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ANALYSES

China joins the Turkmen-Russian gas conflict

China's grant of a US\$4 billion loan to Turkmenistan led to its indirectly becoming engaged in the Russian-Turkmen gas conflict, which started this March and has resulted in Turkmenistan withholding supplies of its gas to Russia, among other consequences. The Chinese financial assistance has significantly reinforced the position of Turkmenistan (which has been deprived of a large part of incomes from gas exports) in its negotiations with Russia concerning conditions of renewing supplies of its gas. At the same time, China's engagement in Turkmenistan is another proof of intensifying Russian-Chinese rivalry in Central Asia.

The Russian-Turkmen gas conflict

The gas conflict between Russia and Turkmenistan has been escalating since March, when the two parties failed to sign an agreement on Gazprom's participation in the construction of the Turkmen internal East-West gas pipeline. A likely cause of the withdrawal was Kremlin's request for a guarantee that the route would be used to transport gas to Russia and not westwards and on to Europe (via the planned Trans-Caspian gas pipeline). The conflict reached its peak in April, when Gazprom reduced its intake of Turkmen gas by 90%, which in all likelihood resulted in the pipeline's failure and the cessation of supplies to Russia. Since that time, Turkmen gas has not been exported to Russia, and the parties have been negotiating conditions for renewing the supplies (Gazprom's demands include a reduction of the price or of supply volumes in the short term).

Since gas supplies to Russia stopped and Turkmenistan was consequently deprived of a significant part of its export incomes, Ashgabat has intensified its efforts to enhance co-operation with the West (as seen by the visits by Foreign Minister Rashid Meredov to Brussels on 3 June and Washington between 22 and 25 June) and China (the visit by Deputy Prime Minister Tachberdy Tagiev to China in early June). Ashgabat wants to strengthen its position in talks with Russia by demonstrating that it has alternative partners.

The Chinese loan

Turkmenistan has been most successful in developing relations with China. On 24 June, during the visit of the Chinese Deputy Prime Minister Li Keqiang in Ashgabat, the Turkmen gas corporation Turkmengaz and the Chinese State Development Bank signed a loan agreement for US\$4 billion. According to Turkmen government's promises, the money will be allocated to developing the largest Turkmen gas field, the South Yolotan. The conditions on which China has agreed to grant the loan have not been revealed; it cannot be ruled out that in exchange for the financial aid, Turkmenistan offered a gas supply guarantee or promised stakes in the gas field to Chinese companies.

An agreement on sale of 10 billion m³ of gas to China was also signed during the visit (in addition to the gas contract envisaging supplies of 30 billion m³ of gas signed in 2008; gas will flow via the currently built gas pipeline to China as early as the end of this year) and a number of executive agreements in connection with previously concluded gas deals. China has also agreed to triple the number of Turkmen students it accepts (90 people) and to supply computers to schools as part of a non-repayable grant.

The consequences

The loan agreement signed by Beijing and Ashgabat has significantly improved China's position in Central Asia, which is becoming a key economic partner, along with Russia, for the region's countries; so far in 2009, China has granted loans worth US\$10 billion to Kazakhstan, and has promised to invest US\$1 billion in Tajikistan. The Chinese engagement undermines the Kremlin's influence in Central Asia and may lead to a bitter clash between Russia and China. Russia seems determined to maintain its previous influence in the region, and its inability to present a financial and economic offer to Central Asian countries may make it to use other tools (for example, military force) to defend its position.

For the West, a stronger Chinese presence in Turkmenistan will make it more difficult to realise its plans to import large amounts of Turkmen gas to Europe, yet those plans have not failed completely. The Chinese loan granted for the development of the South Yolotan field in practice reduces the chance that European firms will obtain stakes in this field. It is also likely that in exchange for the loan, China has been given priority in receiving the gas from this source, which would call the need to build the East-West pipeline into question. Nevertheless, the gas fields located on the Caspian Sea shelf are still a reliable source of gas supplies to Europe.

Turkmenistan's increasing desire to co-operate with the West (which is especially evident over the past few months) will facilitate the realisation of the European plans. The diversification of gas sale routes and markets is a strategic goal for Ashgabat, which convinced it to give up its previous isolationist policy and to carry out plans to export gas to China. At the same time, Turkmenistan fears domination by both China and Russia alike, and will search for additional partners to counterbalance the influences of its powerful neighbours.

A tangible effect of the Chinese loan will be the reinforcement of Ashgabat's position in the ongoing talks with Gazprom on conditions of resuming gas supplies to Russia.

Aleksandra Jarosiewicz

EVENTS

A refinery in exchange for a gas field

On 19 June, the Russian oil corporation LUKoil signed an agreement under which it took over a 45% stake in the Dutch refinery TRN from the French energy corporation Total for US\$725 million. On 24 June, Total signed an initial agreement with the Russian gas company Novatek which provides for a takeover of a 49% share in the Russian gas field Termokarstovoye. This is an example of the Russian strategy of exchanging energy assets between Russian and foreign companies.

The Dutch refinery processes 7.9 million tons of oil annually, and is located in a region where demand for oil products is high. Its majority shareholder (55%) is Total. The French company bought the remaining shares from the previous holder, due to the latter's financial problems, and promptly resold them to LUKoil. This transaction has enabled Total to establish closer co-operation with Russian companies and, as a consequence, gain access to Russian gas (it already holds a 50% stake in the Kharyaga oil field in Siberia and a 25% stake in the company carrying out the first phase of the development of Shtokman gas field on the Barents Sea). The deal with Novatek (48% of the shares are held by the company's management, 19.4% by Gazprom and 18.2% by Gennady Timchenko) will allow the French company to take over a 49% stake in the field whose reserves reach 47.5 billion m³ of gas and 10 million tons of condensate. The estimated costs of the field's development are US\$900 million. The deal was supported by Prime Minister Vladimir Putin. The Russian government, which *de facto* controls the Russian energy sector, restricts foreign investors' access to the national raw materials, making it dependent (for example) on obtaining attractive assets in Europe in exchange. This model of co-operation with Russia has already been applied by Germany's BASF and Italy's ENI. Now Total has joined this group. <iwo>

Prime Minister Putin demands low prices and easily accessible loans

On 24 June, Prime Minister Vladimir Putin sharply criticised the management of certain supermarket chains which allegedly imposed too high margins on food. On 29 June, he also demanded that the management of the largest state-owned banks increase the number of available loans. These two actions prove that Putin wants to control the Russian economy personally during the crisis period; at the same time, they represent his propagandist attempt to put the blame for the problems on 'profiteers' and bankers.

Putin has decided to deal with price rises, which are problematic to the general public; the inflation rate has been high in Russia for years; according to forecasts, it will reach 13% in 2009. He unexpectedly accompanied a government delegation to one of Moscow's supermarkets, where in front of TV cameras he accused the store's management of imposing overly high margins

on dairy products and meat. Several days later, the Federal Anti-monopoly Service started price checks in supermarket chains. The government is to present a bill regulating trade and price setting to parliament within a week. Additionally, the Prime Minister met the management of the largest state-owned banks (Sberbank, Vneshtorgbank and other) and ordered them to increase the loan portfolio by 500 billion roubles (US\$16 billion) until October of this year. He threatened the managers that they could not go on holidays until this task has been fulfilled.

Both moves prove that Putin is trying to adopt a controlling policy towards the banking and trade sectors. It is not clear at all whether he succeeds (for example, despite the management's promises, the prices in the supermarket chain were not lowered after Putin's visit). In this context it is necessary to emphasise the propagandist aspect of Putin's declarations made in the spotlight of TV cameras, which are an attempt to place the responsibility for the crisis-related problems on others, and thus to reinforce his image as a 'knight in shining armour.' <JR>

Gazprom's General Meeting of Shareholders 2009

On 26 June, the annual General Meeting of Shareholders (GMS) of Gazprom approved the financial statement and production report of the company for 2008, which was another year of record-breaking export incomes. However, forecasts for 2009 and the next few years are not so optimistic. Lower incomes as a result of the crisis and the company's huge debt mean that it has no funds for investments. This has been demonstrated by promises of budget cuts for this purpose. These are accompanied by unofficial declarations that Gazprom's investment priorities will change, but these are only propaganda and may be understood as arguments against European plans to diversify gas supply sources.

Gazprom achieved very good results, mainly financial, in 2008 owing to the considerable boom on the oil market (gas prices change together with oil prices, with a delay of 6 to 9 months). The average price of oil sold in Europe was nearly US\$400 per 1000 m³ (compared to US\$270 in 2007). In effect, the gas export volume and incomes reached record-breaking levels. Although the impact of the crisis on Gazprom's condition was belittled in official statements during the GMS, the figures prove that the consequences of the crisis have been rather painful for the Russian monopolist. The main causes for this were the fall in oil prices entailing the reduction of gas prices (the average European price forecast for 2009 ranges between US\$260 and US\$280) and shrinking demand. The decrease in incomes and the company's huge debt (at the end of 2008, Gazprom group's debt was nearly US\$70 billion) will probably cause a reduction of the giant's investment plans. The unofficial declaration on Gazprom's change of investment priorities and the pushing through of the Far East Project (the development of East Siberian fields) at the expense of delaying the implementation of the key Yamal project seems to be a propaganda trick. Its likely intention is to suggest to European customers that Gazprom will develop its exports in the Asian direction. Gazprom seems to be trying to discourage the European Union's attempts to diversify its gas supply sources in this manner. <epa>

Ukrainian GDP breaks a pessimistic record

The State Statistics Committee of Ukraine reported on 30 June that the country's GDP had decreased by 20.3% in the first quarter of 2009 (in comparison with the first quarter of 2008), which was the worst result in Europe.

Considering the results for the last quarter of 2008, its value has shrunk by 22.9% over the past six months. The decrease was worst in the building sector (54.1%), industry (36.5%) and trade (18%). However, all sectors of the economy lost in value, with the exception of agriculture, which increased by 1.3%.

Considering this data, it seems impossible that the state budget can be implemented as presented, because its income was estimated on the basis of a governmental forecast envisaging a 0.4% growth of GDP. If the budgetary problems continue to be resolved by issuing state treasury bonds, which are acquired by the National Bank of Ukraine, this will cause growing inflation pressure and problems on financial markets which may be transferred to the real (non-financial) sector of the economy upon a further upsurge in the crisis. <AnG>

The International Monetary Fund increases support for Belarus

On 29 June, the Board of Directors of the IMF approved a decision to make US\$679 million available to Belarus as the second tranche of the loan of nearly US\$2.5 billion which it granted at the beginning of this year. Moreover, the credit line for Belarus has been increased by US\$1 billion, as a consequence of which the total value of the loan will reach nearly US\$3.5 billion. This means significant financial support for Minsk as it confronts the consequences of the global economic crisis, and at the same time a sign of approval for its previous anti-crisis policy.

The IMF's management stated that its decision resulted from a positive evaluation of the anti-crisis measures taken by the Belarusian government. Special attention was paid to compliance with budgetary discipline, the limitation of wage rises, the adoption of more restrictive monetary and loan policies, and flexible activity on the currency market. At the same time, they emphasised the need to take further actions to liberalise the economy, including increasing the independence of the central bank, ceasing central regulation of prices and wages, and making the Belarusian economy and legal system ready for large-scale privatisation. The IMF is likely to make the availability of the remaining tranches of the loan conditional on the fulfilment of these requirements.

The Fund's financial support is vital for Minsk, whose financial liquidity has improved as a result. This may also help the Belarusian government in its negotiations with Russia, which has been demanding the repayment of nearly US\$240 million of debt, which (in Moscow's opinion) has resulted from the payment of the lower price of US\$150 per 1000 m³ for the Russian gas between January – April 2009 instead of the US\$210 price which applied in those months. <kam>

Russian President visits Azerbaijan

The Russian President Dmitri Medvedev went on a one-day visit to Baku on 29 June. The main effect of the visit was the signature by both countries of a contract to export 500 million m³ of Azeri gas to Russia as part of the first phase of the Shah Deniz project, starting from 2010. The contract is a moderate success for Russia because it does not rule out export of Azeri gas to Europe as part of the second phase of the Shah Deniz project (nearly 14 billion m³), a plan which still has top priority in Azerbaijan's energy policy.

Presidents Dmitri Medvedev and Ilham Aliyev discussed such issues as energy co-operation, the Karabakh conflict and cross-border co-operation. The most important matter was the gas contract signed by the state-owned companies, Russia's Gazprom and the State Oil Company of Azerbaijan (SOCAR). The gas sold to Russia will account for nearly 10% of current Azeri gas exports. The supplies will go to Russian republic of Dagestan. For Russia, the importance of the contract is not limited to the context of its energy interests, but also has a symbolic meaning. Although the visit has not dealt with a number of sensitive issues in mutual relations (such as Russian weapon supplies to Armenia), the contract may be used by Moscow to demonstrate its correct relations with Azerbaijan against the background of its worsening relations with other CIS countries (such as the gas conflict with Turkmenistan, Russian-Belarusian tension, etc.). For Azerbaijan, the contract is essential in commercial terms. It can be seen as a form of pressure on Turkey, which has been blocking transit of Azeri gas to Europe and has not agreed to increase the price of the Azeri raw material. By signing this contract, Baku has also sent a message to European countries, urging them to engage more actively in resolving those issues. <mf>

Tension is rising in the Fergana Valley

On the night of 27 and 28 June, Kyrgyz secret services clashed with Islamic militants near the town of Uzgen in the Jalalabad district. This was the latest of several military incidents in the Fergana Valley over the past month. It cannot be ruled out that the situation in the region will deteriorate within the next few weeks.

Four militants were killed in the clashes. According to official Kyrgyz sources, at least one of them was a citizen of Uzbekistan. The militants were reportedly members of the Islamic Jihad Union (IJU), a terrorist organisation which until recently had its base on the Afghan-Pakistani frontier and is linked to the Islamic Movement of Uzbekistan. The IJU has been accused of launching the attack on the local militia headquarters in Khanabad, Uzbekistan and plotting the terrorist attacks in Andijan (26 May). One day later, unidentified perpetrators shot dead a Kyrgyz border guard. The clashes took place near near Uzgenem, which is believed to be one of the mainstays of radical Islam; it was also the scene of ethnically-motivated Uzbek-Kyrgyz massacres in the early 1990s. This was the second serious military incident in south Kyrgyzstan over the past week; clashes with Islamic militants had taken place on 23 June in the suburbs of Jalalabad. This may be proof of an attempt

to destabilise the situation in the Fergana Valley, which is divided between Uzbekistan, Kyrgyzstan and Tajikistan, by Islamic militants who originate from Central Asia and currently have their main base and logistical support in Afghanistan and Pakistan. If the situation deteriorates further, this may pose a risk not only to the internal stability of the region's countries but also to NATO's transport corridor to Afghanistan, which runs through Central Asian countries. <mf>

CES

The Centre for Eastern Studies

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