



ΠΑΝΕΠΙΣΤΗΜΙΟ ΠΕΙΡΑΙΩΣ

UNIVERSITY OF PIRAEUS

Energy and Environmental Policy Laboratory

Pipeline Geopolitics in Eurasia

The new gas projects linking Russia and China

Dr. Vassilios Sitaras

Working Paper 1

May 2016

The contents of this paper are the author's sole responsibility. They do not necessarily represent the views of the Energy and Environmental Policy Laboratory of the University of Piraeus, of any of the Laboratory's members, and/or of the author's other affiliations.

Copyright © 2016

Energy and Environmental Policy Laboratory at the University of Piraeus

This publication may be reproduced in part for educational or non-profit purposes without special permission from the copyright holder, provided acknowledgment of the source is made. No use of this publication may be made for resale or for any other commercial purpose whatsoever without prior permission in writing from the Energy and Environmental Policy Laboratory.

ISBN

xxxx

Preface

This paper, originally submitted as a Post-Doc Thesis to the University of Peloponnesus in April 2016, examines a high point in energy geopolitics, and, in particular, pipeline diplomacy. It's a very ambitious endeavor (actually a double one...) that only a real energy superpower, like modern Russia, can afford. Two brand-new gas pipelines, namely *Altai* and *Power of Siberia*, demonstrate President Putin's pivot towards China.

While the analysis recognizes the strong rationale behind this audacious move and the enormous consequences of a potential Russia-China "axis" for the status quo of international relations, it concludes that there are still significant challenges to be addressed, especially with oil and gas prices being as low as today (spring 2016). Competition from new LNG projects worldwide and also from much cheaper pipeline gas produced in Turkmenistan -ironically a country still regarded by Russia as "*Near Abroad*"- threatens to derail President Putin's plans.

To sum up, the prospects of Russia's Eastern projects appear rather dubious, at least for the short-to-medium term period. The *Altai* project, which is perhaps the more important on purely strategic terms, has stalled indefinitely since mid-2015. The *Power of Siberia* project is going on, albeit with significant delays, but its profitability for *Gazprom* is no longer guaranteed, because anticipated revenues appear shrinking from the original (as of May 2014) estimates.

Dr. Vassilios Sitaras

Energy security analyst

Corinth, Greece, and Baku, Azerbaijan

Table of Contents

1. Putin’s Grand Strategy and the Energy “Card”	vi
2. Main reasons behind exporting gas to China	vii
3. Projects and Challenges	ix
4. Conclusions	xii

NOTE: For references and bibliography, please see the text’s footnotes

I. PUTIN'S GRAND STRATEGY AND THE ENERGY "CARD". Ever since assuming the leadership of Russia in 2000, Vladimir Putin has had one strategic objective: to restore the nation's status as a Great Power, offsetting the development he had described as *"the single most important geopolitical disaster of the twentieth century"*, namely the demise of the Soviet Union. Putin was well aware that the most significant comparative advantage of Russia was its vast energy (oil and gas) resources, among the largest in the world. In addition, ever in the Soviet times, an enormous export infrastructure network of oil and gas pipelines had been created, although this was purely European-oriented¹. Vladimir Putin's own Ph.D. Thesis for the Mining Institute of St.Petersburg, entitled *"The Strategic Planning of Regional Resources under the Formation of Market Relations"* (1997), was the clear forerunner of this Grand Strategy, to be implemented right after he assumed power. Although the academic originality of the Thesis, which was an essay on how a state should manage its natural resources, is highly disputable,² its far-reaching implications cannot be disregarded.

In 2003, the pivotal White Paper *"Russian Energy Strategy until 2020"* followed.³ This policy paper clearly stated that energy should be treated as *"an instrument of domestic and foreign policy"* and also that *"the role of the country on global energy markets to a great degree determines its geopolitical influence"*.⁴ Russia, by masterfully playing the game of international energy geopolitics, could potentially increase its influence in Eurasia. For the purposes of this analysis, we shall limit ourselves only at the natural gas sector, leaving aside

¹ The first-ever Russian export project to the East was an oil pipeline agreed in May 2003 between a private company, YUKOS, and China's CNPC. After the inglorious demise of YUKOS on Putin's orders, the whole project was continued by a public company, Transneft, and completed only in 2010. It's known as the "Eastern Siberia–Pacific Ocean" pipeline.

² Igor Danchenko and Clifford Gaddy, *"The Mystery of Vladimir Putin's Dissertation"*, Lecture for The Brookings Institution, 30/3/2006, available at www.brookings.edu

³ *Energeticheskaya Strategiya Rossii na period do 2020 goda* (2003), www.rg.ru briefly analyzed in Martha Olcott, *Vladimir Putin and the Geopolitics of Oil*, Baker Institute 2004, www.carnegieendowment.org

⁴ Ibid. The English translation of the text quoted comes from John Lough, *Russian Energy Diplomacy*, May 2011, www.chathamhouse.org.uk

the petroleum one⁵. It seems that the specific objectives of Russian energy diplomacy via the manipulation of gas exports were two-fold: The first concerned the former Soviet republics, and especially Ukraine, a pivotal energy transit country. Perceived as Russia's "Near Abroad" by the philosophy of "Eurasianism", it was time to bring back under the Kremlin's grip⁶. Now that the Red Army was long gone, gas dependence was to be translated into political dependence. The second aim was to increase leverage in the European Union itself, including the new -after the 2004 enlargement- member-states, most of them belonging to the former Communist block.

For this strategy to function abroad, a first step was necessary regarding the internal gas market: implementation of the doctrine of "resource nationalism", which meant state control of the resources⁷. By 2005, the Kremlin had, indeed, managed to regain ownership control (by acquiring a bit more than 50 % of the shares) of *DAO Gazprom*, the world's largest producer and exporter of natural gas⁸. *Gazprom* also owns and operates an enormous pipeline network of 169.000 kilometers, by far the longest in the world. In the skillful hands of Putin, *Gazprom* was a commercial entity no more: it was destined to become an extremely useful lever of foreign policy and a means of power projection abroad, in effect something of a second Ministry of Foreign Affairs.

As far as gas export projects were concerned, Putin's European Strategy focused on two key pipelines, which were, in effect, redundant from a commercial point of view (given *Gazprom's* existing infrastructure): the 55 bcm-capacity "Nord Stream" to Germany, designed to bypass Poland, and the 63 bcm-capacity "South Stream" to Austria and

⁵ Please note that the commodity market of natural gas, still fragmented (only regional markets exist dominated by long-term contracts) and with transportation done mainly via pipelines, is quite different than the oil one (with a global price, spot contracts and mainly ship transportation), so much more prone to politics.

⁶ Thrassy Marketos, *The Geopolitical Components and the New Parameters of Russia's Relations with the Republics of Kazakhstan and Uzbekistan in the post Cold War Period*, Ph.D Thesis, Panteion University, awarded 2006 & published by the Association for the Promotion of Beneficial Books, Athens 2008 (in Greek)

⁷ More about "resource nationalism" in Vassilios Sitaras, "National Oil Companies", *Foreign Affairs-Hellenic Edition*, February 2014 (in Greek), available at www.academia.edu

⁸ More about the role of this company in Vassilios Sitaras, "The EU Commission versus Gazprom", *Foreign Affairs-Hellenic Edition*, April 2014 (in Greek), available at www.academia.edu

Northern Italy, designed to bypass Ukraine. Despite the fact that both projects were highly criticized by many countries of the region as being purely “political”, *GAO Gazprom* was able to find precious allies and partners in the face of powerful energy companies from Germany, the Netherlands, Italy and France. This fact in itself demonstrated that there was no genuine solidarity among EU member-states as far as energy security was concerned, with the stronger -already enjoying differentiated supply routes- ready to sacrifice the weaker ones, in order to promote business interests. The resentment of Poland towards Germany, when (in 2006) the Polish Ministry of Defense compared “*Nord Stream*” to the 1939 Molotov–Ribbentrop Pact, was more than evident. As of today (2016), “*Nord Stream*” is operational⁹ and in the process of being expanded as “*Nord Stream II*”. The “*South Stream*” project, on the other hand, seems to have stalled indefinitely, for a variety of reasons. While the former pipeline did go forward, mainly thanks to the “*specific gravity*” of Germany and the enduring efforts of its former Chancellor, Mr G.Schroder (appointed by Putin as CEO of the project company), by the end of 2014 the latter had run out of steam, financial as well as political. A follow-up project, *Turkish Stream*, was short-lived, as it was a victim to the Russian-Turkey crisis.

II. MAIN REASONS BEHIND EXPORTING GAS TO CHINA. Because of its comparatively high import prices, the European gas market has always been extremely lucrative for Russia’s national champion, *GAO Gazprom*. While in terms of sales volumes it is no more than approximately one third (with the bulk being the domestic market), in terms of revenues it is equal to more than two thirds¹⁰. Of course, due to proximity and developed infrastructure, Europe is Russia’s “natural” or “logical” market. Few, if any, other suppliers can beat the existing Russian price for the majority of EU countries. Nevertheless, too much emphasis towards a single geographical area has certain drawbacks, too. It tends to create a so-called “*monopsony*” relationship, which is now perceived as a “*strategic vulnerability*” by the Russian leadership. Especially after the severe 2006 and 2009 gas supply crises (where Russia had its share of responsibility), strong forces in Europe, led by no other than the EU Commission itself, vehemently opposed *Gazprom’s* new export projects, as they linked them

⁹ The first string was completed in 2011 and the second in 2012. For project details, see www.nord-stream.com

¹⁰ John Lough, *Ibid*, p. 3

to monopolistic practices and abuse of dominant market position¹¹. The Crimean crisis of 2014 further aggravated the whole situation.

Therefore, in a rather unlikely, but still *theoretically* possible, case of an EU embargo against Russian gas (as it was the case with Iranian oil and gas from 3,5 years, from mid-2012 until early 2016), Russia would suffer a severe blow. As Dr. Brenda Shaffer has quite plausibly argued, in line with the theory of structural realism in international relations, asymmetrical energy relations are likely to be exploited by the stronger side¹². This was a key drawback of Russian export structure that had to be addressed by the country's leadership and the obvious alternative was China.

Some basic figures will help highlight the asymmetrical interdependence of the two sides. Despite a common belief for the contrary, Russian gas trade is much more dependent on the European market -as a whole- than the other way around. While no more than 30% of European gas consumption originates from Russia and *Gazprom*, Russian export dependence to Europe was almost 100% before commissioning of its first LNG plant, Sakhalin-2 (2009), with a present output of 13,25 bcma. As late as 2015, no less than 87% of *Gazprom's* total exports (158,6 bcm out of 182,9 bcm) went to Europe, although this figure includes 27 bcm for Turkey. Even we consider Turkey a market of its own, still 72% of *Gazprom's* exportable gas goes westwards, primarily to EU member-states. In addition, according to IEA's estimates¹³, European demand for natural gas (with the sole exception of Turkey, if we consider it a part of the same market) is due to slow down significantly in the forthcoming two decades up to 2035. On the contrary, Chinese demand for natural gas is likely to grow between two-fold and three-fold, for a variety of reasons analyzed by H.Rogers, such as the interests of public health and the commitments China has made to the COP21 process, in order to de-carbonise the atmosphere¹⁴. While as late as 2010 the European market (Turkey included) was almost four times the size of the Chinese one, by 2035 the two markets will be

¹¹ About which see Vassilios Sitaras, *"The EU Commission versus Gazprom"* and Nicolo Sartori, *The European Commission vs. Gazprom: An Issue of Fair Competition or a Foreign Policy Quarrel?*, Istituto Affari Internazionali, 2013, www.iai.it

¹² B.Shaffer, *Energy Politics*, University of Pennsylvania Press, 2009

¹³ *World Energy Outlook 2014* (released on 12/11/2014), www.worldenergyoutlook.org

¹⁴ Howard Rogers, *Asian LNG Demand: Key Drivers and Outlook*. Oxford Institute of Energy Studies, April 2016, www.oxfordenergy.org

more or less equal. Therefore, market dynamics, apart from geopolitical rationale, dictated the Russian shift to the Far East.

Against this background, even before pipeline exports to China were to take place, Russia started to realize the power of LNG exports. LNG is much less of geopolitical “cement” than a major pipeline, but it comes with inherent flexibility, as far as export destinations are concerned. Therefore, apart from Sakhalin-2 (see above), of which sales agreements were signed with Far East consumers in 2004 and exports started in 2009, more projects eyeing Asia are currently in the making. One of them is Yamal LNG in the Arctic Ocean, a 27 billion-USD project with no *Gazprom* involvement¹⁵. A major shareholder of Yamal LNG, which utilizes the enormous resources of the South Tambey Field and will begin shipments in late 2017, is China’s *CNPC* with a 20% share. When Chinese financial institutions announced a mega-loan to the French shareholder *TOTAL* (2015), an expert commented: *“After years of Western-Russian interdependence on energy projects, the sanctions regime seems to have nudged Moscow decisively towards Asia in search of support, financing, and technological know-how”*¹⁶ Maximum output of this LNG plant will be 22,8 bcma.

Originating from the same resource base, the planned *Altai* pipeline to China (see below) will offer Russia an unprecedented bargaining position, as it would be able, theoretically, to detour gas flow from Europe. This could occur either as a result of EU sanctions or as coercive diplomacy on behalf of Russia itself. Of course, *Altai*’s 30 bcma is not a huge amount, compared with the 158,6 bcm that *Gazprom* exported to Europe in 2015. Still, it’s better than nothing. Geopolitically, as the Indian analyst S.Johny has laconically put it, gas pipelines from Russia to China *“bring together two prominent world powers – one the world’s second largest and the fastest growing major economy and the other a former superpower that still nourishes great ambitions (...) Russia is rich with natural resources, while China is badly in need of resources”*¹⁷. If bilateral cooperation advances beyond energy to an entire spectrum of affairs, such as non-energy trade, transportation, defense, transfer of scientific know-how, transactions in their national currencies etc (sectors that have to be

¹⁵ In late 2013, the Russian state amended the law, enabling LNG exports only -not pipeline ones- for private companies, as well, such as *Novatek*, Yamal’s majority shareholder.

¹⁶ Scott Belinski, *Putin May Have Last Laugh over Western Sanctions*, www.oilprice.com 2/4/2015

¹⁷ Stanley Johny, *Putin’s Pivot to the East*, 22/5/2014, www.academia.edu

analyzed in detail by separate papers), it would lead to the creation of a deep, purely strategic alliance. While President's Nixon now legendary "*triangular diplomacy*" of the early 1970s managed to balance the two communist powers (already distanced after the early 1960s rift) against one another, this new rapprochement can potentially close the gap and forge a powerful "axis", strong enough to challenge US global hegemony. The 2014 gas deal (see below), together with some other developments, received attention in the USA as a potential "*threat*" to America's global interests¹⁸.

III. PROJECTS AND CHALLENGES. The big Yamal Peninsula, mentioned above, is much more than a private LNG project: in total, it contains 11 gas and 15 oil, gas and condensate fields, with approximately 16 tcm of estimated reserves, together with the adjacent offshore areas¹⁹. The majority of them belong to *Gazprom*, which started production in 2011 at an initial level of 8 bcma. Initially, this production covers domestic demand, but it is scheduled to peak in the 2030s at more than 300 bcma (Yamal LNG included). To sum up, the Yamal mega-project will play a pivotal role in Russian gas industry development in the 21st century, provided new markets are found. Given Yamal's importance, the key export project for *Gazprom*, as far as pipelines to China are concerned, is the "western" export route or *Altai*, because its gas will originate from Yamal itself, as well as from the old Russian "champion", Urengoi (in production since 1978). It will transport 30 bcma across 2.800 kilometers and over the Altai mountain range, up to the Xingjian Uyghur Autonomous Region.

The history of the project goes 12 years back: as early as October 2004, *Gazprom* and *CNPC* had signed a Strategic Cooperation Agreement, providing for natural gas delivery to China by means to be identified. Almost two years later (July 2006), a Coordinating Committee for the *Altai* project was established²⁰. In June 2009, Deputy Prime Minister of Russia, I. Sechin, and Vice Premier of China, Wang Qishan, signed a formal MoU to cooperate in the gas sector. This led, three months later (Oct. 2009), to a Framework Agreement on the volumes, directions and startup date for supplies, linking the price

¹⁸ Stephen Blank, *New Momentum in the Russia-China Partnership*, 30/3/2016, www.jamestown.org

¹⁹ All data and information from www.gazprom.com

²⁰ Ibid.

formula with an oil-index. *Gazprom* and *CNPC* finalized the key commercial parameters of the contract in October 2010, but no sales agreement was signed, in order for the pipeline to be built. In effect, the whole endeavor was then put on hold for approximately three to four years, due to emphasis allocated to the so-called “eastern” export route (see below).

Nevertheless, in November 2014 a revised Framework Agreement was inked in Beijing by the two companies, in presence of Mr. Putin and the Chinese leader, Xi Jinping. According to the *Gazprom* CEO, A.Miller, with the addition of the western route, potential gas supplies to China could exceed the levels of Russian exports to Europe! The heads of agreement followed (May 2015), outlining the main technical-commercial parameters of supplies, but, as of the time of writing, no sales contract has been reached yet. Actually, by late July 2015, Russian officials had told *Vedomosti* that “*implementation of this gas deal could be delayed indefinitely*”.²¹ According to H.Rogers’ recent calculations, *Altai* is really needed only if we assume that Chinese gas demand increases according to the best-case (or “*high*”) scenario up to 2030, reaching 483 bcm. Otherwise (under the “*low*” or even “*base*” scenarios), it will practically be redundant for China²². There have also been some environmental concerns about the effects of the *Altai* construction, as well as doubts about the existence of a “real” market: despite its vast size, Xingjian is populated by a mere 20 million people. China’s real market is located eastwards, far away from Xingjian.

This is exactly where the other Russia-China gas pipeline is targeting at. It’s the “eastern” export route or *Power of Siberia*. A late starter compared with *Altai*, as of today (spring 2016) it’s a much more “*mature*” project, as construction has already started. This unified gas transmission system will extend from the brand-new Irkutsk and Yakutia gas production centers to Vladivostok in the Pacific Ocean, with another spur to China (Manchuria) halfway. Maximum capacity will be 61 bcma and total length 3.970 kilometers²³. Although the idea was around since the mid-2000s, it remained dormant for some time. The final investment decision (FID) for the development of the new gas fields was adopted by *Gazprom’s* Management Committee in October 2012, allegedly on Putin’s orders.

²¹ www.vedomosti.ru, 22/7/2015

²² H.Rogers, *ibid*, p. 36

²³ All data from www.gazprom.com

The “breakthrough” for *Power of Siberia* finally came on 21/5/2014 in Shanghai, when Alexei Miller and Zhou Jiping (the head of CNPC) signed a sales agreement worth around 400 billion USD (!), providing for the supply of 38 bcma for a period of 30 years. This was probably “*the gas deal of the 21st century*”, dwarfing the combined sales contracts signed in Baku (September 2013) between the Shah Deniz consortium and its European-Turkish customers, which amounted to 16 bcma for 25 years. Putin and Xi were also present on 21/5/2014. Welding of *Power of Siberia*’s first joint took place soon afterwards, on 1/9/2014²⁴. Total project cost, including the development of the gas fields, is estimated at 55 billion USD or two times more than Yamal LNG, which was, until recently, the most expensive gas project in Russia.

As the feeding gas fields concerned have nothing to do with Europe, *Power of Siberia* will not increase Russia’s bargaining position in Europe (by detour of the gas flow to China, as is the case with Altai). Still, it will provide additional export volumes and revenues, especially if the full capacity of 61 bcma is reached²⁵. According to one of the project’s critics, Alexander S. Martin, this pipeline “*presents a complex vector of potential conflict. Arctic ice melt, energy resource shortage, and increasing geopolitical tensions are all implicated*”²⁶. Even if this claim is disputable, current energy prices present a major financial and commercial challenge. Early in 2016, *Gazprom* said it will spend only 1,17 billion USD this year on the construction of the pipeline itself, two times down from the original budget of 2,6 billion USD. Some very big tenders have already being cancelled late in 2015.²⁷ By that time, only 80 kilometers had been built or just 2% of the total length. The break-even point of *Power of Siberia* is said to be at a gas price of no less than 350 USD per 1.000 cubic meters, rather ambitious under present market conditions. As sales revenues appear shrinking from the original estimates, *Gazprom*’s profitability is no longer guaranteed. Of course, the deal is too important to abandon, but financing is extremely difficult and delays should be anticipated.

²⁴ Ibid.

²⁵ This view is shared by Jack Sharples, *The Shifting Geopolitics of Russia's Natural Gas Exports and Their Impact on EU - Russia Gas Relations*, *Geopolitics* 2016, issue and date tbc

²⁶ Alexander S. Martin, *New Grounds For War - How Power of Siberia Impacts the Arctic*, *Modern Diplomacy*, March 2016, www.moderndiplomacy.eu

²⁷ Alexei Lossan, *Gazprom cuts spending on Power of Siberia pipeline, delays Vladivostok LNG*, 9/2/2016, www.rbth.com

An expected prepayment of 25 billion USD on behalf of the Chinese side never occurred²⁸. Actual deliveries are now scheduled to begin much later than originally anticipated (2018), perhaps in 2021 the earliest. Another question is whether the volumes will eventually go up from the initial 38bcm to the maximum possible output of 61 bcm. By increasing the volumes, profits will increase, too, because the pipeline infrastructure will be in place.



The two proposed gas pipelines to China. <https://facingjanus.wordpress.com/tag/iran/>

IV. CONCLUSIONS. Upon arriving at Beijing in order to celebrate the 70th anniversary of Japan’s surrender in W.W.2 (2/9/2015), President Putin sent a message to the West, by saying: *“Our countries are consistently moving towards the creation of a strategic energy alliance that, I am sure, play a significant role in international economic relations (...) The implementation of these large scale projects is our absolute priority for the near future”*.²⁹

Indeed, as we tried to show, there is a genuine rationale behind Russia’s gas export projects to China, pipelines and LNG alike. This includes purely commercial, as well as strategic or geopolitical considerations. According to the former, China is too big a market to

²⁸ M.Lelyveld, *China-Russia Project Stalls, as Energy Prices Plunge*, 25/1/2016, www.rfa.org

²⁹ *Putin moves closer to Beijing with Energy*, www.tass.ru/en , 2/9/2015

be ignored, especially when we project demand into the future (although several demand scenarios vary significantly). Therefore, it's a rationalization of Russian export policy, until recently focused mainly on Europe. According to the latter, a Russia-China "axis", stemming from energy cooperation (which includes increasing crude oil deliveries³⁰ and four atomic reactors constructed by *ROSATOM*, two of them ready in 2006/7 and two more by 2018) but reaching well beyond that, can make the tectonic plates of international order move. United, Russia and China could challenge the US ambitions in the so-called "*Grand Chessboard*".

Unfortunately for its masterminds, this historic shift came a bit late. "*Russian Energy Strategy until 2020*" was forecasting the importance of shifting towards the Chinese market as early as 2003, but no concrete steps were taken back then. The Kremlin had been skeptical for a decade to authorize such a big and audacious move³¹ and the catalyst proved to be the early 2014 Crimean crisis. But, almost immediately after the 2014 gas deal, the global energy landscape moved from a "tight" to a "loose" market and prices literally collapsed. Under these conditions, the situation is not favorable for implementing ambitious -and extremely costly- endeavors. At the end of the day, they are capital investments, which have to pay off. *Gazprom* is adamant in demanding "oil-indexed" gas contracts, which are really profitable, but only when oil prices are high. With *Power of Siberia's* profitability now doubtful and *Altai* construction stalled (see above), the reality is hard for Russia. Had construction of both commenced earlier (when focus was on *Nord Stream* and the ill-fated *South Stream*), their prospects would have been better. Gal Luft, a renowned expert in energy security, is skeptical even about the evolution of the Russia-China energy cooperation itself: "*The deal may not turn out to be a bonding experience for the China and Russia as commonly believed. Russia has always had uneasy relations with its clients and its*

³⁰ In May 2015, Russia became Beijing's top crude oil supplier for the first time after almost ten years (October 2005), overtaking Saudi Arabia. That month, average daily deliveries from Russia to China reached 927.000 barrels per day. www.rt.com Two years earlier, in June 2013, *Rosneft* had signed an oil sales contract with *CNPC* worth some 270 billion USD, providing for deliveries of 360 million tons of crude over 25 years.

³¹ As late as mid-2011, Lough was writing: "*Russia still appears hesitant about establishing gas cooperation with China. There are some grounds to believe that Gazprom has been reluctant to commit gas volumes from East Siberia to China for fear that they might be needed to backfill the gas supply system elsewhere in Russia*". John Lough, *Ibid*, p. 5

relations with China have been historically marred with distrust and mutual antipathy".³²

This remains to be proved in the light of future developments.

Overall, it seems to me that, although bilateral gas cooperation is a “win-win” deal for both regional powers (one being an exporter and the other an importer of energy), China will get the most of it, as its overall economic position is healthier. The timing of the deal could not have been better for Beijing: as Russia was desperate in proving to the West that it could differentiate its markets, it was ready to accept a low price which would have been ruled out a year before (but still higher than the Turkmen gas price, see below)³³. Renegotiation of the contract should be expected well before deliveries commence. Even the Russian doctrine of “resource nationalism” may eventually succumb to Chinese interests: *CNPC*, in the context of the 2014 gas deal, is rumored to acquire 19% of the Russian oil giant and crude exporter to China, *Rosneft*.

Last but not least, we fully agree that “to build robust and lasting relations, the two countries will need much more than steel pipes in the ground”³⁴. Indeed, the strategic interests of China and Russia are not converging in every single case. Where ambitions are overlapping, issues will always arise. Energy interdependence is a stabilizing factor bringing nations together, but never enough. Both regional powers compete for dominance over a very large part of Eurasia, such as the former Soviet republics, where Chinese penetration has been impressive. Because of its extremely expanded non-energy production base and the enormous currency reserves it has accumulated, the Chinese dragon is the rising power of the continent, while Russian influence is rather declining (as did Russian GDP in 2015). The “energy weapon” is powerful, but not omnipotent and it cannot offset Russia’s structural deficiencies.

The role of *CNPC* in Turkmenistan’s energy sector is illuminating, as viability of both Russian gas projects is related, indirectly, to the Turkmen gas exports to China.³⁵ The *Central*

³² Gal Luft, *The Sino-Russian gas deal*, www.ensec.org, 27/5/2014

³³ Luft commented in 2014: “Diplomatically embattled, Russia needs a new market for its gas to replace the increasingly shaky European market”. Ibid.

³⁴ Ibid.

³⁵ M.Lelyveld, *ibid.*

Asia (or Turkmenistan-China) gas pipeline, constructed by *CNPC* and operational since 2009, will carry 65 bcma by the early 2020s, compared with 25,5 bcm in 2014. This staggering volume is close to the sales volumes of *Altai* and *Power of Siberia* combined (68 bcma). By 2015, three of the four parallel strings were in place and the main deposit, the second-largest gas field in the world, had been developed. Turkmen gas is considered to be cheaper than Russian gas in the Chinese market³⁶. Ironically, just a few years ago, Turkmenistan's major customer was *Gazprom*, which has now stopped receiving gas. Competition is a threat for the suppliers, as it pushes prices further down. *Gazprom*, traditionally used to enjoy a dominant market position in many parts of Europe, has to adjust to the new realities, as far as the Chinese market is concerned. If it manages to sell significant quantities (depending on China's future growth rate...), it will probably recoup the investment and even make some money, after many-many years. But gone are the price premiums it used to know...



***Power of Siberia* construction started in September 2014, but progress has been slow.**

<http://politrussia.com/world/naskolko-dlya-rossii-615/>

³⁶ Ibid. A third -minor- source of pipeline gas to China, besides Turkmenistan and Russia, is Myanmar. It exported a modest 4 bcm in 2015, but this will increase to 11 bcm by the early 2020s. Another source of competition for the two planned Russian pipelines is LNG from all over the world, including East Africa, Malaysia and Australia. According to BP's estimates (2016), global LNG supply in 2035 will double against 2014. According to H.Rogers, *ibid*, p. 35, Chinese LNG imports under the "high" consumption scenario will reach 105 bcm in 2030, or four times more than in 2015 (27 bcm). Finally, under any future scenario, from "low" to "high", Chinese gas production, including shale gas, will skyrocket from 133 bcm (in 2015) to 234 bcm (in 2030). This means that, even under the the "high" scenario, by 2030 China will be able to cover almost half of its needs from domestic production.