

## **German-Russian intergovernmental consultations – content dominated by form?**

Justyna Gotkowska

On 18-19 July the 13<sup>th</sup> German-Russian intergovernmental consultations were held in Hanover. A dozen or so ministers from each country participated in the consultations along with Chancellor Angela Merkel and President Dmitri Medvedev. From the Russian point of view the talks did not produce the expected, clear-cut political support for Russia's plans for expansion in the energy sector in Germany and the shift in Germany's position on liberalisation and the lifting of the visa regime between the EU and Russia. For Germany the consultations confirmed the crisis of the German concept of the "partnership for modernisation" with Russia. Co-operation with Russia is beginning to be regarded again as a "partnership for resources" above all, not only in terms of energy resources but also rare earth elements.

### **Consultations under the sign of talks on energy co-operation**

An unexpected change in Germany's energy strategy and an accelerated departure from nuclear energy opened up opportunities for Russian companies to strengthen their position of gas suppliers and enter the German electricity market. For Germany will be forced not only to speed up the development of renewable sources of energy but also to gain an additional approximately 10 GW of power from conventional power plants (mainly gas-fuelled plants) at least until 2022. The financial problems of German companies linked with this are compounded by unfavourable gas prices resulting from long-term contracts with Gazprom. Therefore German companies have started discussing an intensification of co-operation with their Russian partners, which would guarantee lower gas prices enabling them to maintain profitability of gas-fuelled power plants, both those currently operating and those planned. RWE and EnBW are counting on co-operation which would ensure the influx of capital and make possible the construction of new gas and coal-fuelled plants in Germany (Appendix 1).

During the consultations the Russian party wished to demonstrate their readiness to increase gas supplies to its most important European partner in the energy sector (and came up with the offer of building a third branch of Nord Stream). Russia was also interested in winning political support from the German government for Gazprom and other Russian companies which want to enter the electricity market in Germany. However, Russian expectations were not met during the consultations. The German government approached them with caution, not indicating Russia as the priority partner in the process of

its accelerated departure from nuclear energy. Furthermore, Chancellor Merkel expressed her scepticism at Gazprom's estimates which predicted an increase of 30-35% in Germany's demand for gas as well as at Russian offers to extend Nord Stream. Nevertheless, the talks between German and Russian companies about strengthening energy co-operation are still underway and it is highly probable that joint ventures will be established. It however remains an open question what rules will be applied to them.

### **Partnership for modernisation overshadowed by partnership for resources?**

The Partnership for Modernisation between Germany and Russia was one of the announced topics of the consultations. From Berlin's point of view the initiative created in 2008 has not fulfilled Germany's expectations. German politicians have not been alone in openly criticising the deficits of Russia's "modernisation" - they have been joined even by representatives of German business grouped together in Germany's Committee on Eastern European Economic Relations (Ostausschuss). These criticisms point to: the lack of an effective implementation of reforms in economic and administrative law, corruption and bureaucracy, the lack of a friendly climate for investments for small and medium-sized entities, the lack of the independence of the judiciary and no protection of copyrights. From the Russian perspective the "partnership for modernisation" has at least partly met Russia's expectations - German technologies have been transferred to a certain extent and this without the necessity to improve Russia's standards of democracy and the rule of law. It seems that Germany has given up on its expectations of Russia's genuine "modernisation" in the foreseeable future - extending to the reform of the administration and the legal system. This however does not mean a stagnation on trade exchanges and German investments in Russia. Trade will continue to develop. However, in Russia investments from large German companies will prevail, not from small and medium-sized ones which are the driving force behind the German economy but which need a friendly and stable investment climate for their expansion. In case of the consultations in Hanover even contracts with large German companies were not signed. The only more substantial deal was the contract of German Continental AG with the Kaluga Oblast regarding the construction of a car tyre plant (Appendix 2).

With regard to the lack of progress (for Germany) in the "partnership for modernisation" this topic is starting to be pushed out by the theme of the "partnership for resources" in Germany - not only in the area of energy resources but also of rare earth elements. After the national strategy for resources was adopted in autumn 2010, the German government intensified efforts to guarantee German companies access to rare earth elements indispensable in manufacturing high-tech products. Talks are being held with Kazakhstan and Mongolia, as well as with other countries. It appears that for Germany, Russia is another potential "resources partner" in this area. This topic is being heavily promoted by German economic circles and has been discussed in the "Economy" working group under the Petersburg Dialogue - an annual forum gathering business representatives, which accompanies the consultations. Germany is interested not only in an increase in imports of Russian rare earth elements to Germany but also in joint German-Russian investments in Russia in the exploitation and processing of these resources.

## The contentious issue – visas

Russia treats the issue of lifting the visa regime as a priority in its political talks but at the same time does not feel responsible for the introduction of the internal reforms the EU sees as necessary. Germany is one of the countries in Brussels which hold a very cautious position on the liberalisation and lifting of the visa regime due to the great importance of internal security in Germany. Germany also uses strict requirements towards Russian citizens who are applying for a German visa. However, German business has for a long time been championing the liberalisation of the visa regime with Russia. It seems that the German government is ready to soften its position in Brussels on this issue and to facilitate the process of obtaining visas in bilateral relations with Russia – above all for Russian entrepreneurs. During the consultations Chancellor Angela Merkel announced that steps would be taken in this matter.

## The conclusions

1. Germany displays caution in addressing the question of increasing the share of Russia's gas in imports to Germany (although it does not rule it out) and the issue of Russian companies entering the German electricity market. The consultations did not bring unequivocal political support from Chancellor Merkel for the plans of expansion for Russian companies in Germany, which was expected by Russia. Although before the talks the information about Gazprom's possible entry to the market had been met with a positive response from German Minister of Economy Philipp Roesler (FDP). The talks between German and Russian companies are underway and their final outcome remains an open question.
2. The Russian party did not succeed in winning a substantial change in Germany's position on the liberalisation and the scrapping of the visa regime between the EU and Russia but only a promise to introduce facilitating measures in bilateral relations.
3. From Germany's perspective the consultations confirmed the crisis of the German-Russian "partnership for modernisation". The partnership has not led to the realisation of German expectations for reforms facilitating the functioning of small and medium-sized entities on the Russian market to be introduced. However, German business is starting the promotion of the subject of a German-Russian "partnership for resources" which would extend to both energy resources and rare earth elements.

Justyna Gotkowska, co-operation: Russian team

## Appendix 1

The German-Russian talks about strengthening co-operation in the energy sector

**RWE.** Before the consultations it was announced that a memorandum of strategic partnership between RWE and Gazprom had been signed (14 July). It may result in the

establishment of a joint venture which would deal with the exploitation of the existing gas and coal-fuelled power plants and the construction of new ones in Germany, the UK and the Benelux countries. It does not rule out that Gazprom will take over shares in RWE.

**EnBW.** A week before the intergovernmental consultations, speculations appeared in the German press about co-operation between the third largest (after E.ON and RWE) German energy company – EnBW with Novatek – the second (after Gazprom) largest gas producer in Russia. EnBW would sell off up to 25% of its shares in the German company VNG to Novatek. EnBW would place the remaining of 48% of its shares in VNG in a joint venture with Novatek. In exchange for this, EnBW is counting on lower and competitive prices of Russian gas. VNG (in which also Gazprom holds 10.5% of shares) is the largest gas importer in Germany, after E.ON Ruhrgas, RWE Energy and Wingas (50% BASF, 50% Gazprom), with a dominant position in states of eastern Germany. It also deals with the trade, transport and storage of gas in Germany and other countries, including Poland, the Czech Republic and Slovakia.

**E.ON.** Talks on further co-operation are being held also between E.ON and Gazprom. E.ON is demanding lower gas prices and is renegotiating its gas contracts with Gazprom. The company's head does not rule out co-operation with Gazprom for individual projects but claims that E.ON – unlike other companies – is not looking for a strategic partner in Russia.

## Appendix 2

During the consultations 15 documents were signed, including:

### 1. Intergovernmental agreements and joint declarations:

- a joint declaration on the intention to organise a Year of Russia in Germany and a Year of Germany in Russia in 2012-2013
- a joint declaration from the Ministries of Justice and Internal Affairs about legal co-operation under the partnership for modernisation
- a joint declaration about co-operation between the Ministries of Finance in the form of the Russian-German finance dialogue.

### 2. Economic contracts and agreements:

- the agreement on the construction of a tyre plant (the local administration of the Kaluga Oblast, Continental AG)
- a memorandum of understanding (MoU) regarding the possibility of establishing a fund supporting small and medium-sized entities in Russia (Vneshekonombank, Kreditanstalt für Wiederaufbau);
- a MoU in the area of modernisation of electricity networks (Siemens, MRSK Holding, the German-Russian energy agency – Rudea, the German energy agency Dena)
- a MoU regarding the project to construct and exploit a medium-voltage electricity power plant in Russia (Siemens, the German energy agency Dena, InterRAO, the German-Russian energy agency – Rudea).

