



BULLETIN

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Life after South Stream: Accelerated Modernisation of Bulgaria's Gas Sector

Dariusz Kałan

In response to the failure of the South Stream pipeline project, Bulgaria announced its plans to create a European gas hub and the Vertical Corridor with Greece and Romania, as well as to accelerate the exploitation of its own potential gas reserves. Although not all of these ideas have a chance of being implemented, the European Commission should continue to support Sofia in its efforts to diversify routes and sources of gas supply. The success of the EU's diversification projects in the region will largely depend on effects on these efforts.

The South Stream gas pipeline promised to Bulgaria, which is totally dependent on Russian gas, supplied exclusively via Ukraine, diversification of routes, the strategic role of a transit state, and economic benefits connected with new jobs, preferential loans and reductions in gas prices. At the same time many controversies, concerning, among others, uncontrolled growth of expenditure and corruption in the tendering process, exposed Bulgaria to the irritation of the European Commission, which, in June 2014, finally initiated the procedure for infringement of EU law against the country¹. Governments in Sofia have built up the country's energy policy around this project, so its failure poses a challenge to energy security, even if demand for gas in Bulgaria is relatively low: gas accounts for only 13% of the energy mix, three quarters of which is used for district heating and the chemical and glass industries. What is more, South Stream remains an unresolved political and legal problem. On the other hand, its fall is an opportunity for the acceleration of smaller diversification projects, which have long been neglected.

A Nervous Game around South Stream. Putin's declaration, in December 2014 to halt construction of South Stream, was met in Sofia with surprise, not only because the government had not received any sort of official notification, but also because the Russian president blamed Bulgaria for the collapse of the project, saying that, in his opinion, the country had deliberately delayed work on its section of the pipeline. Therefore, there is concern in Sofia that Russia will take legal action and will demand compensation in the International Chamber of Commerce. This actually happened when Sofia withdrew from construction of the nuclear power plant in Belene, in which a Russian consortium, Atomstroyexport, was involved. To avoid such a step, Bulgaria immediately asked the EC and the EU Member States for support. A few days after the Putin's declaration, Bulgarian prime minister Boyko Borisov met with the EU commissioner for energy union, and German chancellor Angela Merkel, who encouraged him to continue dialogue with Russia. Fear of legal action is great, especially as Bulgaria has rather limited tools of defence: Sofia's administrative and intellectual abilities in this matter are so limited that Gazprom's lawyers took part in the preparation of national legislation for South Stream.

The game between Moscow, Sofia and Brussels means that South Stream has not officially been cancelled, and Bulgaria, which has invested approximately €250 million, has not withdrawn from environmental studies and new tenders. It seems that Russia is not interested in closing down the South Stream option either. Although Putin has already announced an alternative, Turkish Stream, supplying gas to the EU via Turkey and the Western Balkans and bypassing Bulgaria, the formal admission to withdraw from South Stream without consultation with partners would expose Moscow to the legal action (unlike at Belene, it was Russia that pulled back from South Stream). Hence, during

¹ D. Kałan. "The 'South Stream' Train Stops in the Balkans," PISM Bulletin, no 82 (677), 11.06.2014.

his visit to Budapest in February, Putin softened his December message. He said that Russia had not renounced South Stream (but was not allowed to "implement" it) and suggested that the door to Turkish Stream was open for Bulgaria. All of this is intended to avoid legal steps, but also to stir up anti-EU frustration in Bulgaria that has been visible at least since the withdrawal under pressure of the West of other initiatives backed by Russia (Belene and the Burgas-Alexandroupolis oil pipeline), especially in business circles, which have suffered financial losses in these unrealised projects.

Gas Hub Illusions. After the suspension of South Stream, Borisov announced the creation of a gas hub in Varna, which would become the centre of storage and distribution of gas from Azerbaijan and Russia to the EU. This initiative should be interpreted as an attempt to rebuild the prime minister's image in the country after the failure of South Stream, to put pressure on the EC, which would fund the investment, and to exploit information about the alleged large gas reserves on the Bulgarian Black Sea shelf, in the Khan Asparukh field (the potential of two other fields, Silistar and Teres, is as yet unknown). Although preliminary studies did not give a clear answer as to whether Bulgaria actually has its own gas, the government attaches strategic importance to this issue, based, among other things, on the existence of gas resources in neighbouring Romania. Sofia was not discouraged by negative experiences with drilling in the Black Sea, where only one attempt out of seven, in Romanian waters, brought results, or by the geological differences between the Bulgarian and Romanian coasts. Neither was the government fazed by the decision of French company Total (a member of consortium, also including Austrian OMV and Spanish Repsol, that manages the field) to put back the start of drilling from 2015 to 2016. Even if Bulgaria receives financial support from the EC, the chances of creating the European gas hub are not high. This is not only because the prospects of Bulgaria acquiring diversified gas sources (including its own) are limited, but also because of competition from other countries in the region. Similar aspirations have already been expressed by Ukraine, Romania and Turkey.

The Policy of Small Steps. Bulgaria could consider a gas hub if it has at least a developed system of connections with its neighbours. In February, Sofia proposed the establishment of the Vertical Corridor, based on existing or planned interconnectors, connecting the country with Romania and Greece. However, although Bulgaria has an internal transmission infrastructure (945 km of pipes and six compressor stations with a total capacity of 214 MW), at the moment there is no international connector with a reverse flow option. The existing pipelines connecting with Greece, Macedonia, Romania and Turkey are purely for the transit of gas from Russia.

The government attaches greatest importance to the repeatedly postponed building of a 183 km connection with Greece (IGB), between Stara Zagora and Komotini, the capacity of which (3 bcm/year, expandable to 5 bcm/year) would be enough to cover Bulgaria's annual demand for gas. Moreover, thanks to this interconnector Bulgaria would obtain access to Greek LNG as well as gas from Azerbaijan, as the connection could become a part of Trans-Adriatic Pipeline (TAP), and Bulgaria has already signed a gas supply contract with Azerbaijan. The main obstacles are associated with economic calculations. Even if the TAP opens in 2018–2019, Azeri gas would not give Bulgaria access to the IGB's full capacity, because, according to the agreement, it will get only 1 bcm/year. What is more, along with the growing economic crisis, the resistance of Greece has been increasing, especially as the IGB requires investment in its internal infrastructure. Hence, launching a reverse flow on the existing Kulata–Sidirokastro interconnector is also being considered, but only as a temporary solution. Both countries, along with Romania, announced the joint development of a floating LNG terminal in Kavala too, but lack of money may again prove to be a barrier.

Construction of a 25 km interconnector with Romania Ruse-Giurgiu, including reverse flow, which would provide Bulgaria with 1.5 bcm/year and access to the markets of Central Europe, is also facing problems. Both sides blame one another for paralysing the project, but after the fall of South Stream the negotiations were restarted, and in January it was announced that the pipeline will be operating this year. Regardless of this shift, the problem of Romanian law, which imposes restrictions on selling gas abroad, remains. There is also an issue with Romania's aging infrastructure, including the lack of a compressor station. On even less advanced stages there are interconnectors with Serbia and Turkey, and the Eastring gas pipeline, promoted by Slovakia, which would deliver natural gas to Bulgaria from the west. After years of neglect, Sofia in turn plans to launch a new gas storage facility. At the moment it has only one, with a small capacity (0.5 bcm), located in the village of Chiren.

Stick and Carrot. Another major challenge is the Bulgarian gas market, which is small, financially inefficient and highly politicised. The two largest state-owned enterprises, Bulgaria Energy Holding and the transmission system operator Bulgartransgaz, use monopolistic practices, as the EC has pointed out many times, most recently in March. It seems, though, that the EC deliberately uses the carrot and stick method, for while criticising the market on the one hand, it also presents a number of positive actions for Bulgaria. The latter include the establishment in Sofia of the High Level Group on Central and South Eastern Europe Gas Connectivity (CESEC) in February, and accusations Gazprom of abusing its dominant position with using the Bulgarian case. These steps will help to rebuild the EC's credibility, strained after the fall of the Nabucco gas pipeline. The EC, aware of both the geopolitical significance of Bulgaria, as well as the favourable political climate in the country, should continue to support Sofia in its efforts to diversify routes and sources, as these are in line with the Energy Union and will affect the whole region significantly. An important challenge is, for example, to adapt the existing one-way interconnectors to make them suitable for reverse flows, which would save the need to build new connections. The EC may act in consultation with the United States, which, during John Kerry's visit to Sofia in January, offered to advise the government in its search for alternative gas sources.