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UKRAINIAN CRISIS: MIRE OF THE REGION

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ABSTRACT

Ukraine is one of the most important energy transit routes from Russia to Europe. This paper analyzes various recent complications and related geopolitics of gas transit to the European nations. It explains that how Ukrainian energy corridor of Russia has become a point of contention, where the United States, European nations, Ukraine and Russia have entwined with and ultimately imposed sanctions on each other. It shows a unique case of growing problems regarding Russian energy supplies to the Europe, but linked with other producer, consumer, supplier, and transit states as well. However, energy resources per se have paved the way to Russian resurgence and restoration in the new energy world order. War of sanctions vis-à-vis energy disputes has grappled Russia that spanned over various countries and regions in the very first decade of the 21st century. It puts energy as instrumental in the foreign policy behavior and geopolitical influence. It provides strength and leverage to the Russian 'state' in world politics and energy market as well. It has strengthened the hope to stride for new horizons as far as Russian energy market is concerned.

KEYWORDS: *Russia; Ukraine; Europe; Energy Geopolitics; Sanctions*

INTRODUCTION

For the last few years, the transit value has become a point of lurement, contention, or bargain with various regional as well as major world powers. Most recently, the Ukrainian crisis has translated this value in a geopolitical tug of war. Ukraine's relation with Russia as well as the European Union (EU) has been fluctuating since the 2004 Orange Revolution. Ukraine, the second-most populous former Soviet republic, and Belarus receive 56%-60% and 65% of natural gas import deliveries respectively from Russian sources (BP 2014).

However, via Ukraine; Bulgaria, Greece, Turkey, Macedonia and Romania receive gas through the three lines of Ananyev-Tiraspol'-Izmail & Shebelinka-Izmail (26 bcm/year); Romania by Hust-Satu-Mare (2 bcm/year); Hungary, Serbia, and Bosnia by two lines of Uzhgorod-Beregovo (13 bcm/year); Poland by the two lines of Komarno-Drozdowichi (5 bcm/year); and along with two lines of Dolina-Uzhgorod (17 bcm/year),Yamburg-Western border- Uzhgorod- (26 bcm/year), Urengoy-Uzhgorod (28 bcm/year), Orenburg-Western border-Uzhgorod- (26 bcm/year) pipelines supply natural gas to Slovakia, Czech Republic, Austria, Germany, France, Switzerland, Slovenia, and Italy. So, out of total existing Russian export capacity of 257bcm/year; Ukrainian transit route accounts for 142bcm/year, which is the highest of Russian supply to Europe. This intense transit corridor advantage placed Ukraine in a bargaining position with Russia as well as the EU. Russia sells gas at a lower price to transit states not only due to their transit value, but also to lure them to join the Russian dominated trade bloc (Soldatkin & Pinchuk 2011; Reznik & Meyer 2013).

The Belarusian transit corridor 'Kobrin-Brest' (especially for Poland) and Yamal-Europe (Torzhok-Kondratki-Frankfurt/Oder) supply natural gas to Netherlands, Germany, United Kingdom, Belgium, and Poland with a total capacity of 38bcm/year.

EXPECTATION AND TROUBLES

Having the aforesaid extraordinary transit value in the Russian gas trade with Europe, Ukraine expects some extra benefits and concessions from the Russian state monopolies. However, this value attracts many more geopolitical forces to manage Russia and contain its energy strength through Ukraine. Since the Orange Revolution (2004), serious trust deficit has been erupted in the Ukraine-Russia relations. Western efforts of regime change have been taken as a sinister game in the Russian neighborhood and an expansionist effort of North Atlantic Treaty Organization (NATO). The desire to drag and ultimately fuse Ukraine in the western block resulted bitterness in trade and transit affairs.

As was happened in 2006 and 2009; on June 15, of this year, Russia again cut off gas supply to Ukraine. However, Gazprom has been providing sufficient amount of gas to the Ukrainian pipelines which can meet the European requirements (i.e. 15% demand of the EU), but not the Ukraine's need. The Slovakian grid operator had confirmed where these pipelines arrive at the European Union, that they did not find any amount of reduction in gas pressure or import volumes (Bloomberg June 16, 2014). In fact, along with Ukraine's huge gas debt of $4.5billion, a price dispute has also been erupted between these two nations. Due to certain geopolitical reasons, the issue of new prices had become central to the disruption of natural gas to Ukrainian market. Moreover, various arguments regarding the new price mechanism of Gazprom ignore some facts. Carden (Oct. 3, 2014) reasonably points out that in 2009, Gazprom in an agreement had given the option to purchase natural gas on the short and medium term basis to the Naftogaz. Kiev was in agreement to purchase Russian gas at a considerable discount in the short-term; however, it was ready to pay (possibly) higher than market rate in the medium term. This high price was 'in return for lower than market priced gas in the 2009' and Ukraine owes $3.5-$5 billion in back payments. While, Noël, Pierre (Sep. 16, 2014) argues that Ukraine has received cheap and free gas from Russia by using its transit value and guarantee of supply Russian gas to Europe. It has bargained Russia for huge rents knowing that Moscow would not cut off the supply to its biggest market. In other words 'Europe has been and extremely useful hostage, allowing Kiev to abuse its power in negotiations with Russia.'

OFFERS, HOPES, AND ACTIONS

According to Igor Shuvalov, Russia will offer cheap gas if Kiev is ready to join the Moscow led economic block and close down the free-trade talks with the EU (Bloomberg Dec. 2, 2013). He further stated that "No one other than Russia can provide Ukraine with the necessary funds so quickly and in such quantity...A gas agreement could help relieve Ukraine of a huge problem. We can also give them a loan, but we will not help them without commitments on their part.'

On the other hand, though, President Viktor Yanukovych had reiterated 'European integration' as the country's goal; the dilemma prevailed. He had shown his bend towards repairing the economic ties with Russia by abandoning talks with the EU. The abandonment of the EU free-trade accord on 21st November, which was due to sign at the Lithuania summit on November 28-29, 2013, sparked aggressive public disapproval demonstration wherein protesters occupied Kiev city hall and Independence Square in December. Failing to sign the accord inspired various outside forces to fuel the protests. On Dec. 14, 2013 in Kiev, American Senators Chris Murphy from Connecticut and Republican Senator John McCain from Arizona addressed a massive crowd in support of overthrowing an elected government. Murphy told the gathering that 'You are making history...If you are successful, the United States will stand with you every step of the way.' While, McCain assured that 'American stands with you.' (Choiniere Oct. 5, 2014). These statements against a legitimate and democratically elected government were sufficient for the President Putin to assume the unrest as a charade, concocted, and carefully orchestrated western plot controlled by covert Central Intelligence Agency (CIA) and NATO forces to change the regime in their interests. More than 17% of ethnic Russian population of Ukraine was a big support for Putin's action. It is concentrated in the eastern and southern regions.

This led one of the fastest and startling courses of actions by Russia. The moment Mr. Yanukovych left the country on February 22; within a week pro-Russian forces seized various key buildings in Crimea, by all means, backed by the paranoid Moscow. Next week on March 6, Crimea's parliament voted to join the Russian Federation; voters chose to secede through referendum on March 16; Crimean parliament declared independence and formally applied to join the Russian Federation on March 17; and a decree signed by the President Putin to annex the Crimea on March 21, in Russia.

NATO Secretary-General Anders Fogh Rasmussen called this whole crisis as the '21st century revisionism.' However, if we add the story of Donbas(s) where following the developments in Crimea, the Luhansk and Donetsk Oblast declared them as the People's Republic on April 8 and held referendums on May 11, on the separation from Ukraine. Since then, pro-Russians are fighting against the Ukrainian forces for their autonomy where a claim of the Soviet identity has also played a significant role. This is a comfortable situation for Russians in which they can penetrate the eastern Ukraine from the south-west region. Along with Abkhazia and South Ossetia; the Crimean annexation has given a message to the West that they should keep their promises made at the time of Soviet disintegration regarding the NATO's expansion.

In spite of worsening situation in Ukraine, the fundamental strategy of the West in the leadership of the U.S. did not change. Russian actions were taken for granted. They adopted, if not completely hostile, an aggressive strategy of sanction and isolation to deal with Russia. At the very beginning of Ukrainian crisis; Barack Obama (March 3, 2014) indicated that if Russians 'continue on the current trajectory that they're on, that we are examining a whole series of steps – economic, diplomatic – that will isolate Russia and will have a negative impact on Russia's economy and its status in the world' and made strong support to the interim government of Ukraine. However, just after two weeks, Vladimir Putin (March 18, 2014) reminded "a whole series of controlled 'colour' revolutions" and a policy of few western powers; i.e. 'who is not with us is against us'. He further stated that Russia would 'always defend the interests of ethnic Russians and Russian-speakers in Ukraine by political, diplomatic, and legal means.' In support of Crimea's accession, he said 'Together we have done a lot, but a lot more remains to be dome, more tasks to resolve.' It was read in a different manner by Russia's immediate neighboring countries including Ukraine and the West collectively.

SANCTION POLITICS

Various developments led the United States and EU to impose sectoral sanctions against Russia which includes military industrial complex and various sectors of economy. Since March 2014, blocking property and visa bans have been imposed on certain government officials. The U.S. Treasury Department's Office of Foreign Assets Control (OFAC) and the U.S. commerce Department's Bureau of Industry and Security (BIS) have identified those people who are involved or can contribute to the Ukrainian crisis. Their Specially Designated Nationals (SDN) List include people and entities connected with energy industry like Igor Sechin- President of Rosneft, Gennady Timchenko- owner of the Volga Group, which is a financier for energy sector, pipeline construction company Stroytransgaz, Transoil, and United Shipbuilding Corporation that is involved in shipbuilding for the energy industry. Newly imposed sanctions include restrictions on export of oil and gas related items for deepwater, Arctic offshore, and shale projects in Russia. However, European Union imposed sanctions on energy related transactions suited for deepwater oil exploration and production, Arctic oil exploration and production, shale oil projects in Russia. Transfer of high technology and technical supports are also restricted (Savage C. et al. Sep.11, 2014). The impact was seen in the state controlled Rosneft's call for state aid as well. Russian largest oil company has sought 1.5 trillion rubles ($42 billion) to come up against the new challenges of imposed sanctions. "Igor Sechin has asked the Kremlin to authorize a payment from the National Wellbeing Fund-used to plug deficits in the pension system-to buy Rosneft bonds" (Kolyandr 2014).

The U.S. targeted Russia's oil and gas industry, which holds the most strategic nature and significant in the geopolitics of current world order. The Treasury of the United States has barred Novatek and Rosneft from the long term American capital markets. However, a person like Timchenko has taken these sanctions in respect of the Russian national interests. In his opinion, this could create certain difficulties, but as compared with safeguarding the national interests, these are not so huge and unbearable. For example, the Kremlin controlled Rosneft oil group has taken a huge sum of debt to finance $55 billion acquisition of BP's Russian joint venture—TNK[1]-([1] It was a major vertically integrated Russian oil company headquartered in Moscow. It was Russia's third-largest oil producer and among the ten largest private oil companies in the world.In 2013 it was acquired by Russian oil company Rosneft.)BP (Tyumenskaya Neftyanaya Kompaniya, Tyumen Oil Company – British Petroleum). Much of this debt is a short term loan. Only $20 billion of debt has to repay by the end of the 1st quarter of 2015. Since, "the company has about $20bn of cash on its books, after receiving upfront payments for oil under long term contracts from China's CNPC, Glencore and others" the risk to its liquidity is minimum. It would "use these payments to finance the upcoming debt maturities. Even without them Rosneft would have a lot more flexibility than most other big companies. It generates oodles of foreign currency from the sale of its oil... It also has privileged access to financing from state banks... it could also postpone some of its big projects to reduce the need for new loans". Similarly, "Novatek, Russia's largest independent gas producer is also sitting pretty. It has a

$350 m syndicated loan falling due within the nest 18months, but generates enough cash flow to repay it in full if refinancing proves impossible. Like Rosneft it can tweak its capital expenditure programme to conserve cash if it has to" (Chazan 2014).

On September 11, a White House press release had given the resolve to impose mounting costs on Russia. And the U.S. will deepen and broaden sanctions in Russia's financial, energy, and defense sectors, which will increase political isolation and economic costs to Russia. However, even after the downing of Malaysian Flight MH17, EU has crafted sanctions very carefully where it has to share the burden on all 28 states as well as to protect specific interests of the Union. These sanctions 'restrict Russia's access to EU capital markets...Ban future EU exports and imports of arms and related materiel...Prohibit sales of dual-use goods and technology for Russian military end-users...(and) Ban sales of certain oil exploration equipment and technology'(Archick & Mix Sep. 16,2014). Though, Obama stated that new combined EU-US measures would 'have an even bigger bite'; these sanctions are not fully harmonized. Both have some crucial variations on services, projects (oil exploration), and Russian individuals or otherwise; e.g. certain oil exploration services have been restricted by the EU only to the future contracts; i.e. contracts ratified after August 6, 2014, which is not with the U.S. concurrence, where sanctions are applied retroactively to the contracts signed before they were put in place (EPIC Aug. 2014).

However, even the caution of the European Union on sanctions could not bring off certain large entities of Russia; e.g. oil companies Rosneft, Transneft, Gazprom Neft; defense groups Oboronprom, Uralvagonzavod and the United Aircraft Corporation; and banks include Gazprombank, Sberbank (Russia's largest), VTB Bank (Bank of Moscow), Vnesheconombank (state development bank), Rosselkhozbank (agricultural bank). Morgan Stanley assumes that its shale production and virgin Arctic fields are at risk, while Barclays assess a declining production ratio in 2015. In light of these sectoral sanctions, International Energy Agency's (IEA) recent oil market report (August 12, 2014) has assessed that "EU sanctions are highly selective, exclude agreed contract, and can only be extended past one year by consensus. Their 'perimeter' seems loosely defined, potentially leaving room for finding ways around the most constraining measure." It further elucidates that 'Neither set of sanctions will have any tangible near term impact on supplies. Even for medium term, their impact appears questionable.'

These sanctions have one more intriguing as well as interesting aspect of ambiguity. If, on the one hand, the U.S restrictions are applicable to both oil and gas production, the EU does not include gas sector and Gazprom. The separation of oil and gas industry is simply hostage to energy dependence of Europe where more than 30% requirements are met by Russia. This division further helps Russia to import machinery and specialized equipments for unconventional gas production. In fact, it is difficult to distinguish shale oil production equipments and shale gas apparatuses. The similarity of purpose makes restrictions blunt regarding unconventional oil extraction. Similarly, joint ventures of Russian oil companies enjoy some other waivers from existing sanctions regime. Therefore, existing ambiguity and differences in the nature of sanctions impede and undermine the impact as well as reduce the effectiveness of the same.

Therefore, it is apparent that Europe is not that much aggressive and keen to punish Russia as the U.S. desires and wish for bashing Vladimir Putin. Along with major banking institutions, sanctions list of the U.S. Treasury Department includes Gazprom (Neft), Transneft, Lukoil and Surgutneftegas, it certainly troubles the European minds. The difficulty, difference, and dilemma of (re)action have been appeared at various stages. It is not only confined to the split between the continental and island states in Europe, but also carving up nations among the least and most energy dependent countries. Since, financial and military concerns vary from state to state; the approach and willingness to comply with the intensity of sanctions are different. Though, the geography has a role to play; it does not guarantee to stick up for the neighboring voice. Neither the Scandinavian countries nor Visegrad states have a single stand, albeit they belong to a separate regional (geographical) entity. In fact, simply by using the phrase 'European Union' does not reveal their united or monolithic structure and neither has it represented their unified singular stand against Russia.

However, in the given complex scenario, as far as Russia per se is concerned, the banking institutions and access to the debt finance is a major concern for big companies. Though, Guy Chazan, energy editor at the Financial Times wrote that "access to debt finance is only part of the problem. What could prove more of a headache is the EU and US restrictions on the export of technologies used in Arctic, deepwater or shale oil exploration. That is a smart weapon trained directly at Russia's future. Production from the ageing workhorses of the country's oil industry – the vast conventional oilfields of western

Siberia – is dropping off sharply. Moscow is determined to offset that decline by pushing beyond frontiers, such as into the oil-rich Arctic oceans and Siberia's vast Bazhenov shale, and by investing in multibillion-dollar liquefied natural gas ventures in the Yamal peninsula and Sakhalin island". He further explains that "such ambitions are crucial for Russia's economic health, with proceeds from oil sales accounting for 44 per cent of budget revenues. It is a cash cow Moscow cannot do without. But branching into such areas requires access to western technology, capital and expertise. Russia does not need western kit to produce conventional oil – it has been pumping crude from its onshore fields for more than a hundred years. But it is unclear how it can exploit its shale oil reserves without sophisticated western fracking equipment. And it does not build the kind of offshore platform that will be required in places such as the Kara Sea, where Rosneft and ExxonMobil started drilling their first well.... Exxon's well is unaffected because its rig was contracted before the latest sanctions were announced". Moreover, Morgan Stanley opined that "Russia would be producing an extra 250,000 barrels a day from its shale deposits and virgin Arctic fields by 2018 – which it says are now at risk. Barclays thinks production will fall in 2015, dragging non-OPEC supplies down with it" (Chazan 2014).

CONTRADICTIONS AND AMBIGUITIES

Europe and its growing united force (?) have many contradictions in the newly born structure as well as ambiguities in the policy formation not only to deal with Russia, but also to poject itself in the emerging world order. Norway and Iceland, two North Atlantic Treaty Organization (NATO) member countries, do not have the EU membership; however, Sweden and Finland, two EU member states are not NATO nations in the Scandinavian region. While Denmark has a membership in both organizations but Greenland has none. This antipodal stand has been reflected in their approaches toward sanctions against Russia as well. Though, at first, Norway had some tough stand on Russia, but later on, it did not favor for a strong presence of NATO in Ukraine. Initial sanctions hit them harder than several other nations because of a ban on the transfer of high technology for Arctic, deepwater, shale production and exploration, in which it has been deeply involved more than many other states. It is the biggest oil and gas producer in Western Europe and have sovereign wealth fund of $860 billion. This fund has stopped trading in Russian market which held roughly $8billion in stocks and bonds at the end of 2013. Sweden and Finland has taken a tough stand due to security concerns in Baltic region. In addition, Georgia, Poland and Ukraine are also playing their role behind the tougher stand of Sweden. The vocal support of conservative factions to Kiev has some sort of sub-organizational characteristics and obligations in addition to the loyalty of political elites. It is known that Sweden was persuaded by Poland for its Eastern Partnership (EaP) program, wherein three Caucasus republics; i.e. Armenia, Georgia, Azerbaijan, along with Belarus, Moldova and Ukraine were involved. Since, these six post Soviet Union republics set out an east European expression, and Russia purported the program as a measure to expand the sphere of influence in search of oil; Sweden at least made a difference in its regional manifestation. However, an open support to Kiev was not only debated and criticized in Sweden and Finland, but also reduced the process and thinking of getting membership of NATO in light of Ukrainian crisis.

Poland, along with Baltic States Lithuania, Latvia, and Estonia, alleges Russia that Ukrainian crisis is an act of aggression against a sovereign state. Polish government may have their own agenda but the skepticism of Baltic republics lie around their demographic distribution. Though, Lithuania has a marginal 6.3% ethnic Russians; Latvia and Estonia have sizable inhabitants in their total population; i.e. 26.9% and 25.6% respectively. Thus, size of territory, population, and energy dependence (Lit. 92%, Lat. 72%, Est. 69%) make them worry when Russia emphasizes to protect the interests of its compatriots anywhere in the world. However, in spite of the huge energy dependence (91%), Poland has taken a strong stand. In fact, its yearning for creating a sphere of influence in Eastern Europe brings back various ideas and programs like EaP and Visegrád Four/Group (V4).

V4 comprises of four Central European nations-Poland, Hungary, the Czech Republic, and Slovakia. Poland's hawkish approach stands isolated on sanctions against Russia in this group. Other three states do not perceive Ukrainian crisis as a threat to the Central Europe. Slovakia understands sanctions are unnecessary and harmful, while Czech does not view Russian actions in Ukraine (Crimea and Donbass) as invasion but a civil war. However, in spite of having some cultural connections and issues regarding Hungarian ethnic minority in the southern Ukraine, Hungary goes by neutrality. Likewise, Romania has its Moldavian cultural concerns in addition to the diaspora in Ukraine; hence, it has not taken a firm stand on various issues. Nonetheless, when dovish actions and approaches of these three nations have been criticized strongly, it is worth reminding that China has adopted more favourable stand for Russia. Its support has not been targeted with the same intensity for the same reasons. However, natural gas dependence of these smaller states provides sufficient reason to take that status-quo like stand for their domestic peace and stability.

In addition, by the first week of October, Russia has started to manage its gas supply for some European states where complaints of reduced supply has been registered by Slovakia and Poland in particular. Interestingly, along with Hungary, these states are making reverse flow of natural gas to Ukraine, when Russia had cutoff its supply in June. At the same time, they are criticizing Russia for making gas as a tool in a political fight where it has become an instrument of political posturing. However, most recently, European Commission has managed to put forward a deal between Russia and Ukraine wherein Ukraine has to pay $3.1 billion of debt with the arrangements of pre-pay for gas month by month at above market rates until April in return for 5billion cubic meters. But the Ukrainian distributor Naftogaz requires 5bcm additional supply from Russia to keep EU supplies uninterrupted, if they do not receive reverse flow of natural gas. Though, the German Chancellor Angela Merkel and EU Commission chief Jose Manuel Barroso have urged Vladimir Putin that Russia should not escalate the gas war; Andrew Rettman (Oct. 2, 2014) quoted the former German chancellor Gerhard Schroeder, working for Gazprom, that the European Union should take back economic sanctions to improve the situation and Russia sanctions are "wrong... I want to say that loud and clear." The stand and voices of these two Chancellors reminds Henry Kissinger (2014), who very recently said that "The economic system has become global, while the political structure of the word remains based on the nation-state", which is probably the best explanation of energy geopolitics and the Russian dilemma of economy and status.

CONCLUSION

Every state takes various measures to ensure a safe and affordable supply of hydrocarbons. They are involved in a complex market mechanism to build a delivery system. However, the natural strength of hydrocarbon endowments provides a peculiar strength to the Russians that propel them to strive for a new status in world politics. The geopolitical uncertainties of oil and gas exporting nations and limited access to international oil companies in major oil and gas fields either in Russia or in the CIS region have created a new equation in the demand-supply mechanism. Major consumer countries are finding themselves in a tough and competitive position to obtain strategic resources.

The Chinese and U.S. interests in the region make Russians cautious about their short and long term moves. American arms and troop's assistance to Georgia is not going to be ignored. No need to highlight the real intentions and expansion moves of NATO. This entire scenario constructs a 'Russian perception' that instigates them to explore their new sources of power. Undoubtedly, apart from defense deals that are directly connected to their military industrial complexes; they find solutions in their energy resources.

Therefore, either it is Europe and the CIS region or East Asia; they are ready to use the power of energy resources to acquire their lost status in world politics along with strengthening their economy. No one should get amazed by their moves. If it is a question of perspective and national interests, things would become natural and expected one. However, it would be farcical to expect philanthropy from a major power in a world where 'I', 'Me', and 'My' comes first.

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