

New Hungarian-Russian gas agreement

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On 27 September, representatives of the Hungarian state-owned energy company MVM and the Russian company Gazprom Export (a subsidiary of Gazprom) signed two new, long-term gas contracts in Budapest. The Hungarian Minister of Foreign Affairs and Trade, Péter Szijjártó, took part in the ceremony. According to the information he provided, the contracts will be valid for 15 years, with the option to renegotiate them after 10 years (including reducing the volume of gas supplies). The contracts provide for total deliveries of 4.5 bcm of gas per year. The pricing and its formula were not disclosed, although Szijjártó emphasised that it would be “more favourable than in the previous contract” in force in 1996–2015 (since it expired, Hungary has been buying the gas which was not used during the term of the contract). In turn, the CEO of Gazprom emphasised that the contracts are important with regard to the diversification of Russian gas export routes. The gas is to be collected at two points: 3.5 bcm annually at the border with Serbia (via TurkStream and the newly opened Hungarian-Serbian connection) and 1 bcm annually at the border with Austria.

The new contracts have been criticised by the Ukrainian foreign ministry on the grounds that the supply route bypasses the country's territory (so far, around 80% of gas to Hungary has been supplied via this route). In protest, Kyiv withdrew its representative from the Ukrainian-Hungarian intergovernmental economic commission which should have been held on 29–30 September in Budapest.

Commentary

- The negotiation of these new contracts between Hungary and Russia has been typical of energy cooperation between the two countries, which generally takes place at a high political level. On the Hungarian side, the negotiations were conducted not by representatives of the gas purchasing company, but by the Ministry of Foreign Affairs and Trade. The political arrangements were made first (Szijjártó gave the details of them in June and August), and only then were the trade agreements signed. The gas contracts probably also form part of the Hungarian-Russian package deals; a modification of the agreement on a loan for Rosatom to build two new units at the Paks nuclear power plant was also negotiated in parallel with the contracts. In April Russia agreed to postpone the start of the repayment of the loan for a further five years (starting in 2031), as this investment has already been postponed for several years.
- The key change in the current contracts, compared to the previous one, is the change in the supply route for Russian gas to Hungary: most of the gas will be collected on the border with Serbia, and not Ukraine (the smaller part will continue to be collected at the

Austrian border; this gas may arrive via Ukraine or via the Nord Stream gas pipeline). This is the culmination of the many years of efforts Russia has undertaken to bypass Ukraine when supplying Hungary and the south-eastern European countries. Originally, the South Stream project was to have enabled this; then, after abandoning it Russia embarked upon the construction of the TurkStream gas pipeline and system connections between Turkey, Bulgaria, Serbia and Hungary. At the start of July, the physical connection with the gas networks of Hungary and Serbia was opened; its target annual capacity in direction to Hungary is 8.5 bcm. The infrastructure on the Hungarian side will need to be expanded for the gas to reach its destination; the missing 15-kilometre section should be completed before the end of October.

- In a situation where neither the pricing formula nor the scope of flexibility regarding the amount of gas purchased from Russia are known, it is difficult to fully assess how much both parties will benefit from the new contract. Budapest has been trying to postpone the signing of a new long-term contract since 2015, in the hope of strengthening its negotiating position thanks to the diversification of gas supply routes. However, it has been only partially successful in this regard: Hungary does have access to alternative supplies from the LNG terminal in Croatia, but its hope of obtaining gas from Black Sea deposits from Romania has not yet materialised. It is known from press reports that the Hungarian side demanded a more favourable price as compensation for losing the revenues from part of the Russian gas transit after the launch of TurkStream (deliveries to Serbia and Bosnia & Herzegovina are currently carried out via the Black Sea route, and not via Hungary), as well as for the costly investments Budapest has carried out in constructing a link with Serbia and expanding the national transmission network. However, due to the current market conditions (record high gas prices and limited availability of LNG), Hungary has had limited opportunities to negotiate more favourable supply prices.
- The issue of the gas prices is also of particular political importance for the Hungarian side. Hungary is a country with a high level of gas consumption, and around 95% of its gas imports come from Russia (8.6 bcm in 2020). The government of Viktor Orbán has highlighted reductions in retail energy prices (including gas) over the last decade as one of its greatest achievements. This was of particular importance before the parliamentary elections in 2014, when the Fidesz campaign presented these reductions as the government's greatest success. Since then, every electricity or gas consumer in Hungary can see how much is being saved on their invoices.
- For Russia, it seems convenient to finalise the negotiations with Hungary now mainly due to the completion of TurkStream and the interconnections on the Balkan route, as these will enable gas to be sent via this route to Hungary; also, the fact that gas prices are currently high is helpful. In conditions where gas exchanges and short-term trading in gas are increasingly important, each long-term contract Gazprom concludes contributes towards maintaining its position on the key European sales market. Instead of the option to renegotiate the contract every five years which Hungary had been asking for, it was agreed that the terms could only be altered after 10 years. In addition, each contract to supply gas to European customers through the newly built gas pipelines (TurkStream, Nord Stream 2) reduces Russia's transit dependence on Ukraine, while at the same time

strengthening Moscow's negotiating position in any talks it may hold with Kyiv on extending the Russian-Ukrainian transit agreement, which is currently in force until 2024. Another political benefit for Russia is the stoking of tensions between Kyiv and Budapest. If individual EU countries agree to Russia redirecting its gas supply routes to new transit lines, this may make it difficult to build a wider coalition to maintain a transit role for Ukraine after 2024.

Map. TurkStream and the gas infrastructure in Central and South-Eastern Europe



Sources: ENTSOG, gas system operators of individual countries.