⁴⁵. While Russia was modestly critical of the Baltic States' EU accession, Russia was very forthright in its hostility towards their NATO membership. Shortly after NATO confirmed the date for NATO's enlargement, the Russian Duma approved a resolution which stated that Russia may reconsider its defence strategy if NATO continued to disregard Russia's interests. The resolution urged NATO

⁴² Russian authorities argue that the Baltic States voluntarily joined the Soviet Union in 1940 (BBC 27 March 2007).

⁴³ Russia had signed the treaty earlier in 2005, but refused to ratify it because of Estonia's inclusion of a preamble that made reference to historical border treaties. Estonian authorities also reiterated their view of the Soviet Union as an occupant.

⁴⁴ Russia was reluctant to extend the Partnership and Co-operation Agreement to the new EU members beyond the original 15 EU members. Furthermore, the EU's Neighbourhood Policy meant Russia became an EU neighbour on par with other European nations, which offended Russia's self-image as a great power (Light in Rowe and Torjesen 2009).

⁴⁵ Lithuanian EU membership meant the country had to implement the Schengen Treaty, which requires that Russian citizens need a visa to enter the EU (Office of the Government of the Republic of Lithuania 2007).

members to ratify the CFE treaty, and warned that Russia may revise a previous agreement on the limitations of troops in Kaliningrad. It also recommended the Russian government to consider the number of troops deployed on Russia's western borders (BBC 1 April 2004).

Chapter four shows that Russia is particularly occupied with the perceived military threat from NATO. The three policy documents were written before the Baltic States became NATO members, and their accession further strengthened Russia's critical view of NATO. Russia claims that the Baltic States' NATO membership means NATO forces and NATO equipment can be stationed in the Baltic States and used to monitor the Russian territory. Russia has also criticized the Baltic States' for not ratifying the CFE treaty, which means that NATO can station military equipment in the Baltic States without verification rights for Russian inspectors (Adomeit in Rowe and Torjesen 2009). Putin argued in his annual address to the Federal Assembly in 2007 that the Baltic States' refusal to sign the CFE Treaty "creates a real threat and an unpredictable situation for Russia" (President of Russia 26 April 2007).

5.2.2 Estonia

Russia's relationship with Estonia worsened in February 2007 when the Estonian Parliament voted in favour of a bill that prohibits the display of monuments glorifying Soviet rule. The bill paved the way for the dismantling and relocation of a Soviet War memorial in Tallinn, the Bronze Soldier, and the reburial of the 13 soldiers buried underneath. Estonia's large Russian-speaking minority were firmly against the plan to relocate the war memorial. They consider the Bronze Soldier as a symbol of the Soviet Union's huge sacrifices during World War II and as an anti-fascist symbol. Estonians, meanwhile, consider the war memorial as a symbol of the involuntary Soviet occupation of Estonia (BBC 15 February 2007). The Bronze Soldier had also become a rallying point for protests by ethnic Russians, which boiled over on 9 May 2006⁴⁶ when serious clashes took place between Estonian nationalists and Russians waving Soviet flags. Russian officials were also incensed by the Estonian plans. Sergei Lavrov, Russia's Foreign Minister, denounced Estonia's decision as blasphemy against the soldiers who defeated Nazi Germany. Estonia's Justice Minister Rein Lang defended the plans, and argued that the monument was built in 1947 "to symbolize the superiority of Russia and Russian rule" (New York Times 25 January 2007). Furthermore, Estonia's president Toomas Ilves argued that the Bronze Soldier had become a rallying point for Russian protesters with support from the Russian embassy in Tallinn.

⁴⁶ 9 May is called Victory Day in Russia, and is used to commemorate the Soviet victory over Nazi Germany.

The Bronze Soldier was removed in the morning of 27 April 2007, and rebuilt at a military cemetery in Tallinn. Violent demonstrations followed the removal of the Bronze Soldier, with clashes of more than 1000 pro-Russian supporters and Estonian anti-riot police, leaving one person dead and more than 150 injured. Large protests also took place outside Estonia's embassy in Moscow, where state-sponsored youth groups surrounded the embassy. They managed to disrupt a news conference held by Estonia's ambassador in Russia without any interference by the police (RFE/RL 29 April 2007 and RFE/RL 2 May 2007)⁴⁷. Nikolai Kovalyov, the Chairman of the Duma's Veterans Affairs Committee, called on the resignation of the Estonian government, and wanted a criminal investigation of the repression of the protesters (Eurasia Daily Monitor 2 May 2007). Sergei Lavrov criticised the EU, NATO and the United States for backing Estonia, and claimed that Estonia's actions "contradict European values and culture". Lavrov also stated that the dispute would affect Russia's relationship with the EU and NATO as Estonia is a member of those organisation, and thus responsible for their behaviour (RFE/RL 4 May 2007 and RFE/RL 8 May 2007). The European Parliament adopted on 24 May 2007 a resolution on the Russian-Estonian dispute. The resolution was critical of Russia's actions towards Estonia, and stated that "the violent demonstrations and attacks against law and order were conducted with active organisation and cooperation by forces located outside Estonia" (European Parliament 24 May 2007).

5.3 Belarus

Belarus is a landlocked country in Eastern Europe that shares borders with Latvia, Lithuania, Poland, Ukraine and Russia. Belarus became independent from the Soviet Union in August 1991, and has been ruled by the authoritarian president Alexander Lukashenko since 1994. Belarus has forged close ties with Russia, both politically and economically, and the Belarusian economy has been greatly subsidised by Russia.

5.3.1 The Failed Russia-Belarus Union State

Belarus has traditionally been Russia's closest ally, and the two countries have since 1993 attempted to create a union state. The first major step was taken in April 1996 when the Russian-Belarusian Community Agreement was signed⁴⁸. Another Union Treaty draft was signed in 1997, which assigned security policies and border controls the highest priority.

⁴⁷ The youth groups painted the embassy's outer walls with hostile slogans, played loud military music 24 hours a day, and took control over the embassy's entrance.

⁴⁸ The Russian-Belarusian Community Agreement treaty aimed at deepening the integration with the purpose of a merger of economic and legal policies and the formation of supranational institutions (Nygren 2008).

Lastly, a new Union Treaty was signed with Vladimir Putin as Russian Prime Minister in December 1999. The Union Treaty envisaged the creation of a single customs and economic space and the co-ordination of foreign, defence and security policies (Main 2006 and Nygren 2008). Despite progress in some areas, Russia and Belarus did not manage to agree on Belarus' place in the union. Alexander Lukashenko emphasised Belarus' sovereignty as an independent state in the union, while Putin wanted Belarus to become a subject of the Russian Federation. Trenin also argues that Lukashenko had hoped to succeed the ailing Yeltsin as president of the union, but later used the talks of a union state as a pretext for receiving Russian subsidies (in Lynch ed. 2005).

The economic aspects of the union became Putin's priority as Russian president, and he chose to downplay the political, security and defence aspects. Discussions continued anyhow on the political form of the union, albeit less frequently. Putin stated in August 2002 that the new union state would have to be in accordance with the Russian constitution, whereupon Lukashenko categorically rejected Putin's proposal as 'unacceptable to Belarus' (Nygren 2008 and RFE/RL 15 August 2002)⁴⁹. The talks experienced a brief positive development with the signing of the Constitutional Act in March 2003⁵⁰. However, the focus soon returned on economic aspects, with a renewed focus on the union currency which had been a stumbling block in the union idea (Nygren 2008 and RFE/RL 12 March 2003)⁵¹. The union currency was problematic for Belarus as Russia wanted full control over the central bank, while Belarus proposed a joint central bank. After Putin argued in August 2003 that a final decision should be made on the union currency, Lukashenko argued that the implementation of the union currency could only come *after* all other union agreements had been implemented (RFE/RL 2 September 2003)⁵². No solution was reached, and the introduction of the union currency has been delayed several times without any new timetable. The later years have seen few developments on the union state, which prompted Lukashenko in 2006 to propose a union with Ukraine as more feasible than with Russia (RFE/RL 27 November 2006). Despite the lack of progress on the union state, the relationship between Russia and Belarus has prospered in other areas. Trade has increased every year in Putin's presidency, and the two countries

⁴⁹ Putin insisted on a union with a single state, single parliament, and single government.

⁵⁰ The Constitutional Act suggested that Belarus and Russia should retain their sovereignty in the union state with a union government of its own that would interact with the respective national governments.

⁵¹ A formal decision was made in April 2001 to introduce the Russian rouble as the sole currency as of 1 January 2005, and a new union currency to be introduced as of 1 January 2008.

⁵² Lukashenko argued that "If we conclude the agreement without resolving economic and financial issues... we might be left without money, wages and pensions" (RFE/RL 2 September 2003)

enjoy a substantial cooperation within the military and defence sector. Belarus is Russia's closest military ally, and is a member of the Russian-dominated Collective Security Treaty Organisation (CSTO). The Belarusian armed forces are also assigned to a 300.000 joint command with Russia's western military districts⁵³, and the two countries adopted in 2001 a joint military doctrine (Trenin in Lynch ed. 2005).

5.3.2 The Last Dictatorship in Europe

Belarus has become increasingly politically isolated because of Alexander Lukashenko's authoritarian regime and poor human rights record, which has led to the labelling of Lukashenko's regime as the last dictatorship in Europe. Belarus has as a result sought closer ties with Russia as the EU has rejected cooperating with Belarus. Particularly important for Lukashenko was Vladimir Putin's support to a change in the Belarusian constitution which allowed Lukashenko to run for a third term in 2006. Russia has also established closer ties with Europe through increased cooperation and economic activity. Rontoyanni notes that Putin's and Lukashenko's relationship has been frosty, and that "Lukashenka's anti-Western rhetoric was arguably rather embarrassing to Putin's efforts to forge close relations with the EU and the US" (Lynch ed. 2005: 61).

5.3.3 Lack of Privatisation of the Belarusian Economy

Alexander Lukashenko's economic model has retained several Soviet-style characteristics⁵⁴. Russian companies have long sought to invest in the state-controlled Belarusian economy, but have been hindered by Lukashenko's unwillingness to loosen his political control over the economy. By retaining state-ownership, Lukashenko has managed to limit the influence of wealthy and influential oligarchs. The most coveted asset in Belarus has been BelTransGaz, the operator of Belarus' gas pipelines which account for ten percent of Russia's gas exports to Europe (Bruce 2005).

5.4 Georgia

Georgia is a small country with a population of about five million inhabitants. Nygren notes that Georgia has been "Russia's greatest strategic and foreign policy problem in the Caucasus" (2008:19) since Boris Yeltsin became Russian president.

⁵³ Belarus' armed forces constitute 80.000 of the 300.000 military personnel.

⁵⁴ According to Main (2006), the Belarusian state controls 75 percent of the economy, and roughly 54 percent of the adult population works in the state-controlled sector.

5.4.1 The Rose Revolution and Georgia's Westward Orientation

The Georgian parliamentary election was held on 2 November 2003, but the election was criticized by the OSCE and Council of Europe for not being of satisfactory standard⁵⁵. Eduard Shevardnadze, the Georgian president, did not agree with these observations, and called the election “the fairest and most transparent election ever held in Georgia” (RFE/RL 4 November 2003). Opposition candidate Mikhail Saakashvili did not accept the election result, and threatened with a ‘revolution’ if Shevardnadze did not step down. Following the Central Election Commission’s (CEC) announcement that the Shevardnadze-bloc was the winner after three weeks of counting⁵⁶, 30.000 Saakashvili supporters assembled around the government and parliament buildings. Shevardnadze then declared a state of emergency, but the army did not support Shevardnadze’s actions. After a meeting with the opposition leaders and Russia’s Foreign Minister Igor Ivanov, Shevardnadze resigned on 23 November 2003, with new presidential and parliamentary elections to be held in 2004. The presidential election in January 2004 saw Saakashvili elected as Georgian President. The political upheaval which brought Saakashvili to power has been called the Rose Revolution. Unlike the Orange Revolution in Ukraine, Russia played only a small role, and Saakashvili expressed surprise at Ivanov’s support following Shevardnadze’s resignation.

Saakashvili’s presidency has seen Georgia seek a closer relationship with Europe and the United States. Although Shevardnadze made an official bid for Georgia to join NATO in 2002⁵⁷, Saakashvili took it a step further and pledged during his presidential campaign to assign Georgian NATO membership the highest priority. Three months after his inauguration, Saakashvili handed over Georgia’s Individual Partnership Action Plan (IPAP)⁵⁸ as a way of “taking concrete steps to join the alliance” (RFE/RL 7 April 2004). Georgia became in October 2004 the first country to agree an IPAP with NATO. The instrument of Intensified Dialogue was formally offered to Georgia in September 2006, but the talks have since then not developed. Russian officials have voiced their disapproval of Georgian NATO membership several times. Following an informal meeting with NATO Defence Ministers,

⁵⁵ Nygren notes that two election problems common to FSU states were prevalent: forged voting lists and government-fund supported candidates.

⁵⁶ The CEC gave the Shevardnadze-bloc 123 of the 235 seats in the Georgian Parliament (Nygren 2008).

⁵⁷ Georgia was accepted as a NATO aspirant in March 2003, but NATO officials stated Georgia had a ‘very long road ahead’ before it fulfilled NATO requirements (Nygren 2008).

⁵⁸ The IPAP lists a set of cooperation objectives and priorities that each aspiring NATO member must hand over to NATO. The objectives deal with political and security issues; defence, security and military issues; public information; science and environment; civil emergency planning; and administrative, protective security and resource issues (NATO 2009a).

Russia's Defence Minister Sergei Ivanov warned that Russia would revise its policies towards Georgia if Georgia joined NATO, and added that such revisions "will not touch only on the military aspects" (RFE/RL 14 September 2005). Foreign Minister Sergei Lavrov also accused Georgia of seeking NATO membership in order to involve NATO for a military solution to the frozen conflicts in Abkhazia and South Ossetia (Adomeit in Rowe and Torjesen 2009).

Although Georgia has taken decisive steps towards joining NATO under Saakashvili, Georgia has still not been offered a Membership Action Plan (MAP). At a NATO summit in Romania in April 2008, the United States' president Georgia W. Bush wanted to offer Georgia a MAP, but several NATO members rejected Bush's proposal. France's Prime Minister Francois Fillon suggested Russian objectives had an important say in their rejection of Georgian NATO membership: "We are opposed to the entry of Georgia and Ukraine because we think it is not the right response to the balance of power in Europe and between Europe and Russia, and we want to have a dialogue on this subject with Russia" (Reuters 1 April 2008). Sergei Lavrov said after the NATO summit that Russia would do everything to prevent Georgia and Ukraine from joining NATO (Reuters 11 April 2008). Georgia's step to join the EU under Saakashvili has also progressed⁵⁹, albeit at a slower pace, and with fewer objections from Russia. Russia's criticism of the EU in relation to Georgia has largely centred on the EU's democracy promotion in FSU, like its support of Georgia's Rose Revolution in 2003. Georgia's close relationship with the United States has also worried Russia. Saakashvili's bloc was during the 2003 election campaign given substantial financial support from the United States. The United States has also strengthened a program which sees the United States offering army training assistance to the Georgian army (Nygren 2008).

5.4.2 The Frozen Conflicts in Abkhazia and South Ossetia

While Georgia declared independence from the Soviet Union in April 1991, two of Georgia's regions had already declared independence from Georgia in 1990. Abkhazia and South Ossetia have since then been de facto independent republics (the two regions are marked on map 3), and have received strong support from Russia. Several armed clashes have taken place between Georgia and the two regions. The most serious clash occurred in 1992 in Abkhazia, when a civil war erupted between ethnic Georgians and ethnic Abkhazians. Despite their status as neutral in the conflict, the Russian forces stationed in Abkhazia sided with the

⁵⁹ Georgia is currently part of EU's European Neighbourhood Policy (ENP), which is offered to the EU's immediate neighbours by land or sea (Nygren 2008).

Abkhazian forces⁶⁰. A failed cease fire agreement in 1993 was followed by another cease fire agreement in 1994, which stipulated the stationing of 3.000 Russian peacekeepers along the border between Abkhazia and Georgia. An Abkhazian referendum voted in 1999 in favour of Abkhazian independence (Nygren 2008).

Map 3: Georgia



Source: https://www.cia.gov/library/publications/the-world-factbook/maps/maptemplate_gg.html

The status of Abkhazia and South Ossetia was still unresolved when Vladimir Putin became Russian president in 2000. Several attempts have been made to solve the legal status of the two regions in Putin’s presidency. However, this was made more difficult after Saakashvili in his inauguration as Georgian president in 2004 promised to restore Georgia’s territorial integrity. A peace plan was proposed by Georgia in June 2004 which defined Georgia as a federal state where Abkhazia would be a ‘sovereign entity’, but the plan was rejected by Abkhazia. Another plan was proposed in September which would grant the two regions ‘the fullest and broadest form of autonomy’, but this plan was also rejected. Several failed attempts and increased Russian frustration over Kosovo’s status saw Putin withdraw his support for a UN draft peace plan for Abkhazia in February 2006, stating the need for

⁶⁰ Ethnic Abkhazians only constituted 18 percent of Abkhazia’s population in 1989, while ethnic Georgians constituted 48 percent. A civil war also erupted in South Ossetia in 1990, which ended with a cease fire agreement in 1992. South Ossetia voted in the same year in favour of uniting South Ossetia with North Ossetia in Russia. Georgian attempts to restore jurisdiction over the region was also in this case driven back by the support of Russian armed forces. A peace agreement was signed in 1992, which stipulated that Russia, Georgia and South Ossetia would deploy 500 peacekeepers each on the South Ossetian border (Nygren 2008).

universal principles in settling ‘frozen conflicts’ (Nygren 2008). Later in February 2006, the Georgian Parliament approved a resolution which called for the revocation of the 1992 agreement for Russian peacekeeping in Abkhazia and South Ossetia. The Georgian legislators argued that the Russian peacekeepers did not fulfil their mandate. Russia’s Foreign Minister Sergei Lavrov denounced the resolution as war-mongering, and warned that the peacekeepers would be kept in Abkhazia and South Ossetia to protect ‘our citizens’ from attack by Georgia (Nichol 2008). More than 90 percent of Abkhazian and South Ossetian residents have been issued Russian citizenship by the Russian Foreign Ministry, but Putin claims that Russia has no territorial ambitions (Nygren 2008 and Popescu 2006). Russia’s Defence Minister Sergei Ivanov also hinted that Georgia would pay a hefty economic price if they went ahead with the resolution, and said that “The Georgian leadership understands very well that without Russia, it will fail to deal with persistent problems in the country relating to energy issues” (Eurasia Insight 9 February 2006). The unresolved frozen conflicts have complicated Georgia’s aspirations to join the EU and NATO, and the status of the two regions was still unresolved at the end of Putin’s presidency in May 2008 (Light in Rowe and Torjesen ed. 2009).

Several other issues have also troubled Georgia’s and Russia’s relationship. Russia has accused Georgia for letting Chechen terrorists freely operate on Georgian territory, and Russia repeatedly postponed shutting down its Soviet legacy military bases on Georgian soil. Russia closed the final military base in 2006, 14 years after she had promised to do so. Russian authorities were further incensed in September 2006 when four Russian military officers were arrested and charged for espionage in Georgia. Putin denounced the arrests as ‘state terrorism’ and called Georgia a ‘bandit state’. Putin also recalled the Russian ambassador in Georgia, and implemented an air, sea and mail blockade on Georgia (Nygren 2008).

5.5 Moldova

5.5.1 Russian-Moldovan Relationship

Moldova is a landlocked country bordering Ukraine and Romania, and is one of the poorest countries in Europe. Moldova has since she became independent in 1991 been engaged in a conflict with Transnistria. Transnistria is a separatist region in the east of Moldova (see Map 4 below for localisation) that voted in favour of independence in a local referendum in 1990. Following Moldova’s declaration of independence in 1991, Transnistria followed suit, and has remained a de facto independent state since then. Moldova’s relationship with Russia has

been relatively strained since independence, largely due to Russia’s role in the Transnistrian conflict. A short war took place during the spring of 1992 between Moldovan forces and Transnistrian forces aided by the Russian 14th army. Russian forces have remained stationed in Transnistria since, and were assigned a peacekeeping status following the signing of a cease fire agreement in July 1992 between Moldova and Transnistria (Nygren 2008).

Map 4: Moldova



Source: https://www.cia.gov/library/publications/the-world-factbook/maps/maptemplate_md.html

The Transnistrian conflict has centred on two intertwined issues: the withdrawal of the Russian peacekeepers and firearms from Transnistria, and the legal status of the Transnistrian Republic. As Russian Prime Minister, Vladimir Putin signed the 1999 Istanbul resolution which stipulated the withdrawal of the remaining Russian peacekeepers, ammunition and firearms stored in Transnistria by 2002. Putin maintained this stance on his first visit to Moldova as Russian president. Despite the initial promises, Russia’s stance has not been consistent. After a meeting with the Transnistrian leadership in the spring of 2000, Putin stated that the withdrawal of troops and armaments had to be synchronized with the resolution of Transnistria’s status. The Russian Duma also refused to ratify the Istanbul resolution in June 2001, angering the newly elected Moldovan President Vladimir Voronin. Putin finally promised that the first stage of withdrawing the troops and armaments would be completed by the end of 2001, but the Russian time schedule was not met as Transnistrian authorities

complicated the OSCE's inspections of the trains carrying the armaments (Nygren 2008)⁶¹. Russia has also played an important role in attempting to solve Transnistria's legal status, and presented in November 2003 the Kozak plan. The Kozak plan proposed an asymmetrical federation between Moldova and Transnistria, with a unified defence, customs and finance systems and a single currency. Both Voronin and Transnistria's president Igor Smirnov initially reacted positively to the plan, but Voronin backed off from the agreement the day before the plan was ready to be signed⁶². Todua (2007) notes that Voronin noticed several Moldovan demands were not met in the final draft agreement. Voronin felt Transnistria was awarded too much power in the proposed asymmetrical federation, which enabled Transnistria to secede from the federation on the slightest pretext. A second Kozak plan was presented in October 2004, but it was immediately rejected by Moldova as Moldovan authorities felt it would lead to the 'disintegration of Moldova (Nygren 2008).

Russia's Foreign Minister Sergei Ivanov has linked the slow withdrawal of Russian troops and armaments to the lack of success in resolving Transnistria's legal status: "the reason the withdrawal of Russian weapons [has been halted] is known: the deterioration of Chisinau-Tiraspol relations after the refusal of the Moldovan authorities to sign [in November 2004] the Kozak memorandum – a document which represented a real solution [for solving] the Transdnister conflict" (RFE/RL 16 December 2004). The Russian-Moldovan relationship has been further strained by Moldova's interest in EU and NATO membership. Voronin expressed an interest in joining NATO and the EU when he was elected president in 2001, and reiterated this stance when he was re-elected in 2005. Moldova was in December 2004 presented an Action Plan by the EU which detailed plans for closer political and economic ties, and signed an IPAP with NATO in May 2006 (NATO 2009a and RFE/RL 9 December 2004). Vyacheslav Kovalenko, the Russian Foreign Ministry's CIS Affairs Department Director, said in November 2005 that the Transnistrian issue was not the only reason why Russia did not withdraw the troops and armaments. He went on to list Moldova's positive

⁶¹ Igor Smirnov, the Transnistrian president, stated that Russia was betraying Transnistria's interests and said that the withdrawal of troops and armaments needed to be synchronized with a normalisation of the relationship between Moldova and Transnistria.

⁶² Moldovans strongly disagreed with the Kozak plan, which led to large protests in Chisinau with calls for Voronin's resignation (Nygren 2008).

attitude towards NATO and the OSCE, and Moldova's role in GUAM⁶³. Kovalenko was particularly adamant that Moldova should be a 'neutral and demilitarized state'. Russian authorities conducted a massive political campaign in Moldova before the March 2005 general election aimed at lifting pro-Russian parties at the expense of president Voronin. Socor notes that "Moscow is signalling [...] that it will not forgive Voronin and his governing team for rejecting Russian-guaranteed "federalization" and seeking international support for the withdrawal of Russian troops" (Eurasia Daily Monitor 1 March 2005). Russian authorities were also angered by the Moldovan authorities' refusal to invite Russian and CIS election observers⁶⁴. The Russian Duma responded with a unanimous vote in favour of recommending Russia's government to impose economic sanctions on Moldova "in response to the Moldovan authorities' policy to escalate tensions around Transnistria (ibid.). The resolution called for visa regulations for Moldovan workers in Russia, charging market price for gas delivered to Moldova, and prohibitive taxation of Moldovan tobacco and wine products.

5.6 Ukraine

Ukraine is the largest of the FSU states besides Russia (see Table 6 p. 41), and has a closely knit history with Russia. Unlike Russia, Ukraine has little gas and oil reserves of its own, and is highly dependent on oil and gas imports from Russia to cover its needs. Moreover, Ukraine is Russia's most important transit country for Russian oil and gas. Roughly 80 percent of Russian gas exports exported through Ukrainian pipelines (EIA 2007).

5.6.1 The Orange Revolution

Viktor Yushchenko was on 26 December 2004 elected Ukrainian president, two months after the initial election was held on 31 October. The election process was marked by election fraud, and the subsequent political crisis and nationwide protests has been called the Orange Revolution. Yushchenko ran on a platform that aimed to lessen Ukraine's dependency on Russia, and he vowed to seek a closer relationship with European structures. Meanwhile, his main opponent in the presidential election, the Ukrainian Prime Minister Viktor Yanukovich, ran on a pro-Russian platform (Samokhvalov 2007). Yushchenko had prior to the election become severely ill by dioxin poisoning, but recovered sufficiently to run against

⁶³ GUAM was created in 1998 with the following members: Georgia, Ukraine, Azerbaijan and Moldova. Uzbekistan has later joined, and the organisation is now called GUUAM. GUAM is perceived by Russia as a pro-Western organisation intended to undermine the Russian-dominated CIS (Nygren 2008).

⁶⁴ The refusal to invite the election observers led Russia's Foreign Ministry to conclude that Moldova's leadership "does not welcome an objective assessment of the elections ... [an attitude] totally incompatible with its assurances about democracy and transparency" (Eurasia Daily Monitor 1 March 2005).

Yanukovich. Large protests erupted prior to the October election. The protesters feared that electoral fraud would be authorised by Ukraine's president Leonid Kuchma, who supported Yanukovich in the election. Vladimir Putin was also personally involved in the election. Although Putin stopped short of openly supporting Yanukovich in an appearance on Ukrainian television, Putin praised Yanukovich's performance as Prime Minister and his role in strengthening Russian-Ukrainian bilateral ties (Nygren 2008 and RFE/RL 27 October 2004). In a meeting with Kuchma and Yanukovich earlier in October 2004, Putin had made it clear Russia was not indifferent to the new Ukrainian leadership: "Ukraine stands on the threshold of very important internal political events. We will respect whatever choice the Ukrainian people makes. But of course we are not indifferent to what will happen, as the Ukrainian Presidential elections are not just a formal legal act. [...] And the future of Russian-Ukrainian relations will depend on how the next leadership of Ukraine organises its policies" (President of Russia 9 October 2004).

The October election handed Yanukovich a narrow victory⁶⁵, but since neither candidates received more than 50 percent of the votes, a second round had to be held on 21 November 2004. Although the exit polls for the November election showed a clear victory for Yushchenko, Yanukovich was declared the victor with 49 percent of the votes against Yushchenko's 47 percent (Nygren 2008). Both the OSCE's election monitors and the United States said the election failed to meet international standards, and Yushchenko refused to accept the election result. Meanwhile, CIS election monitors hailed the election as democratic, and Putin chose to congratulate Yanukovich on his victory despite the lack of an official result (RFE/RL 22 November 2004). The Central Election Commission's (CEC) announcement Yanukovich had won the election were followed by nationwide demonstrations, and the Ukrainian Supreme Court ordered a re-run of the election to be held on 26 December 2004. The December election awarded Yushchenko 52 percent of the votes, and Putin surprisingly immediately recognized the election result (Nygren 2008).

Russian authorities were critical of what they perceived as Western meddling in the Ukrainian election. Three days after Putin prematurely congratulated Yanukovich on his victory, Russia's Foreign Minister Sergei Lavrov urged European governments to "respect the choice of the Ukrainian people and let them decide by themselves how to settle their domestic

⁶⁵ The Ukrainian Central Election Commission (CEC) awarded Yanukovich 40 percent of the votes, while Yushchenko received 39 percent of the votes.

disputes” (RFE/RL 26 November 2004). Lavrov criticized Western governments for their dismissal of the election result, and said there was no reason to it. Lavrov also suggested that the OSCE was being used as a tool for political influence, and Putin criticized the influx of money from Europe and the United States (RFE/RL 8 December 2004).

5.6.2 Ukraine’s Realignment With the West

Viktor Yushchenko was not the first Ukrainian president to seek a closer relationship with the West. Both of his predecessors, Leonid Kravchuk and Leonid Kuchma, had established ties with the EU and NATO. Ukraine was the first CIS country to join NATO’s Partnership for Peace (PfP) agreement in 1994, and signed up for future memberships in EU and NATO⁶⁶. Kuchma’s flirtation with NATO was not well received in Russia, but the strengthening of the Russian-Ukrainian relationship in other areas helped smooth the relationship. Most of the issues had been solved by the time Vladimir Putin became Russian president in 2000. The 1997 Russian-Ukrainian treaty helped solve several problems⁶⁷, and Putin and Kuchma enjoyed a good personal relationship. Trade between the two countries increased, and defence cooperation and joint arms production boomed (Nygren 2008). Moreover, several scandals in Kuchma’s second term as Ukrainian president led to a growing isolation from the EU and the United States. As a result, Kuchma sought to strengthen his relationship with Putin (Fischer 2008 and Nygren 2008).

At the time of Yushchenko’s inauguration as Ukrainian president in January 2005, three FSU states had already joined NATO and the EU. This meant that Ukraine and other FSU states now bordered member countries. Yushchenko made it clear during the election campaign and in the aftermath as Ukrainian president that he would seek Ukrainian NATO membership. Russian authorities warned this would have consequences for Ukraine’s relationship with Russia. Russia’s Foreign Minister Sergei Lavrov said that while Russia would not obstruct Ukraine’s right to choose its own partners, Ukraine could not rely on privileged economic relations with Russia (RFE/RL 4 January 2005). Putin also said in a speech at a Security Council meeting in January 2005 that “We remain convinced there is no real justification for NATO’s geographical expansion” (President of Russia 29 January 2005). Yushchenko ordered Ukraine’s military doctrine to be prepared for NATO membership in April 2005, and

⁶⁶ Ukraine also signed the Partnership Agreement with the EU in 1994, the EU Common Strategy for Ukraine in 1999, and was in 2004 included in the European Neighbourhood Policy (Nygren 2008).

⁶⁷ The dissolution of the Soviet Union left several unresolved questions: the status of Russia’s Black Sea fleet and the naval base in Sevastopol, the handling of Soviet nuclear weapons on Ukrainian soil, the status of Crimea, and unresolved border issues (Fischer 2008).

continued to reaffirm Ukraine's membership plans (Nygren 2008). Ukraine and NATO launched at the same time an Intensified Dialogue⁶⁸, and Yushchenko also made it clear he would seek EU membership. Although the European Parliament in early 2005 called for the Council to consider deeper cooperation with Ukraine, the lack of clear signals caused disappointment on the Ukrainian side. Fischer notes that Russian opposition to Ukrainian EU membership is likely due to the fear of losing the large Ukrainian market where Russia has a dominant position (in Fischer ed. 2008)⁶⁹.

5.6.3 Ukraine's Pipeline System

Ukraine's gas pipeline system is Russia's principal line for transporting gas to Europe (Map 2 on p. 23 shows the pipelines that cross Ukraine's territory). Gazprom has long sought to acquire ownership in Ukraine's pipeline system, which is owned by the Ukrainian state-owned company Naftogaz. Gazprom allowed Ukraine throughout the 1990s to amass a large gas debt, and pressured Ukraine into entering negotiations over an international consortium that would own the pipeline system. Gazprom promised to cancel Naftogaz's gas debt and keep Ukraine's gas price low and stable if a consortium was created. The consortium would consist of Gazprom, Naftogaz, and Ruhrgas⁷⁰. Despite signing the funding documents in November 2002, no agreement was reached on the consortium, and it was declared dead by Yushchenko in June 2005 (Eurasia Daily Monitor 16 October 2006, Russian Analytical Digest 20 May 2009, and Stern 2009). After Putin called to unite Russia's and Ukraine's pipeline system in February 2007, the Ukrainian Parliament voted unanimously in favour of a law that bans the privatisation, sale, transfer, merger or joint venture of the country's pipeline system (RFE/RL 6 February 2007). Ukraine's pipeline system has also been a source of blackmail for Gazprom, as Ukraine has repeatedly siphoned off gas meant for Europe during the 1990s and early 2000s⁷¹, and Naftogaz has often been chronically late in settling its gas debt.

⁶⁸ Intensified Dialogue is a clear signal of support from NATO members for future membership (NATO 2009b).

⁶⁹ 50 percent of the Ukrainian industry was in 2002 owned by Russian capital (Nygren 2008).

⁷⁰ Ruhrgas is a German company. Germany is Russia's largest customer in Europe, and has a large interest in stable supplies from the Ukrainian pipeline system.

⁷¹ Gazprom has also reported missing gas from storage facilities in Ukraine. Gazprom reported missing 7.8 bcm in May 2005, which raised the question whether Russian gas could be stored safely in Ukraine (Stern 2006).

Chapter 6: The 13 Cases of Russian Energy Aggression

6.1 Introduction

After having discussed in chapter five Russia's relationship with the seven countries that have been subject to Russian energy aggression, it is now time to turn to the 13 cases of Russian energy aggression. The cases are the units of analysis in this thesis which the analysis in chapter seven will be based on. This chapter will outline the cases by focusing on how the events unfolded. I will pay particular focus on the negotiation process in order to see which proposals were made and to see if any statements were made that can reveal the back ground for the cases. Before I turn to the cases, I would like to remind the reader how the cases were identified. Russian energy aggression is in this thesis understood as Russian energy cut offs of oil and gas supplies and threats of oil and gas cut offs, and the thesis is limited to cases that have taken place in Vladimir Putin's presidency. The list is non-exhaustive as not all cases of Russian energy aggression is included.

6.2 Belarus

6.2.1 September 2002

Belarusian authorities and Gazprom agreed in April 2002 to sign an agreement whereby Belarus would continue to receive gas from Gazprom at a Russian price level. Belarus would in turn privatise BelTransGaz, the gas transit and transmission network, and create a 50/50 joint venture with Gazprom. However, Belarusian authorities broke this promise. Gazprom discovered in September 2002 that BelTransGaz had not been removed from a list of strategic companies that could not be privatised, and threatened Belarus with a suspension of gas deliveries and a price increase. Gazprom's threat was never executed, and BelTransGaz had by April 2003 become a joint stock company, though still only Belarusian owned (Yafimava and Stern 2007).

6.2.2 January 2004-June 2004

Gazprom cut Belarus' gas supplies on 1 January 2004. Gazprom had already in September 2003 announced a price hike for Belarus. The announcement came at the same time as Gazprom announced it was not interested in acquiring a stake in BelTransGaz due to Minsk's unacceptable terms. Belarus paid at the time \$28-30 per tcm, while neighbouring Ukraine paid \$50 per tcm. The move was supported by the Russian government, which came less than a month after the two countries' dispute over the implementation of the union currency. In

December 2003, Gazprom offered Belarus to continue receiving subsidised gas as if Belarus accepted Gazprom's offer of \$600 million for BelTransGaz. Minsk responded by demanding \$5 billion, and Gazprom countered by cutting Belarus' gas supplies (RFE/RL 10 September 2003, Eurasia Daily Monitor 9 June 2004, and Yafimava and Stern 2007). The independent Russian gas producers Itera and TransNafta were allowed to temporarily supply Belarus with gas. Gazprom officials maintained that Belarus' gas service would be normalised if Belarus agreed to privatise BelTransGaz. By the end of May 2004, Itera and TransNafta had almost exhausted their governmental-allocated export quota, and Belarus ran the risk of being left without gas supplies. The dispute was resolved in June 2004 when Belarus agreed to pay \$46.68 per tcm⁷², but Gazprom did not manage to acquire a stake in BelTransGaz (Eurasia Daily Monitor 9 June 2004 and Main 2006).

6.2.3 September 2006-January 2007

Russia and Belarus were involved in an oil dispute in 2006-2007. Russia were according to an agreement from 1995 entitled to 85 percent of the profits generated from Belarus' export of refined oil. However, Belarus had since 2001 no longer transferred Russia's share of the profits. Russian oil deliveries had also been delivered duty free since 1995. Russia estimated in 2006 that it was losing \$4 billion annually due to Belarus' non-payment, and asked Belarus' authorities to hand over the profits. Transneft put pressure on Belarus by cutting oil deliveries by pipeline from four million tons to three million tons in the fourth quarter of 2006. Transneft also threatened to reduce Belarus' oil supplies for 2007 to only eight million tons, down from 19.75 million tons scheduled in 2006 (Main 2006 and Eurasia Daily Monitor 8 November 2006). The importance of Russian oil exports for the Belarusian economy is demonstrated by Belarus' export figures in 2004: export of oil products amounted to 45.6 percent of Belarus' ten most exported products in 2004 (Zaiko 2006)⁷³. Russian authorities decided on 1 January 2007 to impose an export duty of \$180 per ton oil sold to Belarus. Belarus in turn responded with a transit charge of \$45 per ton Russian oil shipped through Belarus' territory. After Russia refused to pay the import duty, Belarus started siphoning off oil from the pipelines as payment for the transit charge. Transneft started on 5 January 2007 to reduce oil shipments through Belarus' pipelines, and halted oil shipments completely on 8 January. The dispute was settled two days later, which saw Belarus revoke the \$45 per ton

⁷² The price was also applied retroactively to the gas Belarus received in the period of Gazprom's supply cut. The new deal also entailed a higher transit fee for Gazprom's gas transport through Belarusian pipelines.

⁷³ Belarus' profits for 2005 and 2006 would be even higher due to the higher oil prices in those years (see Figure 1 on p. 31).

transit charge on Russian oil (Financial Times 11 January 2007). Russia's export duty was renegotiated only two days later, and was lowered to \$53 per ton oil. Belarus and Russia also agreed on the taxation of refined oil products, with Russia set to receive 70 percent of the profits in 2007 (Financial Times 15 January 2007)⁷⁴. After the dispute had been settled, Vladimir Putin remarked in a statement that despite the recent events, Russia would continue to subsidise Belarus' economy for a long time. Putin estimated that Russia's oil and gas subsidies to Belarus alone would amount to \$5.8 billion for 2007 (RIA Novosti 15 January 2007).

6.2.4 January 2007

At the same time as Gazprom increased the gas price and cut supplies to other FSU states in 2006, Belarus continued to receive a preferential gas price of \$46.68 per tcm until January 2007⁷⁵. Shortly after the Belarusian presidential election in March 2006, Gazprom announced that Belarus would have to begin paying market prices for gas, which would entail at least a threefold price increase. Gazprom offered Belarus the option of receiving cheaper gas in return for a stake in BelTransGaz, but set the deadline at 30 April 2006 for the deal to be completed (New York Times 31 March 2006 and New York Times 7 April 2006). After Gazprom and Belarus could not settle the gas price, Gazprom threatened to cut Belarus' gas supplies as of 1 January 2007. Gazprom's final asking price was \$105-110 per tcm, which was a combination of cash and shares in BelTransGaz. Belarus, on the other hand, was only willing to pay \$75 per tcm, and objected to selling BelTransGaz. Belarus and Gazprom reached an agreement on New Year's Eve 2006, only minutes before Gazprom's deadline expired. Belarus had to concede to Gazprom on every issue. The new deal saw Belarus pay \$100 per tcm for Russian gas in 2007, with the price set to increase gradually to European levels by 2011. Gazprom also obtained a 50 percent stake in BelTransGaz for \$2.5 billion (Goldman 2009 and RFE/RL 1 January 2007)⁷⁶.

6.2.5 August 2007

Gazprom threatened to reduce Belarus' gas supplies by 45 percent as of 3 August 2007. The threat was announced after Gazprom and the Belarusian authorities failed to reach an

⁷⁴ Russia's share was also negotiated to increase in 2008 and 2009 to 80 and 85 percent respectively.

⁷⁵ Ukraine was in 2006 charged \$235 per tcm, while Moldova was charged \$110 per tcm and later \$160 per tcm, but also had to hand over a stake in Moldovagaz.

⁷⁶ Gazprom did not acquire the 50 percent share outright. Gazprom would instead acquire 12.5 percent of the shares annually for \$625 million for four years, which will see Gazprom own 50 percent of the shares in BelTransGaz in 2010. The first instalment was made on 1 June 2007.

agreement over Belarus' gas debt of \$456 million that was due for Gazprom's gas deliveries for the first six months of 2007. The threat was never executed as Belarus agreed to pay the gas debt within a week. The first payment of \$190 million was made on 3 August (New York Times 2 August 2007).

6.3 Estonia

6.3.1 May 2007

Following the relocation of the Bronze Soldier in Tallinn, Russia halted deliveries of oil products to Estonia by railway on 2 May 2007. According to the Russian rail monopoly, Russian Railways, the halt came as a result of maintenance work being performed on the rail link to Estonia. A quarter of Russia's export of oil products are sent by rail to Estonia, from where it is re-exported to Northern Europe. Simultaneously, Russian coal exports to Estonia were also halted, citing a shortage of railway wagons. Russian Railways denied any political motives for the disruption (Reuters 2 May 2007). The day after the halt in oil deliveries, Russia's Foreign Minister Sergei Lavrov stated that the relocation of the war memorial would have 'serious negative consequences' on the bilateral ties between Russia and Estonia (RFE/RL 3 May 2007 and RFE/RL 8 May 2007). Russia resumed oil shipments to Estonia on 17 May (RFE/RL 17 May 2007). Two months after the supply disruption, Russia's Transport Minister Igor Levitin provided additional information regarding Russia's halt of oil deliveries to Estonia. Besides Russia's increased capacity in Primorsk, Levitin stated there were political reasons behind the dispute, and said that "business will develop where the situation is comfortable and profitable and where the moral and political climate is favorable" (U.S.-Russia Business Council 27 July 2007). Levitin also said that while Russia will continue to use ports in neighbouring states, strategic materials like refined oil products will only be shipped through Russian ports (ibid.). The European Parliament's resolution on the dispute "condemns the attempts by Russia to exert economic pressure on Estonia as an instrument of foreign policy and calls on the Russian government to restore normal economic relations between the two States" (European Parliament 24 May 2007).

6.4 Georgia

6.4.1 November 2006

A few weeks after Georgia arrested four Russians suspected of espionage, Gazprom threatened in November 2006 to cut Georgia's gas supplies in 2007 if they did not accept a

doubling of last year's gas price. Gazprom's offer for 2007 was \$235 per tcm, more than double the price Georgia paid in 2006⁷⁷. The price offered was the highest to the FSU states, on a par with Western European gas prices. Meanwhile, Gazprom's Deputy CEO Alexander Medvedev said that Georgia could offer assets to negotiate a lower price. Georgian pipelines are like all former Soviet pipelines connected to the Russian pipelines system, and the Georgian pipelines are also used to supply Armenia, a close Russian ally. This was not the first time Gazprom had expressed an interest in Georgia's pipelines, as they had expressed interest in buying Georgia's pipeline system in January 2005 (Civil Georgia 21 January 2005, Civil Georgia 25 November 2005 and Eurasia Daily Monitor 9 November 2009). Georgia rejected Gazprom's offer as they considered the pipelines too strategically important, and opted instead to pay the full price for Russian gas in 2007. Georgia accepted Gazprom's terms while knowing Azerbaijan would be able to supply two-thirds of Georgia's gas requirements from 2007 onwards following the opening of the Shah-Deniz gas field in January 2007. An unofficial report suggested Georgia paid \$120 per tcm for Azerbaijan's gas, and Georgia will also receive gas as transit fee payment for the pipeline that crosses Georgian soil (Eurasia Daily Monitor 17 January 2007).

6.5 Latvia

6.5.1 2002-2003

The Latvian oil terminal in Ventspils (see Map 2 p. 23) is owned by Ventspils Nafta, and is the largest of its kind in the Baltics. The Ventspils terminal accounted for 22 percent of the entire Baltic Sea oil market in 2002. The sole supplier of oil to Ventspils Nafta was Transneft (RFE/RL 11 July 2002 and New York Times 21 January 2003). Ventspils Nafta first started to suffer from decreasing oil shipments from Russia in April 2002. By September, Ventspils Nafta received only one-third of its capacity. RFE/RL reported that Transneft withheld oil to Ventspils Nafta until it agreed to sell a stake to Transneft. Semyon Vainshtok, the CEO of Transneft, made contradictory statements regarding Transneft's interest in Ventspils Nafta. While denying interest in buying a stake, Vainshtok stated that "I suppose Transneft will agree to buy controlling interest in Latvia's port if the Latvian shareholders ask for it" (RFE/RL 22 October 2002). Vainshtok further stated that "If Transneft decides to develop Primorsk, Ventspils will dry up. But if we are going to suspend phase two of the Baltic Pipeline System, then Ventspils should be controlled by the Russian side" (ibid.). Russia's

⁷⁷ Georgia paid \$110 per tcm in 2006. Gazprom also nearly doubled Georgia's gas price in 2006, which increased from \$63 per tcm in 2005 to \$110 per tcm in 2006.

halt of oil shipments to Latvia happened at a time when Russia was experiencing a post-Soviet record in oil production. Russia's oil production was up four percent in the first ten months of 2002, while Ventspils Nafta oil shipments were down 42 percent with severe financial ramifications for the company (RFE/RL 6 November 2002)⁷⁸.

By January 2003, Ventspils' oil shipments had completely dried up. Transneft cited too high tariffs using the terminal, opting to use their own oil terminal in Primorsk instead (see Map 2 p. 23). Transneft's complete halt of oil shipments to Ventspils happened in the same year as Transneft had stated it would increase oil exports by pipeline by at least 16 percent (New York Times 21 January 2003). Russian oil producers were infuriated by Transneft's actions as Russian oil production and oil prices were soaring. The CEOs of five major oil companies, Lukoil, Yukos, Surgutneftegaz, Tyumen Oil and Rosneft, wrote a letter to Russia's Prime Minister Mikhail Kasyanov where they criticized Transneft's decision. The CEOs called the reason for Transneft's supply cut as 'artificial', and even urged Kasyanov to increase oil shipments to Ventspils. Their motion was rejected, and Russian oil exports to Ventspils Nafta were in February 2003 down 99 percent (RFE/RL 21 January 2003, New York Times 21 January 2003 and RFE/RL 12 February 2003). Transneft continued to send mixed signals regarding their intention with Ventspils Nafta. Although it denied it was plotting a takeover, Transneft acknowledged a desire to buy a stake in the company. Transneft's vice-president Sergei V. Grigoriyev stated that Transneft would be ready to invest in an expansion of the pipeline to the Ventspils port if they had a stake in Ventspils Nafta (New York Times 21 January 2003). In February 2003, Grigoriyev also stated that "Oil can only flow from Russia. You can of course sell [the port] to Westerners. But what are they going to do with it? Turn it into a beach?" (RFE/RL 12 February 2003), and requested that Ventspils Nafta discuss a deal exclusively with Transneft, stating that Transneft would not participate in an open tender.

At the same time as Ventspils Nafta's oil shipments were halted, harsh weather conditions affected Russia's oil exports in the winter of 2003⁷⁹. Due to limited export possibilities, more oil than normal remained on the Russian market, where oil was sold for as little as 5 \$/barrel. In comparison, the average oil price in 2003 was 26.85 \$/barrel, more than five times the Russian domestic oil price (Figure 2 on p. 32 shows the average oil price). Russian oil

⁷⁸ Ventspils Nafta's profits for 2002 plunged 99 percent compared to 2001 (RFE/RL 12 February 2003). Ventspils Port handled 24.3 percent less cargo in 2002 (RFE/RL 13 January 2003).

⁷⁹ The Russian oil terminal in Novorossiisk was shut down several times during the winter due to bad weather, while Primorsk was clogged up with ice up to 25 meters thick.

producers sought instead other export options. Lukoil exported oil through Iranian pipelines, while Yukos utilized far more expensive river and rail options to export oil (RFE/RL 7 March 2003). Transneft later rejected an offer to buy a stake in Ventspils Nafta since Latvian authorities did not offer a controlling stake (RFE/RL 18 March 2003). As of 2008, Transneft had not resumed oil shipments to Ventspils Nafta. The port has instead been supplied by railway, operating at little more than half its normal capacity (Kandiyoti 2008).

6.6 Lithuania

6.6.1 1999-2001

Mazeikiu Nafta is an oil complex that includes the only refinery in the Baltic States⁸⁰, a maritime oil terminal in Butinge (The Butinge terminal is shown in Map 2 p. 23), the Birzai pipeline, and several retail outlets. Mazeikiu Nafta is Lithuania's largest economic asset, and accounts for roughly ten percent of Lithuania's GDP. This makes it Lithuania's largest tax payer, with €209 million in net profits for 2004 (Eurasia Daily Monitor 31 March 2005 and Eurasia Daily Monitor 1 July 2005). Mazeikiu Nafta was first subject to Russian interest in 1999. Lukoil expressed an interest in buying the company, but the Latvian government chose instead to sell a minority stake and the operating rights to the American company Williams International (New York Times 30 October 1999)⁸¹. Lukoil was at the time the government-assigned coordinator of Russian oil exports to the Baltic States, and cut Mazeikiu Nafta's oil supplies shortly after Williams International's acquisition of the company. Lukoil cut Mazeikiu Nafta's oil supplies nine times in the period between 1999 and 2001. Bugajski notes that "Lithuania was given several ultimatums that Lukoil would cut off its supplies unless the company was allowed to acquire majority shares in the pipeline from Belarus to the Baltic Sea and in the Mazeikiai refinery" (2004: 130).

Lukoil's supply cuts heavily indebted Mazeikiu Nafta and Williams International, and deprived Lithuania of its most important source of tax revenues (Eurasia Daily Monitor 31 March 2005). Lukoil hoped that Mazeikiu Nafta's financial squeeze would allow it to acquire a controlling stake in the company. Instead, Yukos bought 26.85 percent of the shares in Mazeikiu Nafta in June 2001⁸². After Yukos announced its acquisition of Mazeikiu Nafta,

⁸⁰ Mazeikiu Nafta is also one of the biggest refineries in Central and Eastern Europe (Baran 2007).

⁸¹ Williams acquired a 33 percent stake in Mazeikiu Nafta in October 1999 for \$75 million, with the option to raise its stake in the company to 51 percent within five years.

⁸² Yukos, unlike Lukoil, had a reputation for being a truly private company that was not controlled by the Russian state (Bugajski 2004).

Lukoil imposed a complete halt of oil shipments to Mazeikiu Nafta. Yukos' stake in Mazeikiu Nafta was increased to 53.7 percent in September 2002, when Williams International was bought out from the company (RFE/RL 27 June 2001, RFE/RL 23 August 2002, and New York Times 19 September 2002)⁸³.

6.6.2 2005-2006

After Yukos was targeted by the Russian state in 2003 and 2004 on several charges, Transneft imposed a complete halt of oil deliveries to Mazeikiu Nafta as they did not allocate Yukos any export quota for the second quarter of 2005. The move was seen as an attempt to force Yukos entirely out of business and to set the stage for a takeover of Mazeikiu Nafta by a Russian company. Lukoil had previously announced it had entered into negotiations to buy Yukos' 53.7 percent stake in Mazeikiu Nafta (Eurasia Daily Monitor 31 March 2005). A Moscow court ordered a freeze on trading Yukos' main assets on 5 April 2005, which barred Yukos from selling its stakes in its major subsidiaries. Russia's Ministry of Justice also asked Lithuania to stop Yukos from selling its shares in Mazeikiu Nafta (New York Times 19 April 2005 and New York Times 26 June 2005). Since Mazeikiu Nafta was owned by the Netherlands-registered Yukos International, Eduard Rebgun openly declared he was seeking to block Lithuania's acquisition of Yukos' shares in Mazeikiu Nafta (Eurasia Daily Monitor 26 April 2006)⁸⁴.

PKN Orlen, Central Europe's largest refiner of oil, ultimately sealed the deal, and acquired Yukos' 53.7 percent stake in Mazeikiu Nafta in May 2006 for \$1.47 billion. PKN Orlen also bought a 30.7 percent stake from the Lithuanian government for \$851.8 million (New York Times 29 May 2006). The Russian companies Lukoil and TNK-BP, and KazMunayGaz from Kazakhstan, also bid for Mazeikiu Nafta. KazMunayGaz's bid was, however, weakened as Transneft blocked the proposed transit of Turkmen oil across Russia to Mazeikiu Nafta (Eurasia Daily Monitor 1 June 2006). Two months after PKN Orlen had bought Mazeikiu Nafta, Transneft stopped pipeline deliveries to the company citing technical reasons for the stoppage of deliveries⁸⁵. Transneft said an oil spill had taken place on 29 July 2006. The pipeline spill would not affect Russian oil exports to Europe, only to Lithuania. Transneft also

⁸³ The Lithuanian state retained a priority right in Mazeikiu Nafta as it considered the ownership rights as a national security issue. The priority right gave the Lithuanian state a right to buy Yukos' shares at a later point by matching the highest bid (Eurasia Daily Monitor 17 March 2006).

⁸⁴ Rebgun, the Moscow-court appointed temporary administrator of Yukos, failed to block the trading of Yukos' stake in Mazeikiu Nafta, as it was beyond the Moscow court's jurisdiction (Eurasia Daily Monitor 1 June 2006).

⁸⁵ The pipeline had provided 80 percent of the Mazeikiu Nafta's crude oil (New York Times 31 October 2006).

said that the work would take one year and nine months as the pipeline could not be repaired, but had to be replaced entirely. Transneft's time frame differed radically from normal time frames for pipeline repairs, which usually only take a few weeks to finish (Eurasia Daily Monitor 3 August 2006 and Eurasia Daily Monitor 7 March 2007). The supply cut meant Mazeikiu Nafta had to operate below capacity and obtain crude oil by ship. Crude oil deliveries by ship adds at least an additional 2-2.5 \$/barrel in costs, which in a year amounts to a minimum of \$146 million in additional costs annually for Mazeikiu Nafta (New York Times 7 August 2006 and New York Times 3 July 2007). Despite high oil prices in 2006, Mazeikiu Nafta's profits decreased 75 percent. After no work had been done to repair the pipeline to Lithuania, Russia's Industry and Energy Minister, Viktor Khristenko, announced in May 2007 that repairing the pipeline would be too complex and uneconomic. Oil supplies would instead be ported to Primorsk, from where Mazeikiu Nafta now has to be supplied by tanker (Eurasia Daily Monitor 6 June 2007).

6.7 Moldova

6.7.1 January 2006

While Europe's attention was focused on the Russian-Ukrainian gas crisis, Russia simultaneously imposed a complete halt on Moldova's gas supplies on 1 January 2006. Gazprom's offer to Moldova for 2006 was \$160 per tcm, twice the price Moldova had paid in 2005. The Russian supply cut happened despite the fact Moldova had paid its gas bills on schedule each year. Moldova, which is 100 percent dependent on Russian gas, was supplied with gas from neighbouring Ukraine while the supply cut lasted (RFE/RL 2 January 2006 and Eurasia Daily Monitor 4 January 2006). A temporary agreement was reached on 16 January 2006 between Russia and Moldova. The agreement saw Moldova's gas price increase from \$80 per tcm to \$110 per tcm, but it was only valid for the first six months of 2006. Moldova also had to concede a 13.4 percent stake in Moldovagaz to Gazprom, increasing Gazprom's stake in the company to 63.4 percent. The 13.4 percent stake was owned by the Transnistrian authorities, but could not be traded legally without Moldovan consent⁸⁶. After the temporary agreement expired at the end of March, Russia and Moldova signed a new agreement for the rest of 2006 which set Moldova's gas price at \$160 per tcm. Russia continued at the same time to supply the Transnistrian authorities with gas without collecting any payment for the debt (Eurasia Daily Monitor 18 January 2006 and Eurasia Daily Monitor 4 January 2007).

⁸⁶ Gazprom acquired a stake in Moldovagaz and other ventures during the 1990s, when Moldova's weak economy led to an indebted relationship with the company.

6.8 Ukraine

6.8.1 January 2006

Russia cut Ukraine's gas supplies on 1 January 2006, after protracted negotiations during the autumn of 2005 offered no agreement on Ukraine's gas price for 2006. The Russian Duma voted unanimously in July 2005 that CIS countries should pay European prices for Russian gas⁸⁷. Ukraine had in 2005 paid \$50 per tcm, while Gazprom's initial offer for 2006 was \$160 per tcm. Ukrainian authorities announced they were ready to pay market prices for gas, but said that it would have to be a phased transition to a market based pricing system. The negotiations deteriorated in October 2005 when Naftogaz threatened to siphon off gas from the pipelines if no settlement was reached. Gazprom increased Ukraine's offer to \$230 per tcm towards the end of 2005 as the 'market price' had changed since the initial offer was made. Gazprom also threatened to cut Ukraine's gas supplies if no agreement was reached by the end of the year. Kremlin supported Gazprom's stance, with Putin taking a leading role in the negotiations (Larsson 2006 and Stern 2006). Gazprom's interest in the Ukraine's pipeline system was again resurrected by Alexei Miller, the CEO of Gazprom, as he stated that Ukraine should surrender the pipelines to a consortium controlled by Russia, Ukraine and Germany in order to avoid a fourfold increase in Ukraine's gas price (New York Times 16 December 2005).

After no agreement was reached, Gazprom cut its gas exports to the Ukrainian pipelines equal to Ukraine's gas consumption on 1 January 2006. Meanwhile, Gazprom continued to export gas to Europe using the Ukrainian pipeline system. Although Europe's gas supplies were meant to be untouched, Naftogaz tapped into the gas deliveries for technical gas⁸⁸, with several European countries experiencing a gas shortfall. Deputy Chairman of Gazprom, Alexander Medvedev, reiterated Miller's offer, and said Gazprom would consider exchanging joint ownership in the Ukrainian pipelines for agreeing to a transition period to market prices: "We are ready to consider other assets that may be of interest to us, [...] But we are particularly interested in the transit pipelines in Ukraine" (Financial Times 3 January 2006b). Gazprom and Naftogaz reached an agreement on 4 January 2006 to resume Ukraine's gas supplies. The agreement set Ukraine's gas price for 2006 at \$95 per tcm. Ukraine's gas price was made up of a majority of cheap gas imported from Turkmenistan at \$65 per tcm, while

⁸⁷ Not all CIS members were included, only Georgia, Moldova, Ukraine, Estonia, Latvia and Lithuania.

⁸⁸ Technical gas is used to provide sufficient pressure in the pipelines for the gas to flow.

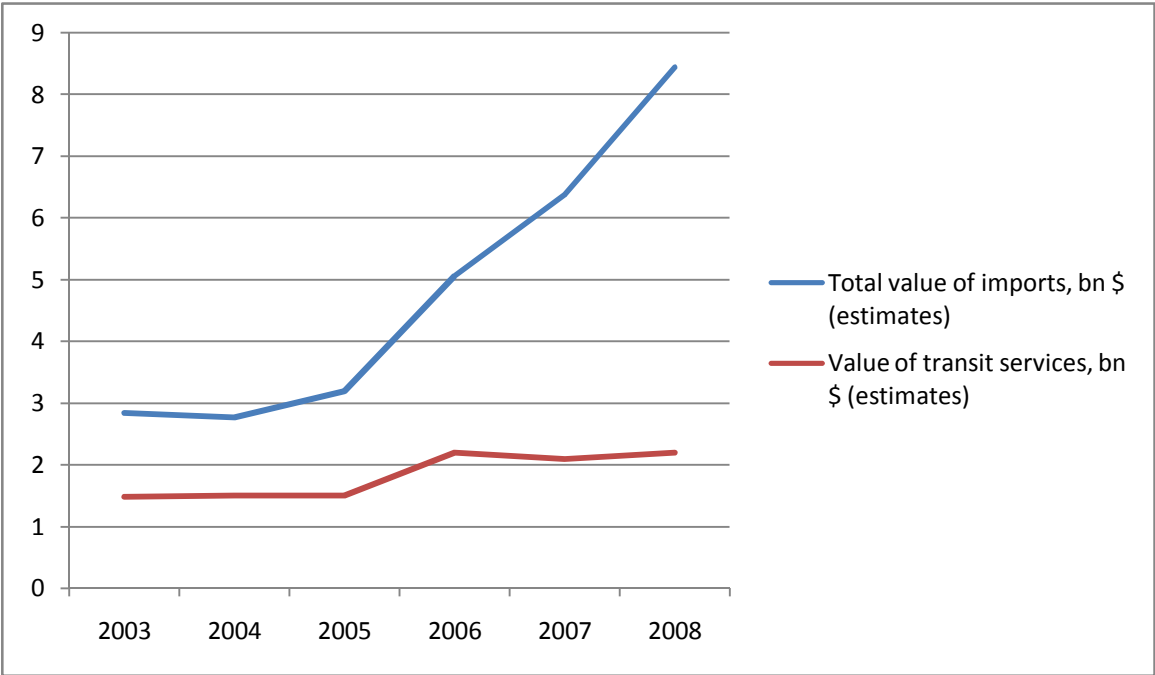
Gazprom supplied the rest at \$230 per tcm. Despite holding no assets of its own, the agreement also made RosUkrEnergo the intermediary company responsible for selling the gas to Ukraine⁸⁹. RosUkrEnergo is a Swiss-registered company that is 50 percent owned by Gazprom, while the other half is owned by the two Ukrainian businessmen Dmitri Firtash and Ivan Fursin (Goldman 2008). Ukraine agreed to import 73 bcm of gas, but had to transfer 20 percent (14.6 bcm) of the gas to RosUkrEnergo. The 14.6 bcm of gas was payment for RosUkrEnergo's service of delivering the gas to Ukraine, which RosUkrEnergo in turn was free to re-export. The agreement also made UkrGazEnergo, RosUkrEnergo's subsidiary, responsible for distributing gas to industrial users in Ukraine, thus capturing Naftogaz's largest source of profit. Meanwhile, Naftogaz was contractually obliged to supply district heating companies and residential users who often had payment difficulties (Russian Analytical Digest 20 January 2009).

The agreement also set a new transit fee for Russia's use of the Ukrainian pipelines, which increased from \$1.09 per 100 km/mcm to \$1.60 per 100 km/mcm. The new transit fee increased Naftogaz's transit revenues from \$1.5 billion in 2005 to \$2.2 billion in 2006. However, while Ukraine's gas price was to be renegotiated annually, Naftogaz's transit fee was locked for five years until 2010⁹⁰. While Naftogaz's transit revenues only increased nominally, Ukraine's gas expenditures nearly tripled between 2004 and 2008. Furthermore, while the transit revenues for 2005 covered nearly half the price for the imported gas, Ukraine's transit revenues only covered slightly over one-quarter of Ukraine's gas expenditures in 2007 (Russian Analytical Digest 20 May 2008 and Russian Analytical Digest 20 January 2009).

⁸⁹ Gazprom has several times used intermediary companies like RosUkrEnergo when selling gas to FSU states. EuralTransGas was until 2004 responsible for selling gas to Ukraine, but was then replaced by RosUkrEnergo. RosUkrEnergo's role was strengthened in the new deal compared to its earlier role (Goldman 2008).

⁹⁰ The development of Ukraine's gas expenditures and transit revenues is seen in Figure 3 on the next page.

Figure 3: Graph Showing Difference in Value of Gas Imports and Gas Transit



Source: Russian Analytical Digest 20 January 2009.

Only six days after the agreement was reached, Ukraine’s government was dismissed in a no-confidence vote by the Ukrainian Parliament. The Ukrainian legislators accused the government for accepting a harmful deal for the country, and the dismissal further increased the political pressure on Yushchenko. The Ukrainian parliamentary elections in March 2006 also saw Viktor Yanukovich’s bloc victorious. Yanukovich subsequently became Ukrainian Prime Minister, and chose to slow down Ukraine’s integration with NATO (Koren and Bukkvoll 2007).

6.8.2 October 2007-March 2008

Another row between Gazprom and Ukraine occurred on 3 October 2007 when Gazprom threatened to reduce Ukraine’s gas supplies if an outstanding gas debt was not settled. The threat came as the votes were counted for the September 2007 parliamentary election where no clear winner emerged. Valery Golubev, Gazprom’s Deputy Chairman responsible for Russian gas sales to the CIS market, said in May 2007 that “If politicians make a decision to establish closer economic ties between our countries, this will guarantee lower gas prices. However, if the politicians decide to separate these ties, then the price of gas for Ukraine will be the same as for Germany” (RFE/RL 30 May 2007). The row was temporary settled on 9 October 2007 when Naftogaz cleared the \$2.2 billion debt by paying \$929 million in cash and

transferring 8.5 bcm of gas worth \$1.3 billion to Gazexport (RFE/RL 4 October 2007 and RFE/RL 11 October 2007).

The conflict resurfaced again in February 2008 when Gazprom once more threatened to cut Ukraine's gas supplies by 25 percent as of 3 March 2008 if Naftogaz did not settle a \$600 million debt incurred in 2008 (RFE/RL 11 February 2008). The supply threat dealt a fresh blow to the new Yushchenko-Tymoshenko bloc that formed government following the September 2007 election. The conflict appeared at first to be settled following an agreement between Vladimir Putin and Viktor Yushchenko in February 2008, but fell apart due to a disagreement over whether the gas debt had been settled or not⁹¹. Gazprom executed the threat on two consecutive days in March 2008 by cutting gas deliveries to the Ukrainian pipelines equivalent to Ukraine's domestic consumption. This prompted Naftogaz to warn Gazprom that it would rather siphon off gas from the pipelines than to cut off gas deliveries to the Ukrainian customers. The conflict was resolved on 5 March 2008 when Naftogaz agreed to pay the outstanding debt (RFE/RL 6 March 2008).

⁹¹ Naftogaz claimed it had settled its debt with RosUkrEnergo in full, which in turn was responsible for settling its debt with Gazprom.

Chapter 7: What Triggers Russian Energy Aggression?

7.1 Introduction

I have now presented chapter five and six, which focus on Russia's relationship with the seven countries and the 13 cases of Russian energy aggression respectively. We now know the context in which the 13 cases of Russian energy aggression took place, which combined with the information in chapter three and four will enable me to answer the research question of the thesis: *what triggers Russian energy aggression*. Based on the three different hypotheses outlined in chapter two, I will conduct a comparative analysis in order to see which of the three hypotheses that serves as the best explanation for what triggers Russian energy aggression. Each of the hypotheses will be dealt with separately, in which I will look for common explanatory factors, and I will summarise the main findings for each of the hypotheses as I proceed. In the cases where there are more than one explanatory variable, I will operate with primary and secondary explanatory variables.

Before I turn to the analysis, I would like to repeat the three hypotheses:

H₁: *Russian companies will exert energy aggression due to economic interests.*

H₂: *Russia will exert energy aggression towards countries that leave its sphere of influence.*

H₃: *Russia will seek to gain energy infrastructure by exerting energy aggression.*

7.2 H₁: Russian companies will exert energy aggression due to economic interests

7.2.1 Introduction

Russia's oil and gas exports are by far the most important source of income for the Russian state, and are the main reason behind Russia's economic revival during Vladimir Putin's presidency. Putin's presidency coincided with a very favourable oil price development (see Figure 1 on p. 31). This helped Putin reverse the negative economic development during the 1990s, and the Russian economy experienced a strong growth each year in his presidency (see Figure 2 on p. 32). While Russia benefited from oil and gas exports to the lucrative Western European market, Russia's closest neighbours in the CIS states were subsidised with a preferential gas price which deprived Gazprom and the Russian state for billions of dollars. Hence, when Gazprom in 2004 moved to end the CIS states' preferential gas price, few could disagree with Gazprom's argument that CIS customers should pay the same gas price as Western European countries. Gazprom increased prices have also led to an increased

indebtedness among Gazprom's customers, which in turn has resulted in difficulties settling their debts.

7.2.2 Debt Collection

The cases that show the greatest support to Russia exerting energy aggression due to economic interests are Gazprom's actions towards Belarus in August 2007 and Ukraine in October 2007-March 2008. Both issues have been debt related. Gazprom first threatened to cut Belarus' gas in August 2007 after Belarus had not settled its gas debt of \$456 million for 2007. The threat was not carried out as Belarus settled the debt. Ukraine was subject to energy aggression a month later, when Gazprom threatened to cut Ukraine's gas supply. Ukraine's gas price had increased 3.6 times between 2005 and 2008⁹², which alongside Naftogaz's low increase in transit revenues and loss of industrial consumers led the company into serious financial trouble. Naftogaz had in September 2007 amassed a debt to Gazprom of \$2.2 billion. After Gazprom threatened to cut Ukraine's gas supplies, Naftogaz settled the debt. Naftogaz's financial troubles increased with the higher gas price in 2008. Gazprom again threatened to halt Ukraine's gas supplies in February 2008 because of an unsettled debt of \$600 million for 2008. After an initial agreement between Vladimir Putin and Viktor Yushchenko was not signed, Gazprom cut Ukraine's gas supplies in March 2008. The conflict was solved two days later when Naftogaz settled the debt.

Several factors may explain Gazprom's debt settlement actions towards Belarus and Ukraine in 2007-2008. First of all, both countries had accepted Gazprom's gas price for 2007, and were contractually obliged to pay Gazprom for the gas supplies. When the debt was not settled, Gazprom had every right to take action. However, Gazprom might have taken a more moderate approach if the indebted countries had a better relationship with Russia. Second, due to Russia's strained relationship with Ukraine and Belarus' failure to reach an agreement on the union state, Gazprom had no incentives to show lenience towards the two countries' authorities. Nor had Gazprom's gas subsidies during the 1990s and 2000s provided the company any gains in the two countries. Third, Naftogaz became infamous during the 1990s and the beginning of the 2000s for not settling its gas debt. Naftogaz has also several times threatened to siphon off gas meant for Europe in case Gazprom cut Ukraine's gas supplies. Naftogaz threatened once more to siphon off gas in this dispute, and have in some cases also

⁹² Ukraine's gas price in 2005 was \$50 per tcm, which increased to \$95 per tcm in 2006, \$130 per tcm in 2007, and \$179.50 per tcm in 2008.

carried out the threat, such as in January 2006. By threatening Ukraine's gas supplies, Gazprom demonstrated to Naftogaz that it would not accept this practice in the future. Finally, if Gazprom had wanted to make a political statement regarding the debt issue, Gazprom's threat to cut Ukraine's supplies in October 2007 would have had greater effect if the threat had been issued *before* the September 2007 parliamentary election in Ukraine, and not shortly after.

7.2.3 RosUkrEnergo's Role in the Ukrainian Gas Trade

The Russian-Ukrainian gas crisis in January 2006 saw RosUkrEnergo become responsible for supplying Ukraine's gas. Vladimir Putin hailed the resolution of the conflict, and called the new relations between Ukraine and Gazprom as "transparent, market-based relations between partners" (President of Russia 4 January 2006). Ukraine is Gazprom's largest customer. Figure 3 (on p. 68) shows that the value of Ukraine's gas imports in 2006 was roughly \$5 billion, set to increase in the coming years due to Gazprom's higher gas price. The central question with regards to RosUkrEnergo is why the company was made responsible for Ukraine's gas supply, and why Gazprom allowed the company to skim the profits from the Ukrainian market? Gazprom only possesses 50 percent ownership in RosUkrEnergo, and RosUkrEnergo does not have any pipelines or gas supplies of its own, nor is it a transparent company. RosUkrEnergo received 20 percent (14.6 bcm) of Ukraine's gas imports as payment for its role as Ukraine's gas supplier. If it re-exported this gas to Western Europe, the company would earn \$2.6 billion from the gas export in 2006⁹³, and even more with higher gas prices. UkrGazEnergo, RosUkrEnergo's subsidiary company, was also made responsible for distributing gas to Ukraine's industrial users, which is the most lucrative part of the Ukrainian market⁹⁴. RosUkrEnergo's financial statements for 2006 and 2007 show a profit of \$785 million and \$795 million respectively (RosUkrEnergo 2007).

Gazprom's use of RosUkrEnergo as an intermediary company in its gas relations with Ukraine does not comply with Putin's statements in January 2006 that market-based relations were introduced between Gazprom and Ukraine, nor does it suggest that Gazprom's actions are guided by economic interests. Larsson argues that "Requiring RosUkrEnergo, a shadowy company with possible links to organised crime, to act as intermediary is scarcely market

⁹³ The sum is based on this calculation: \$246 per tcm (average European gas price in 2006)/\$95 per tcm (Ukraine's gas price) ≈ 2.6 (the ratio European/Ukrainian gas price). RosUkrEnergo's payment amounted to 20 percent of Ukraine's gas, worth \$1 billion priced at \$95 per tcm. \$1 billion $\times 2.6 = \$2.6$ billion (RAD 2009).

⁹⁴ While the Ukrainian state subsidises domestic consumers, industrial consumers have to pay full price.

practice (Larsson 2006: 218). Why would Gazprom use RosUkrEnergo as an intermediary in its gas trade with Ukraine if it sought to maximize its profits in Ukraine? Although Gazprom owns 50 percent of RosUkrEnergo, Gazprom has yet to explain why it has given away the other half of the company. Since Gazprom only possesses 50 percent ownership in RosUkrEnergo, Gazprom missed out on at least \$800 million in profits for 2006 and 2007. Lucas notes that “it is hard to argue that the interests of gas customers, or for that matter those of shareholders in Gazprom and taxpayers in Russia, are best served by secrecy about the company’s activities and business model” (Lucas 2009: 220). Several authors point to another possible reason behind RosUkrEnergo’s role in Ukraine. RosUkrEnergo’s questionable role is likely due to a continuation of corrupt business practises that have marked Russia’s Ukrainian gas trade, where the profit has been distributed among government officials in Russia and Ukraine, and company officials in Gazprom and Naftogaz (Baran 2007, Wallander 2007 and Woehrel 2008).

7.2.4 Differentiated Prices

Gazprom’s shift to market principles suggests equal prices for all gas customers, but this has not been the case. Despite Alexei Miller’s statement in December 2005 that Gazprom applies market principles “to all foreign partners without exception” (RFE/RL 12 December 2005), Gazprom has been selective in enforcing market principles. Miller noted at the same time that Belarus’ gas price for 2006 would be kept down because of negotiations between Russia and Belarus over the union state. While Belarus was allowed to continue to receive subsidised gas at \$46 per tcm in 2006, Ukraine paid \$230 per tcm for Russian gas deliveries. When questioned why market principles were applied to Ukraine’s 2006 gas price while Belarus was exempt, Alexander Medvedev answered that “It’s because Gazprom owns the transit pipeline across Belarus” (New York Times 26 December 2005). Belarus had earlier in 2005 recognized Gazprom’s ownership of the Yamal-Europe pipeline built in 2002. Although Belarus’ gas price increased to \$100 per tcm in 2007, this was substantially lower than Georgia’s gas price at \$230 per tcm. Simultaneously, while Gazprom has increased the gas price to FSU states, Gazprom has showed leniency towards Abkhazia, South Ossetia and Transnistria. Besides receiving heavily subsidised gas supplies from Gazprom, the three separatist regions have also been allowed to rack up large gas debts to Russia without being forced to pay, which contrasts Gazprom’s actions taken against Belarus and Ukraine in 2007-2008. This picture also differs from Gazprom’s actions against Georgia and Moldova, who have suffered from Russian energy aggression over unsettled price agreements.

There are also several cases where Gazprom officials have offered lower prices in return for energy infrastructure. Instead of being concerned with economic interests, applying market principles to the price negotiations has given Russia a strong leverage over concessions in other areas, such as gaining a stake in energy infrastructure in the inflicted countries. Gazprom offered Moldova in 2006 a gas price of \$160 per tcm, but the agreement set Moldova's gas price at \$110 per tcm after Moldova transferred a share in Moldovagaz to Gazprom. This was also the case in Belarus, where Gazprom promised *at least* a threefold increase in Belarus' gas price for 2007. A threefold increase would mean a minimum gas price of \$138 per tcm, but Belarus only ended up paying \$100 per tcm after the Belarusian authorities agreed to sell a 50 percent stake in BelTransGaz to Gazprom. Similarly, Gazprom officials have also offered Georgia and Ukraine lower gas prices in return for energy infrastructure. Gazprom's price differentiation, both in terms of offering different prices to different countries and lower gas prices in return for ownership in energy infrastructure, suggests economic interests does not explain Gazprom's actions. This view is also strengthened by several statements made by Russian officials. After Viktor Yushchenko election victory in December 2004, Russia's Foreign Minister Sergei Lavrov said Ukraine and Georgia could not rely on privileged economic relations with Russia if they sought EU and NATO membership (RFE/RL 4 January 2005). Moreover, Russia's Defence Minister Sergei Ivanov said in February 2006 that Georgia would pay a hefty price if they went ahead with a resolution which called for the revocation of Russia's peacekeeping missions in Abkhazia and South Ossetia. Ivanov warned that "without Russia, it will fail to deal with the persistent problems in the country relating energy issue" (Eurasia Insight 9 February 2006).

7.2.5 Diversion of Oil Shipments

Transneft cut Ventspils Nafta's oil supplies in 2002-2003 citing too high tariffs using the oil terminal. Transneft halted Ventspils Nafta's oil shipments gradually, which was completed by January 2003. Transneft opted instead to send the extra oil shipments to its own terminal in Primorsk, and stated it did not need Ventspils Nafta. Despite this, Transneft continued to show an interest in acquiring a stake in the company. Transneft even proposed to expand the pipeline to Ventspils Nafta if it had ownership in the company (RFE/RL 12 February 2003). Transneft's interest in Ventspils Nafta suggests the company had available oil supplies for Ventspils Nafta. The case of energy aggression also took place in a year where Transneft stated it would increase pipeline exports by 16 percent. Considering the alternative to exporting the oil was for it to be sold much cheaper on the Russian domestic market,

Transneft's actions suggest economic interests did not trigger the halt of oil shipments to Ventspils Nafta. This argument is supported by the Russian oil producers' stance on the issue, as they wrote a letter to the Russian Prime Minister Mikhail Kasyanov. The letter criticized Transneft's decision to halt the oil shipments to Ventspils Nafta, and even urged Kasyanov to increase oil shipments to Ventspils. After Kasyanov disregarded the letter, the Russian oil producers opted to export oil supplies through considerably more expensive river and railway options. The Russian oil producers' actions show Transneft had oil supplies available for export, but chose not to export it through the Ventspils terminal. The case of energy aggression towards Ventspils Nafta shows instead that Transneft wanted to acquire a stake in Ventspils Nafta, and disregarded economic interests while attempting to force Ventspils Nafta into doing so.

7.2.6 Summary

Despite Gazprom's claims that it has changed to market based gas relations with its customers, only two cases of Russian energy aggression support this claim. Furthermore, Transneft's case of energy aggression towards Ventspils Nafta does not seem to be based on economic interests. Although two of Gazprom's cases suggest economic interests triggered Russian energy aggression, the rest of Gazprom's cases paint a different picture. Gazprom's use of RosUkrEnergO as an intermediary company in its gas relations with Ukraine in January 2006 is likely due to corrupt practices by Russian and Ukrainian authorities, and not because of economic interests. RosUkrEnergO's role inflicted Gazprom a loss of at least \$800 million for 2006 and 2007. Gazprom's differentiated gas prices also suggest other motives for exerting energy aggression than economic interests. The biggest difference was seen in 2006, when Ukraine had to pay \$230 per tcm for Russian gas, while Belarus continued to receive heavily subsidised gas at \$46 per tcm. Gazprom has also offered lower gas prices in return for energy infrastructure, and have showed far greater leniency towards the separatist regions concerning gas prices and debt settlement. Transneft's actions towards Ventspils Nafta in 2002-2003 add further strength to the findings in the gas sector. Despite incurring economic losses on Russian oil producers, Transneft chose not to allow them to send oil to the Ventspils terminal. Transneft also expressed an interest in buying Ventspils Nafta, although Transneft argued earlier it did not have sufficient oil supplies to Ventspils Nafta. Both Transneft and Gazprom are what Vladimir Putin's calls 'national champions'. As I showed in chapter three, Putin argues that the national champions should promote state interests over profit maximization, which is evident in the cases I have analysed so far. Although some cases of

Russian energy aggression seem to be based on economic interests, most cases of Russian energy aggression *do not* seem to be triggered by economic interests; hence the strength of the hypotheses is weak.

7.3 H₂: Russia will exert energy aggression towards countries that leave its sphere of influence

7.3.1 Introduction

Boris Yeltsin's presidency saw Russia's international power dwindle; the Russian state was not able to assume the Soviet Union's position at the international stage, and FSU states sought allegiance with other powers, most noticeable from the West. Russia's NSC identifies the weakening of Russia's political, economic and military influence as a threat to Russia's national security, and Vladimir Putin's thesis proposes to use Russia's energy resources to advance the country's interests. Putin's first presidential period, as outlined in chapter three, was largely marked by the strengthening of the Russian state domestically. This is especially evident in Putin's strengthening of the power-vertical and the renationalisation of the oil and gas sector. The strengthening of the Russian state was largely accomplished by 2003, which combined with a surge in energy prices left Russia at a far better footing. Legvold notes that "This notable shift in fortunes, more than anything, corrected the great deficit in prior Russian foreign policy: a lack of self-confidence. By 2005, shortly into Putin's second term in office, the Russians developed a distinctly more assertive approach to the outside world." (2007: 10). Russia's assertive approach has been particularly visible in Russia's dealings with the FSU states, which by Putin is considered Russia's sphere of strategic interest.

7.3.2 The Colour Revolutions in Georgia and Ukraine

The coloured revolutions that took place in Georgia and Ukraine in 2003 and 2004 respectively changed the two countries' relationship with Russia dramatically. The Georgian Rose Revolution in 2003 brought Mikhail Saakashvili to power on a pro-Western platform which sought Georgian NATO and EU membership. The Orange Revolution in Ukraine in 2004 saw Viktor Yushchenko elected on a similar platform, with both countries seeking a closer relationship with the West while distancing themselves from Russia. Common for both were also the United States' financial and political support for their movements. Russia was already provoked by NATO's and the EU's enlargement in 2004, which brought the Baltic States and several former Warsaw pact countries into the organisations. Russia's hostility

towards the two organisations is shown in the NSC. The NSC considers the military strengthening of NATO, NATO's eastward expansion and possible establishment of foreign military bases and presence in neighbouring states, as a threat to Russia's national security. Furthermore, NATO's possible expansion into Georgia and Ukraine does not coincide with Russia's interest, as it would bring a perceived security threat into what Russia wants to be a good-neighbour belt along Russia's border.

NATO and the EU had already conducted the 2004 enlargement process when Yushchenko was elected president in 2004, and the thought of Georgia and Ukraine joining the two organisations was not acceptable to Russia. Rowe and Torjesen argue that "The 'colour revolutions' in Georgia, Ukraine and Kyrgyzstan in 2004 and 2005 further aggravated Russian concerns about outside encroachment, since the new leadership in Ukraine and Georgia (less so in Kyrgyzstan) sought to strengthen ties with Europe and the USA at the expense of Russia" (Rowe and Torjesen 2009: 16-17). Moreover, Rumer argues that Western support to the colour revolutions was "intended to further isolate and encircle Russia and deny it any influence it still has in an area where Russia's interests are far greater than those of the west" (Rumer 2007: 25). It is therefore likely that Russia, after experiencing Saakashvili's western-oriented approach in 2004, chose to interfere in the Ukrainian 2004 election in order to avoid something similar happening in Ukraine. Putin even warned the Ukrainian electorate that the Russian-Ukrainian relationship would depend on how the next Ukrainian leadership organised its policies towards Russia. Putin thus implicitly suggested that Ukraine's future relationship with Russia was contingent on that Viktor Yanukovich, Putin's preferred candidate, won the election. Russia's Foreign Minister Sergei Lavrov also warned Yushchenko that Ukraine's NATO aspirations would have consequences as Ukraine would not be able to rely on privileged economic relations with Russia.

The negotiations for Ukraine's gas price for 2006 were the first major opportunity for Russia's to punish Yushchenko's westward orientation. Gazprom had earlier stated that it would change to market based gas relations with its customers, and these negotiations were the first time it firmly attempted to enforce those principles. Gazprom offered Ukraine gas price at \$160 per tcm for 2006, more than three times the price Ukraine had paid in 2005. The offer was later changed to \$230 per tcm after the two parties failed to reach an agreement. Gazprom knew that Ukraine most likely would not be able to pay this price, and offered

Ukraine a lower gas price in return for energy infrastructure⁹⁵. The proposed gas price would have had severe repercussions for the Ukrainian economy. Ukraine is one of the most energy inefficient economies in the world, and the Ukrainian state subsidises the domestic gas consumption. Furthermore, Ukraine's heavy industry, which accounts for nearly half of Ukraine's export production, is dependent on cheap Russian gas. A substantially higher gas price for the industry would in turn lead to decreasing revenues from the industrial sector. For the Ukrainian electorate, for whom the foreign policy orientation was not the most important one during the 2004 presidential election, the gas conflict could have led to hostility towards Yushchenko's policies as they were seen hurting the economy (RFE/RL 3 January 2006). Since the two sides could not reach an agreement, Gazprom cut Ukraine's gas supplies on 1 January 2006.

The political dimension of the Russian-Ukrainian conflict is strengthened by Putin's heavy participation in the negotiations, as it was Putin who at the most important meetings made the proposals for settlement. Andrei Illarionov, Putin's former top economic advisor who resigned the week before the Russian-Ukrainian gas crisis, also points to the Kremlin's political interference. Illarionov said that Kremlin invoked market rates only after Ukraine expressed an interest in joining NATO and the EU. Illarionov also said that Kremlin had allowed Ukraine to continue to receive gas at \$50 per tcm in 2004 to back Kremlin's favoured presidential successor, Viktor Yanukovich (New York Times 3 January 2006). Furthermore, Andrei Kokoshin, chairman of the Duma committee for CIS affairs and Compatriot Relations, stated that "Russia has the right to demand that CIS countries pay new prices. We shouldn't be subsidising their economies, especially since some of them have announced their desire to integrate with European and North Atlantic structures" (Gromadzki and Kononczuk 2007 – italics added). The likelihood for Russia punishing Ukraine's westward orientation is further strengthened by the siloviki's influence in Putin's administration. The siloviki consider NATO and the United States as external security threats to Russia, and want to create a buffer zone of friendly states around Russia by increasing Russia's influence in the near abroad (Van Bladel 2008). The Russian authorities also attempted to blame Ukraine for the gas dispute, and hoped that Ukraine's reputation as a safe transit country would be hurt. Instead, the attempt backfired on Russia, as the dispute was seen as an attempt to punish Ukraine's

⁹⁵ I will return to this later in section 7.4 as a secondary explanation for Russia's energy aggression towards Ukraine.

westward orientation, which also tainted Russia's reputation as a stable gas supplier as several European customers experienced a drop in their gas deliveries.

The settlement of the dispute on 4 January 2006 was beneficial for Gazprom. Gazprom managed to make RosUkrEnergo responsible for Ukraine's gas supplies, and Gazprom was set to receive \$230 per tcm for its gas sold to the company. Gazprom also managed to limit the increase in Ukraine's transit fee, and locked the transit fee from negotiations until 2010. Stern argues that although Gazprom's increased gas pressure was felt throughout the CIS, and not only in Ukraine, he states that "Had Ukraine chosen to maintain a closer political relationship with Russia, there is no doubt that it could have continued to pay lower gas prices at least for a period of time." (Stern 2006: 13). Besides punishing Yushchenko for his pro-Western orientation, the gas crisis also served to undermine Yushchenko's political support before the March 2006 parliamentary election. Amidst the parliamentary election campaign, the Ukrainian Parliament voted to dismiss Yushchenko's government on 10 January 2006 on the basis of a no-confidence resolution on the new gas deal. The parliament labelled the gas deal as a threat to Ukraine's national security. It particularly criticized the Ukrainian government for allowing the unknown entity RosUkrEnergo to become the monopolist supplier of Ukrainian gas. Although the Ukrainian Parliament probably would have moved to dismiss the government regardless of the gas deal, the resolution did anyhow serve to undermine Yushchenko's bloc's possibilities in the forthcoming election (RFE/RL 11 January 2006)⁹⁶. The March 2006 election saw Viktor Yanukovich's bloc emerge as the winner on a pro-Russian platform, and Yanukovich's tenure as Ukrainian Prime Minister saw Ukraine slow down its integration with NATO.

A similar event unfolded in Georgia in November 2006, when Gazprom threatened to cut Georgia's gas supplies if she did not accept Gazprom's offer for a new gas price for 2007 at \$235 per tcm. \$235 per tcm was the same price offered to Gazprom's European customers, and more than double the price Georgia had paid in 2006. Comparatively, Belarus' gas price for 2007 was only \$100 per tcm, while Moldova paid \$160 per tcm in 2007. At the same time as Gazprom doubled Georgia's gas price, Gazprom launched the construction of an unprofitable pipeline designed to carry gas to South Ossetia (RFE/RL 6 November 2006).

⁹⁶ Yushchenko came to power in 2004 with support from Yulia Timoshenko, and she became Ukrainian Prime Minister after the election. However, their political relationship soon deteriorated, and Yushchenko's dismissed Timoshenko's government in September 2005. The March 2006 election represented a chance for Timoshenko's bloc to strengthen their support at the expense of Yushchenko's bloc (Nygren 2008).

Gazprom never executed the threat as Georgia accepted Gazprom's offer. As outlined above, Georgia and Ukraine share many similar characteristics in its pro-Western approach. Moreover, Georgia had also received military support from the United States. Russia was already critical of the United States' role in the colour revolutions, and was worried that the United States' military presence in Central Asia could pose a threat to Russian influence in FSU states⁹⁷ (Rumer 2007). Putin noted in his speech at the Munich Conference that the United States has "overstepped its borders in every way. This is visible in the economic, political, cultural and educational policies it imposes on other nations" (President of Russia 10 February 2007). Although Russia's relationship with Georgia had been strained throughout Mikhail Saakashvili's presidency, their relationship deteriorated further in 2006. The Georgian Parliament approved in February 2006 a resolution that called for an end to the Russian peacekeeping missions in Abkhazia and South Ossetia. Russia's Defence Minister Sergei Lavrov responded to the resolution by hinting that Georgia could suffer a hefty economic price if the Parliament went ahead with the resolution. Lavrov also said that "The Georgian leadership understands very well that without Russia, it will fail to deal with persistent problems in the country relating to energy issues" (Eurasia Insight 9 February 2006). Georgia had also taken a significant step towards joining NATO in 2006 following NATO's offer of Intensified Dialogue in September 2006, only two months before Gazprom threatened to cut Georgia's gas supplies. The relationship between Russia and Georgia hit rock bottom less than a week later when Georgia arrested four Russian military officers accused of espionage, after which Russia called back the Russian ambassador in Georgia and implemented an air, sea and mail blockade on Georgia (Nygren 2008).

Gazprom's uncompromising offer to Georgia reflects the political relationship between Russia and Georgia. Gazprom's offer combined with Lavrov's statement in February 2006 and Russia's blockade of Georgia, suggests political motives triggered the case of Russian energy aggression in November 2006. If no agreement had been reached between Gazprom and Georgia, Gazprom would likely not have hesitated to cut Georgia's gas supplies. Although Georgia's pipelines also supply Russia's ally Armenia, Gazprom's cut of gas would not have had the same repercussions as Gazprom's supply cut to Ukraine. Georgia's acceptance of Gazprom's gas price was made easier by the knowledge that Azerbaijan would be able to supply two-thirds of Georgia's gas consumption from 2007. This meant that

⁹⁷ Although Vladimir Putin initially offered support to the United States' military presence because of the war in Afghanistan, Putin's view changed quickly as Russia's relationship with the United States deteriorated.

Georgia no longer would be completely dependent on Russian gas. Furthermore, Azerbaijan's reported offer to Georgia of a gas price of \$120 per tcm shows the extortionate character of Gazprom's gas price offer (Eurasia Daily Monitor 17 January 2007).

7.3.3 Russia's Support to Separatist Regions

Russia's peacekeeping forces in Abkhazia and South Ossetia in Georgia have also served as a foreign policy leverage for Russia. Blank notes that "Georgia's ability to enter NATO is clearly tied to its ability to resolve its conflicts peacefully, another reason for Russia to obstruct progress toward such resolution." (Blank 2008: 28). Russia's support to Abkhazia and South Ossetia resembles the Russian support to Transnistria, the Moldovan separatist region. Larsson argues that "Giving support to separatist regions against the central powers of sovereign states has been one of Moscow's best leverages against Moldova and Georgia" (2006: 219). Transnistria has since Moldova became independent in 1991 been a thorn in the Russian-Moldovan relationship. Moldova's president Vladimir Voronin has like Mikhail Saakashvili and Viktor Yushchenko expressed an interest in joining NATO and the EU. Vladimir Putin's relationship with Voronin has not been the best either. Putin's discontent with Voronin became particularly evident in March 2005 when Russian authorities aimed to topple Voronin by supporting pro-Russian parties in the parliamentary election.

Russia's main motivation behind the stationing of the peacekeeping forces in the separatist regions has been to use the Russian presence as foreign policy leverage. This is evident in a statement made by Vyacheslav Kovalenko in November 2005, which linked the settlement of the Transnistrian conflict with Moldova's positive attitude towards NATO. Russia's Foreign Minister Sergei Ivanov also cited Moldova's refusal to sign the Kozak memorandum as a reason for the deteriorating relationship between Russia and Moldova. Gazprom's gas supply cut to Moldova on 1 January 2006 resembles the Georgian and Ukrainian cases with respect to Russian hostility towards NATO. Kovalenko stated less than two months before the supply cut that Russia was concerned with Moldova's positive attitude towards NATO. Furthermore, Moldova and Russia had not come any closer to resolve the Transnistrian issue, but seemed instead to be drifting apart from each other on the issue. Since Russian authorities have openly admitted utilizing economic and political sanctions towards Moldova⁹⁸, it is reasonable to assume that Russia is willing to use gas as a form of leverage to gain

⁹⁸ The Russian Duma approved a legislation in February 2005, which called for visa regulations for Moldovan workers in Russia, charging market price for gas delivered to Moldova, and prohibitive taxation of Moldovan tobacco and wine products (Eurasia Daily Monitor 1 March 2005).

concessions from Moldova. Hence, Gazprom's offer of \$160 per tcm to Moldova, one of the poorest countries in Europe, must be considered as a political punishment of Moldova. This is also reflected in Kokoshin's statement cited earlier. Gazprom did not budge in the negotiations, and chose to cut Moldova's gas supplies for 15 days before reaching a settlement. Although Moldova only had to pay \$110 per tcm, the agreement was only valid for the first six months of 2006. Moldova had to pay \$160 per tcm for the second half of 2006, and also had to transfer a stake in Moldovagaz to Gazprom⁹⁹.

7.3.4 Lack of Progress in the Russian-Belarusian Relationship

The cases of Russian energy aggression towards Belarus in 2006-2007 took place in a context where the Russian-Belarusian relationship had gradually deteriorated. Russia and Belarus have since 1993 attempted to create the Russia-Belarus union state. While the union state experienced some initial progress under Boris Yeltsin's presidency, little progress had been made under Vladimir Putin's presidency. Putin prioritised the economic aspects of the union state, and took a firmer approach towards creating the union state on Russian terms. This is evident in Putin's proposal for Belarus to become a part of the Russian state, and his rejection of a joint central bank. The indefinite postponement of the union currency in 2006 marked the failure of Putin's economic ambitions with the union state. Russia's attitude towards Belarus changed in 2006. Shortly after the March 2006 presidential election, which saw Lukashenko re-elected to a third term as Belarusian president, Gazprom announced that Belarus would have to start paying market price for gas. The timing of Gazprom's announcement suggests more than economic interests. Why did Gazprom announce the price hike shortly after the election? Although Putin wanted to demonstrate that Russia sought to reduce Russia's subsidies in form of cheap gas supplies, it is likely that Putin waited until after the election in order to avoid the risk of a repetition of the coloured revolution in Georgia and Ukraine. Main argues that "Russia does not want to trigger a chain of events which would lead to instability in Belarus and possibly the replacement of the regime by one more favourably disposed towards the West than to Moscow. Russia has gained nothing from the earlier "coloured revolutions" and has no intention of starting one in an ally of such importance" (Main 2006: 10). Lukashenko's economic model is inextricably dependent on subsidised gas from Russia, hence Gazprom allowed Belarus to receive gas priced at \$46 per tcm for 2006. Lukashenko's

⁹⁹ I will return to this later as a secondary explanation for Russia's energy aggression towards Moldova in section 7.4.

economic model has also been heavily dependent on the re-export of refined Russian oil, which in 2004 amounted to 45.6 percent of Belarus' ten most exported products.

The first case of Russian energy aggression towards Belarus in 2006-2007 was initiated by Transneft in September 2006, which reduced Belarus' oil supplies by a quarter for the remainder of 2006. The supply cut was used as a coercion tactic to pressure Belarus into transferring Russia's entitled share of the profits generated by the re-export of Belarusian refined oil. No initial agreement was reached on the subject. The dispute worsened in January 2007, when Belarus imposed a transit charge on Russian oil exports through Belarusian territory as a response to a new Russian export duty on oil. Transneft again exerted energy aggression towards Belarus by reducing oil shipments to Belarus, and succeeded in forcing Belarus to revoke the transit charge. The second case of Russian energy aggression was executed by Gazprom. Gazprom increased the pressure on Belarus by threatening to cut Belarus' gas supplies as of 1 January 2007, after negotiations in 2006 had failed to offer an agreement on Belarus' gas price for 2007. Gazprom had announced it sought at least a threefold increase in Belarus' gas price for 2007, but emphasised several times that Belarus could negotiate a lower gas price if Gazprom received a stake in BelTransGaz. Gazprom and Belarus reached an agreement shortly before Gazprom's deadline on New Year's Eve, in which Gazprom agreed to lower Belarus' gas price in return for 50 percent ownership in BelTransGaz.

Russia's tougher stance towards Belarus in the oil sector is understandable from an economic point of view. Russia had since 2001 allowed Belarus' to reap 100 percent of the profit made from the export of refined Russian oil. However, why did Russia exert energy aggression in 2006-2007 to end this practice, and not earlier? A statement made by Putin in mid-January strengthens the likelihood that economic interests are not the primary explanation. Putin said at a Cabinet meeting that Russia would continue to heavily subsidise Belarus' economy, albeit at a lower rate. Russian subsidies for 2007 would amount to \$5.8 billion¹⁰⁰. One of the subsidies in 2007 came from Russia's decision to lower the export duty from \$180 per ton oil to \$53 per ton oil, less than a third of the initial price Belarus was forced upon.

That Belarus' export duty was lowered to \$53 per ton suggests the initial price of \$180 per ton was used as a warning of how much Belarus could risk paying if Lukashenko did not return

¹⁰⁰ Gas subsidies would amount to \$3.3 billion, while oil subsidies would amount to \$2.5 billion.

any favours to Putin. This also shows that economic interests are not the primary explanation behind Transneft's energy aggression. Instead, the most likely explanation is that Russia chose to subsidise Belarus' economy for as long as it was beneficial for Russia. Stent argues that "The political union moved no closer to realisation under Putin and appeared unlikely to progress further" (2008: 1101). After discussions over the union state and the union currency had failed to produce any progress, Putin wanted to state an example to Lukashenko. Putin punished Lukashenko politically by cutting Russia's subsidies to the Belarusian economy and exerted pressure on Lukashenko by cutting Russia's oil shipments to Belarus. Gazprom's gas dispute with Belarus was likely motivated by the same reason, as an increased gas price would lower the profitability of the Belarusian industry. By pressuring Lukashenko, Putin signalled to him that the Belarusian economy's well-being is dependent on a good relationship with Russia. Although Gazprom's threat to cut Belarus' gas supplies was politically motivated, the primary explanation behind Gazprom's energy aggression is best explained by Gazprom's interest in acquiring a stake in BelTransGaz. I will return to this in section 7.4.

Russia's increased pressure on Lukashenko's regime was made possible by Belarus' dependence on Russia. The Belarusian economy is, as I have noted earlier, heavily dependent on cheap Russian energy. Russia is also by far Belarus' largest trading partner, both in terms of exports and imports, and is far too vital for Belarus' economy for Lukashenko to turn away from Russia. Moreover, Lukashenko's reputation as 'the last dictator in Europe' left him with little room to manoeuvre when Putin decided to reduce Russia's subsidies. Unlike Mikhail Saakashvili and Viktor Yushchenko, who received strong support from Europe and the United States after Russia exerted energy aggression against the two countries, Lukashenko's international standing left him with no real allies. Furthermore, Belarus' importance as a transit country for Russian oil and gas did not provide her with the same kind of leverage against Russia as Ukraine's leverage. Hence, although Putin did not seek to completely alienate Belarus, Belarus' vulnerable standing allowed Putin to punish Lukashenko politically without fearing Belarusian repercussions in the form of 'defection' to the West.

7.3.5 The Bronze Soldier and the Russian Diaspora in Estonia

Russia's relationship with the Baltic States has been troublesome since the dissolution of the Soviet Union. The two largest issues have concerned the Baltic States' westward orientation, which culminated in NATO and EU membership in 2004 for all three countries, and the

Baltic States' treatment of the large Russian diaspora that is primarily found in Estonia and Latvia. Russia's NSC considers it as a matter of national security to secure the rights of Russians abroad. The emphasis on protecting the Russian diaspora is also evident in the FPC, which states that the relationship between Russia and other states will depend on the guarantees of the rights of Russian citizens abroad. Russia and the Baltic States have clashed several times over this issue, but none greater than the row concerning the relocation of the Bronze Soldier in Tallinn. Estonia experienced a halt in oil shipments only six days after the Estonian government authorised the relocation of the Bronze Soldier on 27 April 2007. The period between the relocation and the halt of oil shipments was marked by large demonstrations by ethnic Russians in Tallinn. The demonstrations turned violent, and left one person dead and more than 150 persons injured after the demonstrators clashed with Estonian anti-riot police¹⁰¹.

Estonia's oil supplies are imported by railway since no oil pipeline connects the country with Russia, and the Russian state-owned company Russian Railways is responsible for delivering Estonia's oil. Russian Railways' official reason for the halt of oil shipments to Estonia was maintenance work being carried out on the rail link to Estonia. However, there are several reasons to believe that this does not explain the halt of oil shipments. First of all, the message that maintenance work would be carried out was announced shortly after the Estonian government relocated the monument on 30 April 2006. As I will show in section 7.4, this was not the first time Russian companies has used this reason. Transneft used a similar explanation as the reason behind a halt of oil shipments to Lithuania in 2006. Common for both supply disruptions it that they only affected Estonia and Lithuania, while Russia's oil exports to Europe were not disrupted. Second, the halt of oil shipments was not the only supply disruption Estonia experienced, as Russian coal exports were halted at the same time citing a shortage of railway wagons. Third, like Gazprom and Transneft, Russian Railways is also a state-owned company that can be influenced by the state's priorities. There is no reason to believe that the Russian state is not willing to use Russian Railways like it uses Gazprom and Transneft to exert influence. Lastly, the Bronze Soldier row was not the first time Russia and Estonia has clashed over the treatment of the Russian diaspora in Estonia. Woehrel argues that "these actions fit a pattern in Russian foreign policy toward neighboring countries of interrupting energy, transportation, and other links under various pretexts to punish these countries for perceived anti-Russian behavior" (2007: 4). The likelihood that Russia exerted

¹⁰¹ The figures were grossly exaggerated in the Russian state-controlled media.

energy aggression on Estonia as a political punishment is further strengthened by a statement made by Russia's Transport Minister, Igor Levitin. He confirmed there were political reasons behind the dispute, and said that "business will develop where the situation is comfortable and profitable and where the moral and political climate are favorable" (U.S.-Russia Business Council 17 July 2007).

7.3.6 Summary

The analysis of H₂ has shown that five out of 13 cases of Russian energy aggression are primarily explained by this hypothesis. Furthermore, one additional case of Russian energy aggression is secondarily explained by H₂. The large number of cases that can be attributed to this hypotheses shows that Russian energy aggression is frequently used in Russia's foreign policy arsenal. Vladimir Putin's PhD dissertation argues that Russia should use the country's energy resources to advance the country's interest. Although the Russian FPC does not state directly that Russian energy aggression may be triggered by political motivations, it does state that "Russia must be prepared to utilize all its available economic levers and resources for upholding its national interests" (Foreign Policy Concept 2000). The FPC and NSC both identify NATO and the United States as a threat to Russia's security. The Georgian, Moldovan, and Ukrainian cases can be fully or partially explained by Russia's hostility towards NATO and the United States. Russia has also attempted to exploit the presence of Russian peacekeeping forces in Abkhazia, South Ossetia and Transnistria to gain concessions from Georgia and Moldova in other policy areas, such as their attitude towards NATO. The Belarusian case differs from the previously listed cases as Belarus has not sought a closer relationship with the West. Instead, the Belarusian case shows that Russia is willing to utilise energy aggression in order to punish a country's regime for failing to return any noticeable progress in important policy areas. Finally, the Estonian case demonstrates that the conditions of the large number of Russians abroad can trigger politically motivated energy aggression.

7.4 H₃: Russia will seek to gain energy infrastructure by exerting energy aggression

7.4.1 Introduction

The dissolution of the Soviet Union saw Russia become dependent on transit states for Russian oil and gas exports. Balmaceda (2008) argues that this dependency has led Russia into seeking ownership of pipelines in transit states in order to secure oil and gas exports. Ukraine's pipelines account for roughly 80 percent of Russia's gas exports, which combined

with Belarus' and Moldova's pipelines account for 95 percent of Russia's gas exports to Europe (Bruce 2005). The Russian economy is highly dependent on oil and gas exports, above all on the revenues generated from oil and gas exports to Europe. The Russian energy strategy recognizes this importance, and calls on "state and private entities to exert pressure on regional states to ease Russia's access to international markets" (Stulberg 2007: 98). The dissolution of the Soviet Union also left Russia with a lack of oil refineries and export possibilities besides pipelines. Lithuania was left with one of the largest oil refineries in Central and Eastern Europe, and Russia became dependent on oil terminals in the Baltic States for oil exports by tanker.

7.4.2 The Battle for BelTransGaz

The Belarusian pipeline operator BelTransGaz has been subject to interest from Gazprom several times during Vladimir Putin's presidency. Three cases of Russian energy aggression towards Belarus are closely linked to Gazprom's interest in BelTransGaz. However, while Gazprom has sought to acquire a stake in BelTransGaz, Lukashenko has repeatedly rebuffed Gazprom's interest in the company, citing security concerns behind Belarus' rejection to hand over such an important asset to foreign owners. The two first cases of Russian energy aggression towards Belarus in September 2002 and January-June 2004 respectively, took place before Gazprom had stated a change in policy towards market based gas relations. While the analysis so far has shown that Gazprom still employ differentiated gas prices, this practice was even more prevalent before 2004. Gazprom's agreement with Belarus in 2002 saw Belarus receiving gas priced at a Russian level on the condition that Gazprom received a stake in BelTransGaz through a joint venture ownership with Belarus. Although Gazprom's act of energy aggression towards Belarus took place only after Lukashenko had failed to privatise BelTransGaz, threatening Belarus' gas supplies shows the importance Gazprom ascribe to ownership and control of the company. Gazprom could also have resorted to other measures than threatening Belarus' gas supplies, such as increasing Belarus' gas price if Lukashenko did not keep his promise.

While the first case of Gazprom's energy aggression towards Belarus may be considered legit due to Lukashenko's broken promise, Gazprom's second act of energy aggression in 2004 paints a different picture. Gazprom announced in September 2003 that it was seeking an increase in Belarus' gas price for 2004, which came shortly after Gazprom had rejected to buy BelTransGaz on Belarus' terms. Belarus was in December told she could negotiate a lower

gas price contingent on Gazprom being allowed to buy a stake in BelTransGaz. Gazprom offered Belarus \$600 million for the company, which was rejected by Lukashenko who demanded \$5 billion. Later valuations have actually set BelTransGaz's value at \$5 billion, which shows the extortionate character of Gazprom's offer. By linking Belarus' gas price to Gazprom's valuation of BelTransGaz, Gazprom tried to squeeze Belarus: either Belarus would continue to receive subsidised gas and have to sell BelTransGaz at below market price, or Belarus would be left without gas. Since Gazprom and Belarus could not agree new terms for Belarus' gas price nor reach an agreement over BelTransGaz, Gazprom partially cut Belarus' gas supplies in January 2004, and increased the pressure by cutting Belarus' gas supplies completely in February. Itera and TransNafta were in the meantime allowed to export gas to Belarus. However, when their government-allocated export quota was almost reached, Belarus conceded to Gazprom on the price issue, but did not sell a stake in BelTransGaz. Instead, Belarus and Gazprom agreed to appoint an independent valuator to value BelTransGaz's value¹⁰².

Gazprom and Belarus were once more involved in a dispute over BelTransGaz in January 2007. As I have argued in section 7.3.4, this dispute also had a political side to it. However, I will argue that the primary explanation in this case is that Gazprom's long-standing interest in BelTransGaz triggered the case of energy aggression. When Gazprom upped the pressure on Lukashenko by announcing an increase in Belarus' gas price following his re-election in March 2006, Gazprom did so knowing Lukashenko's regime is dependent on cheap Russian gas to prosper. This knowledge provided Gazprom with a leverage in negotiations with Belarus over BelTransGaz. Gazprom initially announced it sought at least a threefold increase in Belarus' gas price, and later threatened with a fivefold increase which would bring Belarus' gas price up to European levels. However, like the 2004 case, Gazprom announced that Belarus could negotiate a lower gas price if Gazprom was allowed to buy a stake in BelTransGaz. After Gazprom threatened to cut Belarus' gas supplies as of 1 January 2007, Gazprom and Belarus reached an agreement on New Year's Eve 2006. The agreement set Belarus' gas price at \$100 per tcm, less than half the price Gazprom had threatened to impose

¹⁰² Deloitte & Touche was first appointed to estimate BelTransGaz's value, but it is unknown whether they completed the valuation. ABN Amro was later appointed and suggested four possible valuations, where the highest was \$5 billion. In light of the increased value of Gazprom's gas export, it is likely that ABN Amro's valuation of BelTransGaz at \$5 billion reflected the company's value (Goldman 2008).

on Belarus¹⁰³. Gazprom was in return allowed to acquire a stake in BelTransGaz, which by 2010 will be 50 percent owned by Gazprom. Kuzio argues that although Gazprom claimed it was not seeking control over BelTransGaz, this is “obviously a charade to camouflage a long-standing Russian strategic objective of seeking control of former Soviet pipelines transporting gas into central and Western Europe” (Kuzio 2007).

7.4.3 Oil Infrastructure in the Baltic States

All three of the Baltic States have been subject to Russian energy aggression. While Estonia was subject to a politically motivated case of Russian energy aggression in May 2007, three cases in Latvia and Lithuania suggest neither economic interests nor political motivations triggered those three cases. Baran (2007) argues that Russian companies’ failure to obtain Ventspils Nafta and Mazeikiu Nafta led to the cases of Russian energy aggression. The Latvian company Ventspils Nafta, which encompass the largest oil terminal in the Baltic States, was in 2002-2003 subject to energy aggression executed by Transneft. The first halt of shipments took place in April 2002, and Ventspils Nafta’s oil shipments had by January 2003 completely dried up. I have already argued in section 7.2.5 that economic interests do not explain Transneft’s halt of oil shipments to Ventspils Nafta. Several factors suggest Transneft halted the oil shipments in an attempt to gain ownership in Ventspils Nafta. Sergei Grigoriyev, Transneft’s vice president, stated in January 2003 that Transneft “would be ready to invest in an expansion if we had a stake in it” (New York Times 21 January 2003). Grigoriyev’s statement shows two things. First of all, it shows that Transneft had an interest in ownership of Ventspils Nafta. Second, the statement also shows that Transneft was interested in expanding Ventspils Nafta’s capacity, which logically implies that it had sufficient oil supplies available for such an expansion. This is further strengthened by Transneft’s announcement that it would increase oil pipeline exports by at least 16 percent in 2003. Moreover, the letter sent by the CEO’s of five major Russian oil companies, shows they needed Ventspils Nafta’s export capacity. By halting Ventspils Nafta’s oil shipments, Transneft put the company and the Latvian state in a financial squeeze. Mite argues that the halt of oil shipments decreased Ventspils Nafta’s value, which in turn could have made it easier for Transneft to buy the company (RFE/RL 10 January 2003). Although Ventspils Nafta could be supplied via other alternatives, they would have been a more expensive option than Russian pipeline deliveries.

¹⁰³ Belarus gas price at the time was \$46.68 per tcm. If Gazprom had imposed a fivefold increase in Belarus’ gas price, Belarus’ new gas price would be \$233.4 per tcm. Due to Belarus’ dependence on Russian gas and lack of diversification possibilities, Belarus had no other alternative than to accept Gazprom’s offer.

Chapter six shows that Mazeikiu Nafta has been subject to two cases of Russian energy aggression. The first case took place in 1999-2001¹⁰⁴, and the latter in 2005-2006. The 1999-2001 case was executed by Lukoil, which at the time was the government-assigned coordinator of Russian oil exports to the Baltic States. This case shows a direct connection between Lukoil's failure to acquire a stake in Mazeikiu Nafta and the halt of oil shipments to the company. Lukoil had expressed an interest in buying Mazeikiu Nafta in 1999, but cut the company's oil supplies shortly after Williams International had acquired a stake. It is likely that Lukoil tried to financially squeeze Mazeikiu Nafta and Williams International by disrupting the oil shipments. Although Lukoil was not a state-owned company like Transneft and Gazprom, the Russian state could have threatened to remove Lukoil's coordinator role if it objected to Lukoil's actions. Since the Russian state did not, and Lukoil were allowed to disrupt Mazeikiu Nafta's oil supplies nine times between 1999 and 2001, one can assume Lukoil's actions were supported by the Russian state.

The second case of Russian energy aggression towards Lithuania took place in the aftermath of the Russian state's crackdown on Yukos. Transneft first halted Mazeikiu Nafta's oil shipments in the second quarter of 2005, as Yukos was not allocated any export quota. Socor notes that Russia's actions seemed to prepare a takeover by the Russian government under the guise of collecting Yukos' debts while seeking to devalue Mazeikiu Nafta's stock (Eurasia Daily Monitor 25 July 2005)¹⁰⁵. I have already shown in section 6.5.2 that the Russian state made several attempts to prevent other companies from acquiring Mazeikiu Nafta. These attempts show the connection between the Russian state's interests and Russian oil companies' interests. After the Russian state's attempts proved unsuccessful, the Polish company PKN Orlen bought Yukos' 53.7 percent stake in Mazeikiu Nafta in May 2006. Only two months after Mazeikiu Nafta was bought by PKN Orlen, the company experienced a complete halt in oil shipments. Transneft made a statement which stated that an oil spill had taken place on 29 July 2006. That the Lithuanian authorities chose a Polish company was especially troublesome for Russia, as Russia's relationship with Poland has been very strained¹⁰⁶. It is noticeable that *the pipeline spill only affected oil exports to Lithuania, not Russia's oil exports to Europe*. Cornell and Nilsson argue that if a Russian company had been

¹⁰⁴ Although this case of Russian energy aggression started in 1999 while Yeltsin was still Russian president, the brunt number of Lukoil's shutdown occurred in Putin's presidency (Bugajski 2004).

¹⁰⁵ Larsson (2006) notes that Mazeikiu Nafta's share price dropped almost 23 percent following the Yukos-affair.

¹⁰⁶ Poland has never forgiven Russia for the Soviet atrocities during World War II. Furthermore, Russia has accused Poland for using its position in NATO and the EU to turn those organisations against Russia. Poland also supported the coloured revolutions in Georgia and Ukraine (Nygren 2008 and Lucas 2009).

allowed to acquire a stake in Mazeikiu Nafta in 2006, it is likely that “there would not have been a “technical malfunction” and that the pipeline would still be operational today” (Cornell and Nilsson 2008: 159). While normal pipeline repairs only take a few weeks to complete, Transneft said that the pipeline would have to be replaced entirely, and rejected Lithuania’s offer to examine the problem (Lucas 2009).

Transneft never commenced any work on the pipeline, which suggests Transneft was waiting for a Russian company to acquire a stake in Mazeikiu Nafta. PKN Orlen opted instead to import oil by tanker, which Lucas notes is only profitable when oil prices are high, and could lead to bankruptcy if prices fall. An escape clause in the contract PKN Orlen signed when they acquired Mazeikiu Nafta may explain Transneft’s decision to delay commencing any work on the pipeline. The escape clause provided PKN Orlen with an option to cancel the acquisition of Mazeikiu if the company’s market value dropped significantly before PKN had completed the takeover (New York Times 27 October 2006)¹⁰⁷. Ten months after the initial spill, Russia’s Industry and Energy Minister Viktor Khristenko ruled out repairing the pipeline. While pipelines to Europe have not experienced any technical spills with major consequences for their supplies, both Lithuania and Estonia have experienced serious supply disruptions as a result of alleged technical malfunction¹⁰⁸. Furthermore, Larsson notes that the three cases of Russian energy aggression towards Ventspils Nafta and Mazeikiu Nafta have been conducted in order to gain ownership in the companies: “On the most important occasions (Ventspils, Mazeikiu, Beltransgaz, and the trunk pipelines in Ukraine and Georgia) Russia has tried to acquire them by force” (Larsson 2006: 267).

7.4.4 The Georgian, Moldovan and Ukrainian Cases

I have already established in section 7.3 that the cases of Russian energy aggression towards Georgia, Moldova and Ukraine in 2006 are primarily explained by political motivations. However, I will also argue that they can be secondarily explained by Gazprom’s interest in acquiring pipeline infrastructure in the three countries. Common for all three cases is the connection between Gazprom’s offers of lower gas prices in return for a stake in the respective countries’ pipeline systems. The timing of the cases of energy aggression have also increased the pressure on the inflicted countries, as all three cases have occurred during winter

¹⁰⁷ The sale was completed on 15 December 2006 (New York Times 15 December 2006).

¹⁰⁸ Georgia has also experienced pipeline problems, after TNT explosions damaged two Russian gas pipelines to Georgia in January 2006. The repair took longer time than expected, and Georgia’s offer to send specialists to assist the pipeline repair was not accepted by Gazprom (Eurasia Insight 26 January 2006).

months when gas consumption is at its highest. Gazprom showed a particular interest in Ukraine's pipeline system during the negotiations with Ukraine in 2005, which can be explained by its importance for Gazprom's gas exports to Europe. I have already documented in chapter five that Gazprom has made several attempts to create a pipeline consortium that would make Gazprom one of the joint owners of Ukraine's pipeline system. This offer resurrected by Gazprom's CEO, Alexei Miller, who stated that Ukraine should surrender the pipeline to a consortium in order to avoid a fourfold gas price increase.

Gazprom attempted to pressure the three countries into allowing Gazprom to acquire energy infrastructure by demanding artificially high gas prices. While Gazprom sought to double Georgia's and Moldova's gas price, from \$110 per tcm to \$230 per tcm and \$80 per tcm to \$160 per tcm respectively, Gazprom's offer to Ukraine would have resulted in a fourfold increase in Ukraine's gas price. Gromadzki and Kononczuk argue that "Irrespective of certain differences in Gazprom's pricing policy towards Belarus, Ukraine and Moldova, the aim in each case is the same: to take control of their energy sectors" (Gromadzki and Kononczuk 2007: 26). Gazprom allowed Moldova a lower gas price for the first six months of 2006 in return for a stake in Moldovagaz. In the Georgian and Ukrainian cases, where Gazprom has not been successful, the higher gas price has weakened their economy, which in turn can make it easier for Gazprom to acquire energy infrastructure in the future. Vahtra notes that "the massive indebtedness has considerably weakened the political bargaining of many such countries against Russia" (2005: 16). This has particularly been evident in Ukraine, where Naftogaz was deprived of its most important source of income after the Russian-Ukrainian gas crisis in 2006.

7.4.5 Why Energy Infrastructure Is Important for Russia

The Russian energy strategy shows that the Russian state highlights the export capability of the Russian energy sector. Furthermore, the NSC considers a weakening of the economy as a threat to Russia's national security. I have already established in chapter three the Russian economy's dependency on oil and gas exports. Table 4 (on p. 33) shows the direct connection between higher oil prices and the growth in Russia's exports. Russia's trade balance increased 2.6 times between 2001 and 2007, and Russia's export of goods grew from \$101.9 billion in 2001 to \$354 billion in 2007. Russia's economy has in the same period become *more dependent on energy exports*, as the share of energy resources in exported goods has risen from 51.2 percent in 2001 to 61.5 percent in 2007. The Russian economy has in the same

period experienced a strong growth, with an annual average growth of 6.6 percent (Figure 2 on p. 32). However, while oil and gas exports are important for the Russian economy, nothing is more important for the Russian economy than *Russian oil and gas exports to Europe*. I will argue that this factor to a large extent can explain the findings in the preceding analysis.

Securing Russia's long-term export capability of oil and gas to Europe is more important for the Russian economy than promoting economic interests in its energy relations with the FSU states.

Russian efforts to secure its oil and gas exports are not only visible in Russian attempts to acquire energy infrastructure in FSU states. Section 3.5.5 shows that Russia has initiated several pipeline projects that aim to lessen Russia's dependency on existing transit countries. Overland argues that "the country where the pipeline is located will ultimately have the power to do things with the pipeline" (RFE/RL 10 January 2007). By diversifying Russia's export options, Russia decreases the existing transit countries importance for its oil and gas exports. Ukraine is Russia's greatest threat to export security, as it accounts for 80 percent of Gazprom's gas exports to Europe, and Nord Stream will lessen Russia's dependency on Ukraine. BTS-2 is an oil pipeline under construction that will Russian Transneft's dependency on oil exports through Belarus and the Baltic States. Transneft's CEO has called the pipeline an "absolutely unprofitable political project" (RIA Novosti 1 July 2008), but the pipeline has nevertheless been initiated. Russia has also attempted to avoid competition on the European gas market by trying to avoid the construction of the NABUCCO pipeline, and by limiting the size of the Iran-Armenia pipeline. Furthermore, the Russian Duma has allowed Gazprom and Transneft to form its own armed units to protect their pipelines. All these efforts to strengthen Russia's export capability and stronghold over Europe's gas imports show the importance of oil and gas exports to Europe for the Russian economy. This in turn clarifies and strengthens the findings presented in section 7.4. By attempting to acquire energy infrastructure in the FSU states, Russia has attempted to secure oil and gas exports to Europe. However, as these attempts have largely failed, Russia has instead sought to bypass the existing transit countries.

7.4.6 Summary

The dissolution of the Soviet Union saw Russia become dependent on independent countries for its oil and gas exports. Section 7.4.5 has shown that Russia's access to the European oil and gas markets are important for the Russian economy. The analysis of H₃ has shown that six out of 13 cases of Russian energy aggression are primarily explained by Russian attempts to

acquire energy infrastructure in the inflicted countries, while three more cases are secondarily explained by this motivation. The large number of cases that can be attributed to H₃ makes it the hypothesis that best explains Russian energy aggression. This is also reflected in the fact that six out of seven countries have been subject to Russian energy aggression because of the countries' energy infrastructure. Estonia is the single exception. However, this is comprehensible considering the lack of pipelines and other forms of energy infrastructure in the country. Out of the nine cases that are primarily or secondarily explained by Russian interest in energy infrastructure, six of them are concerned with Russian interest in gas pipelines. The remaining three cases concern oil infrastructure in Latvia and Lithuania.

Chapter 8: Concluding Remarks

8.1 Main Findings

Before I turn to the main findings in this thesis, I would like to remind the reader how the thesis has reached the main findings. The background for this thesis was to perform a multiple case study analysis of Russian energy aggression during Vladimir Putin's presidency in order to see what triggers such energy aggression. The thesis came to fruition due to a lack of literature on the subject, which is seen in the absence of already established theories that I could have employed in the analysis. Since the literature on the topic has largely focused on single case studies and multiple case studies on small samples of cases, this thesis will contribute by generating some preliminary hypotheses. Moreover, as I will return to next, the analysis has also enabled me to discuss the relative merit of the hypotheses. The purpose of discussing the relative merit is to show which of the hypotheses have the greatest explanatory power.

The comparative analysis has been based on the analysis of the three hypotheses presented in chapter two. The thesis has been hypothesis-generating in the sense that it has generated hypotheses that have served as the starting point for the multiple case study analysis. The three hypotheses are:

H₁: Russian companies will exert energy aggression due to economic interests.

H₂: Russia will exert energy aggression towards countries that leave its sphere of influence.

H₃: Russian companies will exert energy aggression in order to acquire energy infrastructure.

I have already summarised the main findings in the previous chapter as I progressed with regard to the analysis of the hypotheses, which makes a detailed summary unnecessary in this conclusion. The analysis of the 13 cases of Russian energy aggression during Vladimir Putin's presidency has shown that such energy aggression is not primarily explained by one variable. Table 7, which on p. 96 summarises all the cases in this thesis and what triggered them, shows that two hypotheses seem to offer the best explanations for what triggered Russian energy aggression. The hypothesis that receives the strongest support from the preceding comparative analysis of Russian energy aggression is H₃, which states that Russia will exert energy aggression in order to acquire energy infrastructure. Six out of the 13 cases of Russian energy aggression are primarily explained by Russian interest in energy infrastructure, while three more cases are secondarily explained by H₃. The relative merit of H₃ shows that nine out of

the 13 cases of Russian energy aggression are primarily or secondarily explained by this hypothesis.

Table 7: Summary of Cases of Russian Energy Aggression

Cases	Initiator	Oil/ gas	Economic interests	Sphere of influence	Infrastructure
Belarus: September 2002	Gazprom	Gas			x
Belarus: January 2004-June 2004	Gazprom	Gas			x
Belarus: January 2007	Gazprom	Gas		+	x
Belarus: September 2006-January 2007	Transneft	Oil		x	
Belarus: August 2007	Gazprom	Gas	x		
Estonia: May 2007	Russian Railways	Oil		x	
Latvia: 2002-2003	Transneft	Oil			x
Lithuania: 1999-2001	Lukoil	Oil			x
Lithuania: 2005-2006	Transneft	Oil			x
Georgia: November 2006	Gazprom	Gas		x	+
Moldova: January 2006	Gazprom	Gas		x	+
Ukraine: January 2006	Gazprom	Gas		x	+
Ukraine October: 2007-March 2008	Gazprom	Gas	x		

Legend:

x - primary explanation

+ - secondary explanation

The hypothesis with the second strongest explanatory power is H₂, which states that Russia will exert energy aggression towards countries that leave its sphere of influence. Five cases of Russian energy aggression are primarily explained by H₂, and one additional case is secondarily explained by this hypothesis. By adding the number of cases that are explained by H₂ and H₃, it shows that eleven out of 13 cases of Russian energy aggression are primarily explained by these two hypotheses. By comparison, the comparative analysis has also shown that only two cases of Russian energy aggression is primarily explained by H₁; hence economic interests is the poorest explanatory variable for Russian energy aggression. Thus, the relative merit of the hypotheses shows the following ranking order: H₃ has the greatest explanatory power, H₂ the second greatest explanatory power, while H₁ has the least explanatory power.

The preceding analysis has shown that the use of economic interests as a pretext for exerting energy aggression is weakened by Russian offers of concessions in the negotiations, such as the acquisition of energy infrastructure in return for a lower gas price. Moreover, using

RosUkrEnergo, a non-transparent company that deprived Gazprom of at least \$800 million in 2006-2007, is hardly protecting economic interests, nor is offering differentiated gas prices based on their relationship with Russia. Instead, I have argued that Russia is trying to protect its long-term economic interest by attempting to acquire energy infrastructure control in neighbouring countries. By securing control over oil and gas exports to Europe, Russia also protects the single greatest source of income for the Russian state.

8.2 Limitations of the Findings

After having established the main findings of this thesis, it is time to discuss the implications and limitations of these findings. First of all, the thesis is limited in time and space. As I have noted in chapter one, cases of Russian energy aggression have occurred both before and after Vladimir Putin's presidency, but this thesis has only focused on cases in Putin's presidency. Hence, while the findings in this thesis have a high validity with regard to cases of Russian energy aggression during Putin's presidency, the findings cannot be generalised to all cases of Russian energy aggression. The findings can only hint to possible explanatory variables that can be subjected to analysis beyond Putin's presidency. Moreover, since the findings are concerned with Russian cases of energy aggression, they cannot be generalised to cases of energy aggression exerted by other countries.

Second, the findings also show that none of the hypotheses can be dismissed. I discussed in the previous section the relative merit of the hypotheses and showed that nine out of the 13 cases of Russian energy aggression are primarily or secondarily explained by H₃. The analysis has also shown that H₃ does not explain four of the cases of Russian energy aggression.

Hence, although H₁ only explains two cases, the occurrence of those two cases shows that the analysis is not unambiguous with regards to what triggers Russian energy aggression. This is due to the thesis' research design since it suffers from multiple causation, which is a common problem for studies based on the method of agreement. Like a study based on the method of agreement, this thesis has analysed all cases of the outcome on the dependent variable¹⁰⁹.

Third, this thesis suffers from selection bias as the cases are only selected on the value of the dependent variable. The selection of cases is in this respect similar to the approach in the most different systems design (MDS), as no negative cases of Russian energy aggression have been analysed. We are as a result not capable of measuring the significance of the independent variables I have identified. The exclusion of negative cases is due to the

¹⁰⁹ I write all cases of Russian energy aggression. However, as I have noted earlier, this thesis does not include all cases in Vladimir Putin's presidency. Instead, it includes all cases that have been possible to analyse.

difficulty in defining what negative cases of Russian energy aggression would be. If negative cases were possible to include in the thesis, it would be fruitful to employ the most similar systems design, where it would be possible to compare positive and negative cases of Russian energy aggression.

Fourth, the hypotheses' relative merit is closely connected to the outlook of Putin's presidency and his view on energy policies. The thesis has analysed all possible cases of Russian energy aggression in Putin's presidency. In other words, the relative merit of the hypotheses that I have documented earlier in this chapter is only valid for Putin's presidency, and it may change if we look at cases beyond Putin's presidency. If the Russian regime became more liberal, such as if Medvedev's regime were to coincide with a more liberalised regime, it is likely that future versions of the current policy documents would reflect a more liberal approach with regards to Russia's national security, foreign policy and energy strategy. Moreover, it is also likely that the relative merit of the hypotheses would change completely, such as more cases of Russian energy aggression that are triggered by economic interests. Furthermore, if Russian companies were successful in acquiring energy infrastructure in the FSU states, either by force or by capitalist means, H₃'s relevance would disappear.

8.3 Where Do We Go From Here?

Vladimir Putin stepped down as Russian president in May 2008, and was followed by his handpicked successor Dmitry Medvedev. Medvedev has formerly served as first deputy Prime Minister of Russia, and was chairman of the board of directors in Gazprom. Although Medvedev now is the Russian president, Putin has continued as a major political force in Russian politics as Prime Minister in Medvedev's government. Kroutikhin argues that "Dmitry Medvedev is still just a nominal head of state; he has not yet amassed a significant group of influential allies of his own and has not yet achieved a high degree of personal control over the country, including the vital oil and gas industry." (2008: 24).

We are presently only 17 months into Medvedev's presidency. However, the end of Putin's tenure as Russian president has not led to a halt in cases of Russian energy aggression. January 2009 saw a repeat of the 2006 Russian-Ukrainian gas dispute. After a prolonged period of discussions, Gazprom cut Ukraine's gas supplies on 1 January 2009. As with the cases of Russian energy aggression in this thesis, the central question with regards to this case is what triggered it. The most obvious utility of this thesis is to see if the main findings in this thesis can contribute to the understanding of cases of Russian energy aggression beyond

Putin's presidency. Was the end of Putin's presidency a watershed in how Russia conducts her energy policy, or has his continued presence in Russian politics led to 'more of the same'?

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