

## The role of the Arctic in Russian energy strategy in Europe

By Jakub M. Godzimirski

Over the past few years, Russia has gone through a period of both high expectations and sobering experience of the global economic crisis, revealing the failure of the strategy of economic development propounded by its ruling elite. This experience is like to force the elite to rethink and partly reformulate goals of the long-term strategy for the country's development and may have impact on the realization of several strategic projects, also in the sphere of energy.

National self-confidence soared to unprecedented heights in summer 2007 when the Russian flag was planted by the Russian expedition at the North Pole. This stunt of Artur Chilingarov was widely seen as a highly symbolic proof that Russia was returning as a great power with not only regional but also global ambitions. This move was combined with the semi-official Russian discourse on the country as an indispensable energy superpower and with a growing focus on building a Russian version of what was labelled 'sovereign democracy' intended to make Russia immune to external pressures.

In fact, there are not only symbolic but also other, more down-to-earth reasons why Russia has been paying increased attention to developments in the Arctic. One of those concerns the energy resources believed to be located in this area. According to the last estimates issued by the USGS, 'the mean undiscovered, conventional, technically recoverable petroleum resources in the Barents Sea Shelf are estimated to be more than 76 billion barrels of oil equivalent, which includes approximately 11 billion barrels of crude oil, 380 trillion cubic feet of natural gas, and 2 billion barrels of natural gas liquids'.<sup>1</sup> Those figures make clear how high the energy stakes are and why Russia has again chosen to face the Arctic challenge. This also explains why Russia will have to 'go Arctic' in order to be able to realize its ambitious strategic energy projects.

Some of these projects are especially vulnerable to what will happen in the Arctic, and the most exposed is definitely the Nord Stream gas pipeline. According to official plans, this pipeline will provide Germany and the rest of Europe with up to 55 bcm of natural gas. Half of this volume is to come from the Yuzhnorusskoye gas field, currently being developed by a consortium of Russian and German companies. The other half is to be shipped, starting from 2013, from the Shtokman gas field, the world's second biggest offshore gas field, with 3 800 bcm of gas reserves, to be developed jointly by Gazprom, Total and Statoil. However, it seems that the development of this field may be in grave peril.

Several factors may make the project non-viable. Until recently, it might have appeared that the main obstacles could be of a geopolitical nature, as there was strong opposition in some EU countries to the construction of the Nord Stream pipeline needed to transport gas from Shtokman to West European markets. The recent decisions of the Danish, Swedish and Finnish governments to allow Nord Stream to go through those three countries' exclusive economic zones seem to have removed this obstacle, as the remaining two governments that have to approve the project are those of Germany and Russia, and this seems to be a mere formality.

However, other, perhaps more serious, dangers now seem to loom. The fact that the companies involved in development of the Shtokman field decided to postpone the final decision to 2010 may mean that the purely technological

challenges may be greater than originally expected.<sup>2</sup> Another important factor is the uncertainty linked to the future development of oil and gas prices. In 2008, with the oil price hitting first the magic \$100 per barrel mark and then skyrocketing to almost \$150, it could seem that the project that was to send until 70 bcm of gas to European and global gas markets could become an effective money-making machine, and that technological solutions would be found, whatever the cost. Calculations based on the average gas price in 2008 (\$410 per 1000 m<sup>3</sup>) showed that the project could generate as much as \$30 billion revenue per year – but then came the dramatic drop in oil prices, to \$30 per barrel in December 2008, demonstrating the massive price volatility and the impossibility of making reliable short-, mid- and long-term calculations of the commercial viability of such projects.

The economic crisis has also resulted in a significant drop in demand for Russian gas in Europe, forcing Gazprom to reduce its gas production.<sup>3</sup> This lessened Gazprom's revenues, which were already suffering from the lower gas price on the European gas market, and forced the company to announce cuts in its ambitious investment programme.<sup>4</sup> Due to the lack of infrastructure, the surplus of gas cannot be shipped to other markets – like the Chinese – to compensate for the fall in European demand. As Russia has no LNG facilities near fields that produce gas for the European market, that option could not be used either. The global LNG market also seems affected by two recent developments – the current economic crisis, and – perhaps even more important in the long run – the increasing production of non-conventional shale gas in the USA, which should substantially reduce the US demand for LNG. As part of the gas from Shtokman was to be sent to the USA as LNG, this might also have negative implications for that project.

The last factor involved is the Gazprom's decision to cut its investments programme. True enough, Prime Minister Putin has announced that those cuts will not affect the development of the gas sector in Russia.<sup>5</sup> All the same, this may lead Gazprom to focus less on the challenging Shtokman field and to concentrate instead on the Yamal Peninsula, from which gas could be transported not only to Europe but also to China, as announced by Putin during his recent visit to Beijing. Such a change of focus could jeopardise the realisation of the Nord Stream: there simply might not be the gas to fill that planned pipeline.

*Jakub M. Godzimirski*

*Senior Research Fellow*

*Centre for Russian and Eurasian Studies*

*NUPI*

*Norway*

<sup>2</sup> The problems faced by Statoil in the Snøhvit field clearly illustrate how challenging technologically similar projects may be. For details on the latest developments there see <http://e24.no/boers-og-finans/article3387391.ece>

<sup>3</sup> <http://www.reuters.com/article/rbssEnergyNews/idUSLU3329520090930>

<sup>4</sup> <http://lenta.ru/news/2009/09/03/gazprom/>

<sup>5</sup> <http://lenta.ru/news/2009/07/13/cut1/>

<sup>1</sup> <http://pubs.usgs.gov/fs/2009/3037/pdf/FS09-3037.pdf>