

Chairing the G8

Russian Energy and Great Power Aspirations

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At the start of 2005, Russia hit a low in its international relations. Awkward interference in the Orange Revolution in Ukraine resulted in serious tensions with the European Union. The Bratislava summit was marked by little of the old chemistry between Presidents Vladimir Putin and George W. Bush. In the Organization for Security and Cooperation in Europe, Russia again found itself in a minority of one. Russia's external profile also suffered from internal setbacks, such as the revolt of pensioners over proposed reforms to the social benefits system, and the obvious disorganization of decisionmaking after the sudden death of Askar Akayev's regime in Kyrgyzstan. At that point, many experts and politicians questioned the rationale for Russia's participation in the G8, and the possibility that Russia would become its chairman looked like a joke.

Half a year later, Russia's international standing has strongly recovered, albeit with little effort on the part of its leadership. The inexorable rise in oil prices was a major factor behind Russia's rehabilitation, but not the only one. Helping to improve Russia's relative status in the G8 even more was the series of setbacks other members experienced: the French leadership was disorganized after losing the European Union constitutional referendum; Germany was preoccupied with parliamentary elections that then produced an unstable coalition; Tony Blair's hopes for setting the ambitious agenda for its G8 chairmanship were undermined by the London terrorist attack; and the Bush administration, in addition to mounting problems in Iraq, was hit by

Hurricane Katrina.

President Putin regained his confidence step-by-step, beginning with an encouraging April meeting in Moscow with U.S. Secretary of State Condoleezza Rice. He unambiguously supported Aleksandr Lukashenko, known as the last dictator in Europe, against revolutionary pressure from Belarus' western neighbors. He then provided invaluable support to Islam Karimov, effectively shielding him from demands to conduct an international investigation of the May bloodshed in Andijon. Moscow's position on Iran's nuclear program became less and less helpful for the efforts of the European *troika* of Germany, France, and the United Kingdom. Much-advertised joint military exercises with China in August were followed by exercises billed as counterterrorist in Uzbekistan in September. Putin's August participation in a flight on a strategic bomber was personally a great confidence booster for the Russian president, who in September bragged publicly about new generation strategic missiles "invulnerable to the strategic defense that is developed by some of our partner-states."

Speaking at the United Nations General Assembly in September, Putin showed no regret about the UN's lack of reforms, which effectively ensured for Russia ongoing status as one of the organization's top five members. Given this situation, who would possibly challenge Russia's right to preside over the very exclusive G8? The question may be rhetorical, but it is still worthwhile to assess how much Putin's agenda for Russia's chairmanship of the G8 may diverge from the aspirations of other members, disunited as they are at this juncture.

Energy Security and the Oil Weapon

During the G8 summit at Gleneagles, Scotland, in July 2005, Putin's announcement that one of the main themes of Russia's chairmanship would be energy security did not capture much attention. The topic appeared relatively uncontroversial and fit nicely into the current political priorities of the industrialized nations. However, at the September meeting of the financial G7 (a grouping of finance ministers in which Russia is not a participant), a less perfect fit of agendas became apparent. Making a spot estimate of the global damage from Hurricanes Katrina and Rita, the seven ministers (broadly supported by the IMF and the World Bank) expressed serious concern that oil prices at a level of \$70 a barrel would have a detrimental impact on global economic growth. Russia, seeking to boost its status as an observer in the G7, duly asserted that it would continue to increase its oil exports in order to stabilize prices.

It is, however, difficult to score cheap points among professionals through unsubstantiated statements. Russian oil policy is in reality entirely consistent with the position of OPEC, which earlier in September had decided to maintain the same level of production as before while affirming an absurd commitment to an optimal price corridor of \$25-28 a

barrel. In fact, Russia has abandoned its caution with regards to budgetary planning and now aims to massively increase domestic spending on the basis of its oil dividend. The World Bank explicitly warned Moscow against such a relaxation of financial discipline. Many Russian experts predict that this spending spree will have multiple negative impacts, including galloping inflation. Nevertheless, Putin remains personally committed to his social initiatives which, strictly speaking, require that oil prices continue to climb towards the mind-boggling level of \$100 a barrel.

Defying classical patterns of Dutch disease (whereby countries dependent on the export of natural resources ultimately erode their economic competitiveness and well-being because of appreciation of their natural currency), Russia's oil industry is not showing symptoms of overdevelopment despite the fact that the country is becoming increasingly dependent on revenues from its energy sector. On the contrary, a significant decline in investment activity has been registered over the last few years, leading to stagnation in production. Up to October 2005, Russian officials were promising a 3 percent increase in crude oil production, although it was clear that 2.5 percent was the maximum possible; in 2006, it is going to be problematic to achieve even that. These figures are significantly lower than the guidelines in Russia's 2003 Energy Strategy.

The main reason for this slower increase is the gradual re-nationalization of the oil industry. It began in mid-2003 with the concentrated attack on Yukos, Russia's largest oil company, and the confiscation of most of its assets in favor of the state-owned Rosneft. The next step was the September 2005 purchase by Gazprom of Russia's sixth-largest oil company, Sibneft, which will secure for the state control of over a third of Russia's total oil production. Another leading oil company, Lukoil, prefers to invest its profits abroad, particularly in Kazakhstan, while a fifth, Surgutneftegaz, just accumulates cash. No company is investing in refineries. This unprecedented stagnation in an industry awash in profits may someday be called the "Russian repercussion."

The picture looks significantly different in the natural gas sector, where Russia is seeking to advance strategically. Russia is making full use of the unique advantages it enjoys through its possession of the bulk of the world's natural gas reserves and its control over the export routes of other producers such as Turkmenistan. Gazprom has opened new export channels to Turkey and Europe and is now finalizing plans to construct a new high-capacity pipeline under the Baltic Sea.

The political decision not to reform Gazprom and to encourage its expansion into the oil sector, however, has brought an inevitable decline in this energy giant's efficiency. In the last three years, Gazprom's investment plans have been repeatedly subject to radical revision and reorientation, and the accumulated debt of the company has been growing

even faster than its market capitalization (which surpassed \$100 billion in early September). New gas fields have been developing too slowly; the largest project, offshore Shtockman in the Barents Sea, will not come on line any sooner than early in the next decade.

Thus, in essence, Russia has very little to contribute to the West's short-term energy security. Moscow shows little concern about its stalled energy dialogue with Washington. Russia's longstanding discussions with Beijing, Tokyo, and New Delhi have been equally unproductive. While Russia might not be expected to deliver on any of its promises in the short-term, it will have to make certain choices in order to fulfill at least some of them in the long-term. The pressure of Russia's unreformed energy quasi-market will only grow, and that increases the insecurity of the global energy balance.

Moscow has been very careful to avoid any politically damaging abuse of its oil power; many predictions regarding its predilection for blackmail, focused mostly on the recently ended monopoly on transporting Caspian hydrocarbons, have not come true. However, the Russian leadership, even if it prefers gentle persuasion, plays into the hands of those oil producers who are currently reevaluating the potential for the weaponization of Russia's energy resources. Oil that is priced at \$70 a barrel makes a weapon of much greater destructive (or, for that matter, deterrent) power than one would have thought just a couple of years ago. Western, as well as Chinese and Indian, economies have shown remarkable resilience to the repetitive shock of upward mobility in oil prices. This resilience has a limit, however, which has yet to be tested. It is impossible to predict when Europe's sluggish economic growth will worsen, or which new increase in the trade deficit will trigger a massive correction of the dollar, but such vulnerabilities are visibly on the rise. Moscow is unconcerned about such economic disasters-in-the-making and, apparently, expects that explosions, strikes, and hurricanes will continue to boost its budget revenues. So much for energy security.

Counterterrorism and Counterrevolution

Joining forces in the fight against international terrorism has been one of Putin's favorite topics ever since he arrived in the Kremlin on the Chechen war ticket. He gave it prime attention in his September 2005 speech at the UN General Assembly, and the London terrorist attack, timed to coincide with the G8 summit at Gleneagles, has made terrorism a very appropriate theme for Russia's G8 chairmanship. Indeed, Putin has already achieved his main goal in exploiting this theme: Western criticism of the conduct of the war in Chechnya has been reduced to a negligible whisper.

But while Putin might simply want to consolidate this achievement, he has also sought fit to stretch the terrorist theme to cover a challenge that worries him greatly: color revolutions. The political theory advanced by the Kremlin is quite elementary. Instability in post-Soviet states is

generated by political extremism of various stripes, and this extremism naturally mutates into terrorism. Terrorism, in turn, is organically linked to international terrorist networks. It was problematic to apply this scheme to post-revolutionary Georgia, but Georgia has nevertheless been implicitly threatened by Russia with preventive strikes. In the case of Orange Ukraine, which continues to be the main obsession of Putin's political ideologues, the Kremlin has obviously been unsuccessful in applying the theory. In Kyrgyzstan, Moscow has firmly embraced the country's new leadership.

The only place where it is at all possible for Moscow to try and demonstrate a link between revolutionary activities and terrorism is Uzbekistan. Moscow firmly asserted that the May uprising in Andijon was a terrorist attack organized by militants based in Afghan camps. Russian Defense Minister Sergei Ivanov insisted on this interpretation at a meeting of the Russia-NATO Council, and he later personally supervised the first Russian military exercises in Uzbekistan, even mentioning Russia's possible interest in the K2 airbase, scheduled to be evacuated by U.S. forces.

The instrumental character of Russia's thinly-supported explanation of the Andijon events is obvious. Ruling regimes in Central Asia, increasingly connected with Moscow, eagerly subscribe to it. Putin spends a great deal of time meeting with them, seeking to strengthen their readiness to suppress supposedly terrorist groupings that pose as nongovernmental organizations and thus make certain that the revolutionary tide has indeed been turned. A series of joint counterterrorist exercises staged in Central Asia this autumn was intended to confirm that Russia could provide direct support to local regimes in case of an emergency and not only airlift a desperate former leader-for-life to his retirement retreat.

Moscow hardly harbors any illusions about the persuasive power of this counterterrorist theory over its Western partners. As Putin was performing ritual hugs at the Russia-EU summit in October, the EU announced the unilateral termination of its partnership agreement with Uzbekistan because of its refusal to permit an international investigation of the Andijon events.

Nevertheless, Moscow has proposed to make political developments in the post-Soviet space a key theme of its G8 chairmanship. The focus of this exercise in building a common understanding is not likely to be Central Asia, where Russia now feels rather confident, but Belarus. Moscow has committed itself to supporting Belarus' unashamedly authoritarian leader Aleksandr Lukashenko, now under serious pressure from the West. The opposition in Belarus is clearly much weaker than in Ukraine, and the September explosion in Vitebsk demonstrates that a terrorist connection to any potential revolutionary events in Belarus could easily be organized.

Putin has made several warnings about the risks of exporting democracy and wants to impress upon his G8 counterparts that Belarus, as Russia's key ally, is off limits, whatever the personal failings of its leader.

It is entirely possible that an agreement to disagree can be reached on this issue, but unproductive debates will hamper discussions on other terrorism-related problems, including nuclear proliferation, a topic on which several promising joint projects are in progress.

Conclusions

Russia will be quite content with a G8 chairmanship low on content and heavy on public relations, as it expects that the fact of its formal leadership in this exclusive club will provide a sufficient boost to its international profile. Other members, including the United States, may accept this as well, as they will assume that a public quarrel with Moscow will not help at all to overcome multiple global troubles.

The problem, however, is that some of these troubles may acquire a scale or character that will require concerted action. Oil shocks, terrorist attacks, or revolutionary uprisings cannot be postponed for a year. Every attempt to forge a consensus in the face of a newly-exploding crisis will inevitably expose the real scale of divergence between Russia and the rest of the G8. Whatever Putin's personal aspirations as an enlightened and Westernized ruler, the anti-democratic evolution of his regime has determined the key content of Russia's foreign policy. Faking cordial entente is often a useful political tactic, but sometimes even politicians need to get real. And in real terms, Russia and the rest of the G8 are on different sides of too many political barricades.