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Nabucco West—Perspectives and Relevance: The Reconfigured Scenario

Energy ministers from countries involved in the construction of the Nabucco West gas pipeline—Turkey, Bulgaria, Romania, Hungary and Austria—and their counterpart from Azerbaijan, met in Vienna on 8 October to support the project politically. The aim of the pipeline is to supply Eastern and Central Europe with gas from sources other than Russia. Initially, this most probably would be Azerbaijani gas from the Shah Deniz Phase 2 project. Given the determination of Azerbaijan and Turkey to complete the Trans-Anatolian gas pipeline (TANAP), it is likely that Azerbaijani gas will eventually reach the European market. Although the recent meeting in Vienna suggests that Nabucco West is a realistic project, the TANAP company has yet to choose whether to connect with this pipeline or the Trans-Adriatic Pipeline, which is aimed at supplying the Italian market. The decision is due in 2013.

This paper examines the impact that TANAP and Nabucco West could have, if implemented, on the energy security of the countries involved—Bulgaria, Romania, Hungary and Austria. Analysis suggests that Nabucco West's geostrategic and economic relevance varies significantly for each of these states.

From Nabucco to TANAP and Nabucco West

A need to find an alternative to natural gas from Russia was the main factor influencing Eastern and Central European states' interest in energy cooperation with the South Caucasus. The purchase of non-Russian gas was hampered by a lack of both gas interconnectors with Western Europe and gas terminals to bring LNG from other sources. Thus Russia retained its monopoly and used this position to gain political leverage in its influence over Eastern and Central European states. The need for alternative sources became especially visible in January 2006 and January 2009, when supplies to several Eastern and Central European countries were disrupted because of gas price

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disputes between Ukraine and Russia. Among them, the most vulnerable were Moldova, Slovakia and Bulgaria.

Following two waves of enlargement to the east in 2004 and 2007, the EU became even more involved in the search for new gas supplies to Member States. The European Commission seeks to add the Fourth Corridor or the Southern Gas Corridor to the three existing gas corridors (Mediterranean, Northern and Russian). This would consist of gas pipelines delivering Caspian and/or Middle Eastern gas to the EU countries. Among the gas transit routes considered the most important was—until recently—the Nabucco gas pipeline, planned to transport gas from Azerbaijan, Turkmenistan and Iraq¹ through Turkey to the EU countries (Bulgaria, Romania, Hungary) and on to the Austrian gas hub in Baumgarten am den March. This “Nabucco classic” concept transformed this year into two compatible pipeline projects. These are the Trans Anatolian Pipeline (TANAP), which would carry Azerbaijani gas through Turkish territory, and Nabucco West, which would continue gas transportation through the European sector as planned in the first version of this pipeline (“Nabucco classic”). TANAP² is to be built by Azeri and Turkish state oil and gas companies—SOCAR, BOTAŞ and TPAO, as well as also some Western European companies, which are to be included in the project consortium.³ TANAP is designed primarily to transport Azerbaijani gas from the second phase of the Shah Deniz project—estimated at 16 bcm of gas in 2018 up to 31 bcm annually by 2026. The builder of the Nabucco West pipeline is to be Nabucco Gas Pipeline International GmbH. The company has six shareholders: OMV (Austria), MOL (Hungary), Transgaz (Romania), Bulgargaz (Bulgaria), BOTAŞ (Turkey) and RWE (Germany).⁴ The planned capacity of “Nabucco classic” was 31 bcm per year, reduced to 10-23 bcm gas per year in the case of Nabucco West.

The other pipelines mentioned by the European Commission were the Turkey-Greece-Italy Interconnector (ITGI) and the Trans Adriatic Pipeline (TAP).⁵ At the moment, the latter pipeline is competing with Nabucco West for the gas from Azerbaijan. It is up to Azerbaijan and Turkey to decide which gas export route from TANAP to Europe to use. While TAP offers certain commercial advantages, it lags in terms of legal preparations (e.g., environmental permissions) and it does not enjoy the same political support as Nabucco West, which is backed by an inter-governmental agreement. The presence of Azerbaijani Minister of Energy Natig Aliyev at a recent meeting of Nabucco countries’ energy ministers is a sign that the project is attractive for Azerbaijan and TANAP. According to Reinhard Mitschek, managing director of Nabucco Gas Pipeline International GmbH, the Nabucco West project has already started cooperation with TANAP by offering its engineering

¹ Iran was another country that at the beginning of the last decade was considered to be a potential supplier to Nabucco. However, Iranian participation in the project has become less and less realistic as the country’s controversial nuclear programme and U.S. pressure on European partners to apply sanctions on the regime in Tehran has led to its greater international isolation.

² The project was first announced at the end of 2011. In December last year, Turkey and Azerbaijan signed a memorandum of understanding establishing a consortium to build and operate the pipeline. On 26 July, Turkish Prime Minister Recep Tayyip Erdogan and Azerbaijani President Ilham Aliyev signed an intergovernmental agreement on the construction of TANAP. “The Energy of the Future is Ready”, <http://www.tanap.com/en/the-energy-of-the-future-is-ready.aspx>

³ “BP confirms intention to acquire 12-percent share in TANAP”, 09. 11. 2012, <http://en.trend.az/capital/energy/2086095.html>.

⁴ According to OMV CEO Gerhard Roiss, inclusion of Azerbaijan as an upstream country in the shareholder group is possible. 08. 08. 2012. <http://www.platts.com/RSSFeedDetailedNews/RSSFeed/NaturalGas/8610397>.

⁵ The Shah Deniz consortium already resigned from investigating ITGI as possible route for Azerbaijani gas from TANAP in February.

data to the Turkish–Azerbaijani side.⁶ However, the final decision concerning Nabucco West and TAP will be taken only next year.

Besides Azerbaijan, Turkmenistan and Iraq are potential gas suppliers for Nabucco, which may in future be the sources for TANAP and Nabucco West. The inclusion of Turkmenistan's gas resources is considered by the EU to be viable. Turkmen President Gurbanguly Berdymuhamedov is willing to send his country's gas to Europe, and made several statements expressing Turkmenistan's desire to do this. This was confirmed by Turkmenistan during a visit by Gunther Oettinger, European Commissioner for Energy, to Ashgabat on 4 September.⁷ However, the chances of Turkmenistan being included in the chain of TANAP and Nabucco West suppliers are still low, because of the Russian and Iranian veto on the construction of the Trans Caspian gas pipeline. The latter would transport Turkmen gas through the Caspian Sea to Azerbaijan, and later via Baku Tbilisi Erzurum/TANAP/Nabucco West pipelines to Europe. The governments in Moscow and Tehran cite ecological concerns for their opposition to this project—and they also do not want to be excluded from the profitable transit of Turkmenistan gas. Azerbaijan and Turkmenistan signed a deal with Ankara on gas transit to EU states in October 2011. However, the countries' dispute over the Kyapaz-Serdar oil field under the border in the Caspian Sea complicates their potential cooperation on the issue of a Trans Caspian gas pipeline.

Another potential source of gas for TANAP/Nabucco West may be Iraq. However, the export of Northern Iraq's vast hydrocarbon resources requires consensus between the autonomous Iraqi Kurds (controlling the area) and the government in Baghdad. Up to now, growing political disputes between them has made it impossible to reach agreement on sharing of profits and development of the necessary legislation. The recent surge of terrorist activity by the Kurdish PKK in southeastern Turkey also poses a risk to the transportation of gas through the region. Therefore, the most reliable possible supplier is Azerbaijan.

Besides the supplier issue, in analysing the fate of “Nabucco classic” and prospects for the Nabucco West pipeline's construction, one must not forget Russia's competitor project—the South Stream gas pipeline. This project proposed by Russia in 2007 aims to supply gas to the same region as the Nabucco West project and is planned to bypass Turkey and Ukraine, traversing a 900-kilometre offshore section from the Russian to the Bulgarian coast and with a planned capacity of 63 bcm of gas.⁸ After reaching Bulgaria, South Stream was supposed to supply the same countries as Nabucco, with the exception of Romania (the link between Bulgaria and Hungary would go through Serbia). The South Stream gas pipeline, a far more ambitious project than “Nabucco classic” may never be built, as neither the funding nor the 63 bcm of gas have been identified, and Gazprom is due to make a decision on whether to invest in the project by mid-November. Nevertheless, South Stream has, during the past five years, been presented by Russian politicians and Gazprom as a more attractive and realistic project than Nabucco, which certainly had an impact on the failure of the “Nabucco classic” project.

The joint decision of Azerbaijan and Turkey to build TANAP is fully understandable. First, this project, in which the supplier country is involved, is much more realistic than “Nabucco classic”.

⁶ *Nabucco West starts cooperation with TANAP*, 12. 10. 2012, <http://en.trend.az/capital/energy/2076228.html>.

⁷ “EU: Energy negotiations in Ashgabat constructive”, 05. 09. 2004, <http://en.trend.az/capital/energy/2062063.html>.

⁸ In June, Gazprom CEO Alexei Miller spoke of a new, phased approach, with two initial pipelines each carrying 15.5 bcm gas, with the possibility of expanding this to four at a later date.

For Azerbaijan, the TANAP project secures control of its product all the way to the EU markets. For Turkey, it guarantee it will be a gas transit country with all the advantages of this status (such as discounts on Azerbaijani gas plus transit fees). Finally, for the governments in Baku and Ankara, support for Nabucco West, a project strategically important for the European Commission, means political advantages in their relations with the European Union. TANAP, if constructed and linked to Nabucco West, will influence the energy security situation of some Eastern and Central European countries. The impact will be especially noticeable in those areas where the pipeline will be built, namely Bulgaria, Romania, Hungary and Austria.

Bulgaria: High Stakes and High Chances

Bulgaria imports about 75% of its primary energy resources (oil, gas, nuclear fuel and coal) from Russia, with the rate of imported gas reaching as high as 100%. There are prospects for finding shale gas and some offshore gas, but there are not yet any proven domestic reserves. For a market of only around 3 bcm per year, the country has an extensive system of gas pipelines that serves its own needs and those of neighbouring Turkey, Greece, and Macedonia (85% of the gas flow is in transit). While energy markets remain heavily monopolistic at all levels, the gas market is a frontrunner in this respect. All gas is imported by the single public supplier Bulgargaz EAD (a fully-owned subsidiary of the 100% government-owned Bulgarian Energy Holding EAD), through two parallel lines that come from Russia. Despite the existing legal framework, true market liberalisation and competition are likely to emerge only after actual diversification of gas supply by source, route, and supplier.

One attempt to solve the question of diversification is to build a grid of interconnectors with neighbours. The one with Romania is scheduled to be completed this year, and others are planned with Serbia, Greece and Turkey. In addition to this, Bulgaria is simultaneously engaged in both the Nabucco West and the South Stream projects. While commitments to the first seem unabated (especially as Bulgaria is certainly on the planned Nabucco West route), prospects for participation in South Stream have been more ambiguous because of the traditionally confrontational tone of Russian-Bulgarian energy dealings and Gazprom's tactics of conducting negotiations with several potential partners in order to optimise its ultimate position. Additionally, the final phase of bargaining over South Stream were also strained by Bulgaria's urgent need to ensure further Russian gas deliveries—and preferably, at a reduced price—as the current gas contract will expire at the end of this year. An investment decision about South Stream, between Gazprom and Bulgarian Energy Holding EAD, is scheduled to be signed on 15 November, provided that the long-term gas supply contract between Bulgargaz and Gazprom is signed before that.

This almost total reliance on Russian gas places Bulgaria in an extremely difficult position, with less space for manoeuvre than Hungary, Romania or Austria. However, its geostrategically important location (it has a Black Sea coastline, is a gateway to Europe for Caspian gas and an important transit route for Russian gas towards the Balkans) gives Bulgaria an added value that makes it an almost indispensable partner in both Nabucco West and South Stream.

Romania, the Least Teetering Nabucco West Partner

Romania's energy dependency in general is considerably below the EU average because its proven domestic reserves. For instance, natural gas reserves are estimated to suffice the country for approximately the next 15 years. Its annual natural gas supply needs are 17 bcm, of which 30% is imported. Prospects for further domestic sources also exist. Shale gas resources have been identified, although neither the exact quantities nor the legal framework for their exploration and exploitation has been clarified as of now.⁹ Additionally, an estimated 70 bcm of natural gas was detected under the Black Sea continental shelf (a territory obtained from Ukraine through a ruling by the International Court of Justice in 2009). Therefore, seeking domestic alternatives is just as important for Romania as is gaining access to Caspian gas. To that end, however, large-scale investments are required, which in turn could be attracted by a further liberalisation of the energy market—a process initiated as early as 1998, but still far from being concluded.

Because of these uncertainties about alternative sources, the diversification of gas supply resources is high on the Romanian political agenda. Romania remains committed to its engagement with the Nabucco West project (it has participated from the beginning of the process) and is ready to follow EU policy choices.¹⁰ The benefits of this gas pipeline, which would cross 470km of Romanian territory, lie mainly in the expected €1.5 billion in investments in infrastructure and logistics, in transit fees and in access to a portion of the gas, which, however, would probably only partially substitute for Russian imports. In parallel to its commitments to Nabucco, initially Romania had not, at least theoretically, excluded the option of joining South Stream. However, Romania was only considered a potential transit route when Gazprom used it to pressure the company's Bulgarian partners by threatening the use of possible alternatives (for instance, in negotiations in 2010). With the South Stream route now finalised without it on board, Romania's willingness to participate in Nabucco West is unequivocal.

In fact, despite its relatively lower degree of dependence on energy imports compared to regional standards, Romania has from the very beginning been one of the most stable partners in the Nabucco consortium. This is not only because of the slight chance of inclusion in South Stream but also because of the country's pro-EU foreign policy orientation.

Hungary: Gas Dependency and National Sovereignty

Natural gas makes up the largest share of Hungary's total primary energy supplies, standing at almost 40%. Even though gas demand has dropped since its peak of 15 bcm in 2005, five years

⁹ Energy giant Chevron struck a deal with the Democrat-Liberal government in the spring regarding the exploration of supposed shale gas reserves. In June, shortly after the unexpected change in government, the new Social-Liberal government coalition announced a moratorium on shale gas exploration. Legislation was also proposed to ban shale gas exploitation by means of hydraulic fracturing, the issue has, however, been suspended until parliamentary elections, planned for December.

¹⁰ A view expressed by Romanian President Traian Băsescu in an interview for the Voice of Russia: http://romanian.ruvr.ru/2012_08_15/85172633.

later it still stood at 12.1 bcm.¹¹ Overall gas consumption relies on imports, with 80% coming through Ukraine and Austria, in both cases from Russian sources. The 2006 gas crisis was the catalyst for a series of measures by the government, including increased storage capacity through considerable public stockpiling of both oil and gas, gas-fired electricity capacity also became, to a great extent, convertible to oil, and various options started to be weighed in order to diversify supply routes and sources.

With the new energy strategy approved by parliament in October 2011, three principal government action lines started to emerge. One is increasing the state's role on the energy market, which had been changed to a competitive model in 2008. Another, more long-term objective is to turn Hungary into a regional energy hub by building interconnectors with neighbouring states.¹² Such ambitions are by no means unrealistic, as, out of the approximately 12-15 bcm gas transported on Hungary's transmission network annually, some 4 bcm are reserved for transit through the grid.

The third and politically most articulated government ambition is to reduce the country's high dependence on gas imports. As with other states that appear on maps of plans for the competing South Stream and Nabucco West projects, Hungary has been party to both initiatives. MOL has been a member of the Nabucco project since its initiation in 2002. In April, the prime minister spoke publicly about the possibility of quitting the consortium. Nevertheless, Hungary became, in August, the first of the subscribers to finish its environmental permitting process, thus signalling its continuing commitment to the project. At the same time, Hungary's state-owned power company MVM (Magyar Villamos Művek) is, with Gazprom, the joint owner of the Hungarian part of the South Stream project. Despite news in August that Gazprom was considering to opt for Croatia instead of Hungary, a final investment decision between MVM and Gazprom was signed on 31 October.

While Hungary's need for greater gas supply independence is indisputable, it must also be remembered that the government sees this not only as an economic and security priority but also as a matter of national sovereignty, and hence, Hungary's willingness to engage in any project that can serve this cause.

Austria: Nabucco West, a Matter of Business

Austria is exceptional for its high use of renewable energy, with hydropower contributing more than half of national power generation. Although energy policy focuses mainly on increasing the use of renewables, demand for natural gas is slightly on the rise. Approximately 16% of the supply is satisfied by domestic reserves, with the rest is imported from Russia (51 %), Germany (14 %) and Norway (10 %). This means, that out of the 8 bcm (net import), some 6.4 bcm arrives from

¹¹ "Oil and Gas Security. Emergency Response of IEA Countries: Hungary", p. 2, http://www.iea.org/publications/freepublications/publication/Hungary_2012.pdf.

¹² Interconnectors with Romania and Croatia are already operational, an agreement to build one with Slovakia was signed in January 2011, and the possibility of building one with Slovenia is also under investigation. These efforts are also part of a wider regional ambition of creating a so called North-South Gas Corridor linking the planned LNG terminals at Świnoujście in Poland and the island of Krk in Croatia.

Russia. With a domestic gas grid of more than 38,000 km in total, Austria is an important transit route for natural gas.¹³ The Baumgarten gas hub owned by energy company OMV and located close to the borders with Hungary and Slovakia is the destination for about one-third of Russian gas exports to Western Europe.

Even though Austria's strategic emphasis seems to be more focused on developing renewables and improving energy efficiency compared to Eastern and Central European countries, the diversification of import sources also remains an objective. What is telling in this respect is that OMV initiated the Nabucco project a decade ago. Austria seemed for some time to be willing to participate in both the Nabucco and the South Stream projects, driven by the logic that the more pipelines that go through Baumgarten the higher the storage and transmission fees will be. But following the EU's block of Gazprom's purchase of 50% of the Central European Gas Hub (the trading platform located at Baumgarten, one of the most important in Europe), Gazprom turned its attention towards Italy instead of Austria for the South Stream route. Left with only one option, OMV invests its hopes in Nabucco West—as signalled by Vienna hosting the meeting of energy ministers in October. The Austrian commitment to Nabucco is also emphasized by the fact, that of the six consortium members, only OMV and MOL have upstream operations in the Caspian region.

While Austrian natural gas imports rely extensively on Russian sources, the country's energy profile is far more diversified than those of the other countries analysed because of the country's considerable use of renewables (primarily hydropower). As such, participation in Nabucco West is just as much motivated by expected profits from transiting gas and from the possibility of an increased role for the CEG Hub as by an urgency to reduce dependency on Russia.

Conclusions

The TANAP and Nabucco West gas pipelines still remain the most ambitious proposals within the EU's Southern Corridor framework. While TANAP probably will be built, the fate of Nabucco West depends on Azerbaijan's decision about whether to choose it or TAP. That decision is expected to be taken next year. Certainly, these projects not only have economic but also political implications. Besides bringing economic profits, exporting gas to EU countries could make Azerbaijan and Turkey more important political partners for Brussels. It could also strengthen both countries' ties with their Eastern and Central European neighbours.

A closer country-by-country analysis of the situation of the EU members participating in Nabucco West suggests that while Caspian gas is generally important in easing the overdependence on Russian supplies, these countries have varying degrees of interest in the project as well as various motivations for participation. The project's significance is often also overplayed in their political discourse. Only 10 bcm of Azerbaijani gas from the Shah Deniz in 2018 (or even 20 bcm at later stages) will not substitute for Russian imports to the region. It may help, however, to increase the energy security of some of the states. Its significance lies also in more competitive prices stemming from alternative gas sources and in challenging Russia's monopoly.

¹³ About 80% of the gas carried on the Austrian network is in transit towards its neighbours and Western Europe.

Bulgaria is by far the most in need of non-Russian gas, with Hungary following a close second. However, because of their fortunate geographical locations, the development of an interconnector grid will be a significant step towards diversifying supplies and routes, and their potential to become regional transition hubs promises not only better security prospects but also commercial gains from transit fees. Hungary is at a more advanced stage than Bulgaria in building interconnectors with neighbouring countries. For Romania, supply dependency is not as burning an issue as it is for Hungary or Bulgaria, because of both proven and estimated domestic reserves. Nevertheless, Romania seems to be the most consistently committed to participation in the Nabucco West project. Austria, too, is acting as a reliable partner, but there the project is more a matter of commercial interests than of energy security.

Except for Austria, achieving lower energy intensity through modernisation and opening the market are equally high priorities for each of the analysed countries. For both of these aims, the primary effort is needed from the state, which then can attract more investment. Decisive steps in this direction are necessary for Bulgaria, Romania and Hungary. It is also important to underline that at the end of the day it will not be the Central and Eastern European governments or their national gas companies but the supplier countries that will decide the fate of Nabucco West. Therefore, the countries that are potential gas recipients should still support the idea of this pipeline and the broader concept of a Southern Gas Corridor, but also should seek other ways of improving their energy security.