

## 7 EURASIAN INTEGRATION AND THE ENERGY FACTOR: WHERE DOES THE EAEU STAND?

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The availability of vast hydrocarbons reserves represents one of the key geoeconomic and geopolitical assets of the Central Eurasian area (CEA).<sup>1</sup> Hence, it goes without saying that it is almost impossible to discuss Eurasian politics and economy without making reference to the energy sector.

Through the 20th century, the growth in international consumption of fossil fuels – and, therefore, the steady rise in their geoeconomic and geopolitical relevance – overlapped with the Central Eurasian history’s key watersheds. From World War I to World War II, from the establishment of the Soviet Union to its rise as the fulcrum of the ‘Eastern bloc’, from the detente to the demise of the Soviet Empire and the birth in its place of 15 independent states: all these events were partially shaped by the energy needs and the energy policies of its protagonists.

Generally speaking, the sector’s relevance to regional cooperation derives primarily from the role it played in the Soviet Union’s state-building process. That is, having inherited the exploration and production assets already exploited under the Imperial rule in the Southern Caucasus area, the Soviet leadership ever since the 1920s sought to base the industrialization of the Union upon the successive development of oil and later gas fields in the Caspian, Volga-Urals and Western Siberian areas. Besides the efforts undertaken in the upstream sector, Soviet energy policy entailed a massive construction project in order to ensure an efficient midstream and downstream network, consistently within the specialization logic underlying Union’s economic architecture. Accordingly, the Soviet Republics – whether producer, transit or consumer states – were bound together by a massive pipeline network, the so-called Unified Supply System (USS): at the time of the dissolution of the USSR the gas transport network totaled 220,000 km of pipeline linking over 200 gas fields, while the oil pipeline network amounted to 64,000 km.

The development of the Soviet energy policy and the connected construction of the Unified Supply System had far-reaching consequences, both domestically and externally.

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1 For the sake of this chapter we identify the Central Eurasian area with most of the former Soviet Union one – *i.e.* with the Republics which gained independence following the USSR dissolution minus the Baltic states, which completed the process of integration in the Euro-Atlantic structures.

From the first perspective, it ensured a vital source of foreign currency for the state budget, serving simultaneously as a privileged tool to attract foreign know-how and technology, with a goal of efficiently exploiting the resource base and modernizing national assets. Thus, the USSR worked as a vehicle for modernization as well as an incentive and tool for intra-Union cooperation. From an external point of view, hydrocarbons stood simultaneously as a privileged vehicle for cooperation with foreign interlocutors and costumers, both within and outside the Socialist block. Therefore, besides its economic benefits, the energy sector provided Moscow with an invaluable geopolitical factor over the three concentric regional circles of cooperation linked by the oil and gas pipeline networks: the Soviet Union itself, the Eastern European Socialist block and the wider European area.

The economic and geopolitical relevance of the sector went unaffected through the dissolution of the USSR, as it remained a key driver behind interstate relationships inside and outside the CEA. In the post-Soviet era, however, intra-CEA energy relations have been characterized by a constant dialectic between cooperation and competition, as well as between integration and disintegration trends. This ostensible contradiction is rooted in the conditions under which interstate energy relations took shape after 1991 – and a better appraisal is helped by making a comparison with conditions characterizing the post-WWII Europe.<sup>2</sup> While in the latter case energy cooperation developed in a highly fragmented context, on the contrary post-Soviet CEA was bound together by the functional interdependencies inherited from the USSR economic and industrial system. Therefore, although in both cases political considerations played a central role in encouraging energy cooperation, in the European scenario they worked unequivocally by fostering a drive toward the deepening and broadening of the cooperation itself, whereas in the post-Soviet context they resulted in more nuanced – if not ambiguous – attitudes among its participants. This was essentially the result of the power asymmetry characterizing the post-Soviet space in the aftermath of the USSR dissolution, *i.e.* a power imbalance that threatened to revive the colonial relationships between the center and the periphery that were typical of the Soviet (and Imperial before it) system – a connotation clearly absent in egalitarian relations among the protagonists of the European project. These attitudes resulted in a dichotomy between the *need* for cooperation among post-Soviet actors and the *will* of the junior partners to make the development of energy cooperation a tool to enhance independence and sovereignty, avoiding the risk that the sector might become a vehicle for reintegration into the Soviet imperial structure.

*Mutatis mutandis*, this dichotomy persists in the case of the Eurasian Economic Union (EAEU), *i.e.* in the latest and most advanced framework for integration in the CEA. On

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2 The relevance of the comparison between CEA and post-World War II Europe results primarily from the centrality taken on in both integration processes by the energy sector. Moreover, the European integration process has traditionally been a reference point and a model for cooperation and integration framework in the CEA – since the 1993 Economic Union proposed by Russia till the EAEU itself.

this backdrop, the aim of the chapter is precisely to appraise the role played by the hydrocarbons sector for the Eurasian integration project – and particularly for the EAEU – with a focus on appraising the balance between integration and disintegration trends and, ultimately, to understand whether the sector may be considered a centrifugal or, rather, a centripetal force. In order to do so, after having introduced the key geoeconomic and geopolitical features of the regional energy sector, the chapter will analyze both internal and external forces influencing energy cooperation in the CEA. From the first perspective, it will appraise the EAEU experience in the light of the main characteristics manifested by regional energy cooperation since its inception. Successively, the chapter will focus on the external dimension of energy cooperation in order to evaluate the current and foreseeable prospect for interaction and cooperation with third actors with an aim at understanding whether the latter tend to play an incentive or rather a disincentive role for the regional integration in the CEA.

### 7.1 CENTRAL EURASIAN AREA KEY ENERGY FEATURES

The Central Eurasian area today stands as a key hub in the global arena in the production and export of hydrocarbons. Possessing around 8.2% and 28.7% of the world proved reserves of oil and gas, it jointly accounts for the 15.7% and 21% of their annual production (see Table 7.1).

**Table 7.1 Oil and Gas reserves and production in the CEA and EAEU area (2015)**

Country	Oil Reserves	World (%)	Oil Production	World (%)	Gas Reserves	World (%)	Gas Production	World (%)
Russia	102.4	6.00	10,980	12.40	32,300	17.30	573.3	16.10
Kazakhstan	30	1.80	1669	1.80	900	0.50	12.4	0.30
Turkmenistan	0.6	-	261	0.30	17,500	9.40	72.4	2.00
Azerbaijan	7	0.40	841	1.00	1100	0.60	18.2	0.50
Ukraine	-	-	-	-	600	0.30	17.4	0.50
Uzbekistan	0.6	-	64	0.10	1100	0.60	57.7	1.60
<b>Total EAEU</b>	<b>132.4</b>	<b>7.80</b>	<b>12,649</b>	<b>14.20</b>	<b>33,200</b>	<b>17.80</b>	<b>585.7</b>	<b>16.40</b>
<b>Total CEA</b>	<b>140.6</b>	<b>8.20</b>	<b>13,815</b>	<b>15.70</b>	<b>53,500</b>	<b>28.70</b>	<b>751.4</b>	<b>21.00</b>

Oil reserves in thousand million barrel; oil production in thousands of barrels per day. Gas reserves and production in billion cubic meters.

Source: BP Statistical Review of World Energy (2016).

Thus, the availability of vast hydrocarbon reserves stands as a pivotal geoeconomic and geopolitical asset to the regional actors. Therefore, among newly independent producing states, it is no wonder that the exploitation of energy potential became the most relevant pillar upon which to base the difficult process of post-Soviet transition. As a matter of fact, it served not only as a tool to get out of the economic hardship following the USSR dissolution, but also as a vehicle to build consensus *internally* while improving geopolitical relevance *vis à vis* consumer countries *externally* – a ‘double legitimizing role’ of the energy sector, which provided regional producing countries with a typical *petrostate* posture.<sup>3</sup> Moreover, the domestic linkage between energy policies and state-building processes went as far as determining an overdependence on the sector in both economic and political terms, connoting producing countries as *rentier states* – *i.e.* states “reliant not on extraction of the domestic population’s surplus production but on externally generated revenues, or rents, such as those derived from oil”.<sup>4</sup>

Yet, as far as the interstate cooperation potential enshrined in the energy sector is concerned, the availability of wide hydrocarbon reserves is not the only geopolitical factor to take into consideration. Subsoil wealth as a source of power and positive geopolitical asset has indeed to be balanced with a limiting one, given by the landlocked condition shared by most, if not all, the regional producing countries.<sup>5</sup> Such a condition implies that, in order to translate the extractive potential into economic and political advantages, the producing states need to interact and cooperate with the transit ones, with a focus on covering the physical distance toward consuming countries.

The landlocked condition has three relevant and connected consequences for the development of regional cooperation schemes in the energy sector. First and foremost, it

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3 As per the concept of petrostate, see M.I. Goldman, *Petrostate: Putin, Power, and the New Russia*, Oxford University Press, New York, 2008. See also L. Alieva, ‘Azerbaijan: Power in the Petro-State’, in M. Emerson & M. Youngs (Eds.), *Democracy’s Plight in the European Neighbourhood: Struggling Transitions and Proliferating Dynasties*, Centre for European Policy Studies, Brussels, 2009, pp. 112-119.

4 L. Anderson, ‘Policy-Making and Theory Building: American Political Science and the Islamic Middle East’, in H. Sharabi (Ed.), *Theory, Politics and The Arab World: Critical Responses*, Routledge, New York, 1990, p. 61. As per the rentierism in the CEA’s country, see R. Auty & I. de Soysa (Eds.), *Energy, Wealth and Governance in the Caucasus and Central Asia. Lessons Not Learned*, Routledge, Abingdon, 2006. See also P. Jones Luong & E. Weinthal, *Oil Is Not a Curse. Ownership Structure and Institutions in Soviet Successor States*, Cambridge University Press, New York, 2010.

5 Although the only regional producing country being strictly land-locked is Uzbekistan, nevertheless the other exporting countries present the main features of land-lockness. As far as the Caspian littoral states are concerned, the access to the Volga river does not exclude them from the mentioned category. Indeed, as Glassner noted, the latter includes those states “which have access to the sea via internationalized navigable rivers [...]. Such states exhibit some of the characteristics of coastal states, but consider themselves land-locked and are here considered land-locked because they do not exercise ‘sovereign’ control over their aqueous highways to the sea”. I. Glassner, *Access to the Sea for Developing Land-Locked States*, Martinus Nijhoff, The Hague, 1970, p. 2. At the same time, although not strictly being a land-locked country, Russia itself shares some of the limitation typical of these countries, due to the lack of direct access to ‘warm seas’ as well as to the physical distance from its main energy market – that is, at least for the time being, Europe.

ensures that the economic benefits of the regional energy sector development are not limited to producing countries but, rather, are shared also by the transit ones – e.g. in terms of transit fees. Second, the benefits to the transit countries are not limited to the economic sphere, but do also extend to the political realm. Indeed, the need for producing countries to interact and pursue mutually satisfactory arrangements with the transit ones generates a politically relevant dependency relationship. The so-called ‘political land-lockness’,<sup>6</sup> unavoidable corollary of the lack of access to the sea, works therefore by reducing the bargaining power asymmetry between producer and consumer states, as long as the latter are simultaneously client and transit states. Such a consumer-transit state hybrid nature is a key feature of various actors in the Central Eurasian area – i.e. Belarus and Ukraine in the case of Russia, or Georgia in the case of Azerbaijan – and contributes in shaping the latter’s bilateral relations with the supply-export country. Finally, the energy transit operation imposed by the land-locked condition is, by nature, extended in time and space, generating a managing system that tends to be complex and vulnerable to fragmentation and rent-seeking activities.<sup>7</sup> Therefore, the relation between land-locked and transit countries requires a reasonable level of *entente* and political cooperation, essential in order to safeguard the energy security interests of the exporting state.

The transit dependence associated with the landlocked condition of the Central Eurasian producing countries stands as the main feature of regional energy cooperation and makes all the more relevant the interdependencies among USSR successor states, as established during Soviet times and crystallized by the USS. Much has been written in the literature about the economic and political value attached to the pipeline network inherited by the former-Soviet Republics. On the one hand, the Russo-centric nature of the network led many authors to view the USS as a ‘steel umbilical cord’<sup>8</sup> linking the former Soviet empire center and peripheries. According to such a view, the USS enabled the Russian Federation to exert a high degree of economic and political influence over Central Eurasian energy producing and consuming countries, thus relaunching under different forms the past imperial rule over the region. On the other hand, there are those authors who underlined, rather, the ‘free gift’ left by Soviet planners to newly established national elites, who otherwise would not have the possibility – at least in the short and medium term – of exploiting the natural wealth of respective countries.<sup>9</sup>

6 D. Anglin, ‘The Politics of Transit Routes in Land-Locked Southern Africa’, in Z. Cervenka (Ed.), *Land-locked Countries of Africa*, The Scandinavian Institute of African Studies, Uppsala, 1973, p. 112.

7 J.F. Arvis, G. Raballand & J.F. Marteau, *The Cost of Being Landlocked: Logistics Costs and Supply Chain Reliability*, World Bank Policy Research Working Paper No. 4258, June 2007, p. 33.

8 R. Ebel, *Energy Choices in the Near Abroad*, The Centre for Strategic and International Studies, Washington, 1997, p. 5.

9 See L. Grigoriev, ‘Russia, Gazprom and the CAC: Interests and Relations’, in A. Dellecker & T. Gomart (Eds.), *Russian Energy Security and Foreign Policy*, Routledge, New York, 2011, p. 148.

Actually, both interpretations seem to catch part of the Central Eurasian energy development, while simultaneously missing the whole picture. On the one hand, it is impossible to underestimate the upper hand ensured to Russia by the *de facto* monopsony held – for almost a decade – over the purchase of regional hydrocarbons production. On the other hand, it is nevertheless indisputable that regional producers benefited from the availability of energy export infrastructures, with no investment cost or corporate debt. The same holds true also with regard to the regional consuming-transit states. While it is unquestionable that Moscow, being a monopolistic energy supplier to most of these countries, enjoyed a relevant goeconomic and geopolitical tool, it is equally true that Russian transit dependence enabled the formers to pursue rent-seeking behaviors as well as to extract concessions in terms of hydrocarbon purchase price.<sup>10</sup> Finally, it would also be misleading to underestimate the economic cost associated with the Russian drive for cooperation in the CEA.<sup>11</sup>

Summing up, it may be said that the combination of the two previously mentioned key Central Eurasian geopolitical factors – *i.e.* the possession of huge reserves of hydrocarbons and the landlocked condition – offers a self-evident explanation of the relevance acquired by the energy sector to the development of regional cooperation schemes. At the same time, it helps to clarify the scope of the power asymmetry associated with the sector. While the pivotal role played by Russia is manifest – in terms of both resource availability and infrastructures – it would be misleading to assess the latter without keeping into consideration the limitations that the country suffers in terms of transit dependence.

## 7.2 ENERGY AS A PRIVILEGED VEHICLE FOR REGIONAL COOPERATION IN THE CEA: FROM CIS TO EAEU

As already said, ever since the dissolution of the Soviet Union, energy has been a key driver behind cooperation and competition in the Central Eurasian area. While the reconstruction of the factual and normative components of the past energy cooperation schemes falls outside the scope of the present chapter,<sup>12</sup> their main characteristics nonetheless may help

10 Extracting concessions in terms of hydrocarbon purchase price proved to be particularly important to many transit states – *i.e.* Belarus or Ukraine – since it enabled national leaderships to artificially maintain energy price at low levels for both domestic and industrial use.

11 Besides the economic cost deriving from the granting of preferential energy prices, some authors highlighted a more significant political price for Moscow, *i.e.* the possibility of indirectly supporting the recipient states' reform path which, in turn, may facilitate their integration in Euro-Atlantic structures at Russia's cost. See I. Kobrinskaya, 'The Post-Soviet Space: From the USSR to the Commonwealth of Independent States and Beyond', in K. Malfliet, L. Verpoest & E. Vinokurov (Eds.), *The CIS, the EU and Russia. The Challenges of Integration*, Palgrave, New York, 2007, pp. 17-18.

12 See Z. Kembayev, *Legal Aspects of the Regional Integration Processes in the Post-Soviet Area*, Springer-Verlag, Berlin, 2009.

in better portraying and appraising the efforts currently being made under the EAEU umbrella.

A key aspect worth being introduced in order to appraise the evolution of energy cooperation in the CEA and to highlight its disintegration potential, is that *all* the cooperation schemes in the post-Soviet space had to do with energy, *not just* the Russian sponsored ones. Suffice here to recall the GUAM grouping (1997), whose members – *i.e.* Georgia, Ukraine, Azerbaijan and Moldova – merged around the resolve to support each other's independence and sovereignty. A central pillar of the aforementioned effort was precisely the will to jointly develop a 'Euroasian, Trans-Caucasus (energy) transportation corridor' to link the Caspian producing area to European markets bypassing Russian territory.<sup>13</sup> Therefore, energy has been not only a privileged tool for cooperation and integration, but also a typical ground for competition with Moscow for the diversification of regional export routes outside the Russian ones, consistently with the US regional strategy.<sup>14</sup> Under this perspective, GUAM fully embodies the disintegration potential inscribed in the regional energy sector.

Recalling the GUAM experience is also useful to highlight two classical features of energy cooperation in the CEA. First and foremost, far from being developed in a political void, energy cooperation has traditionally been part of wider diplomatic *ententes* or projects among involved actors. That is, the degree of politicization of energy cooperation went well beyond the above-mentioned need to establish sound politico-diplomatic bilateral relations between exporting and transit countries. Rather, it ended up playing a pivotal role for the latter's foreign policies, with all the *pro* and *contra* of being caught up in wider geopolitical calculations and confrontations. Second, the close link between energy and wider diplomatic cooperation paved the way for the former to influence the course of the latter. That is, energy cooperation provided a vital stimulus for the enhancement of bilateral or multilateral cooperation, with a spillover effect on other strategic levels of entente – *e.g.* economy, finance or security.<sup>15</sup>

A second feature characterizing multilateral schemes for energy cooperation in the CEA results from the evident gap between theory and practices, *i.e.* between normative

13 Joint Communiqué, Meeting of the President of Azerbaijan, Georgia, Moldova and Ukraine, Strasbourg, 10 October 1997. Following the 'colored revolutions' in the post-Soviet area, the revolution in Ukraine, the group was relaunched under the name 'Organization for Democracy and Economic Development – GUAM'. However, the focus on the energy cooperation as a tool to strengthen the members' full independence and sovereignty remained unaffected.

14 See C. Frappi, 'The Caspian Sea Basin in United States Strategic Thinking and Policies', in C. Frappi & A. Garibov (Eds.), *The Caspian Sea Chessboard: Geo-Political, Geo-Strategic and Geo-Economic Analysis*, Egea, Milan, 2014, pp. 181-202.

15 An example of the mentioned trend may be found in the evolution of triangular cooperation among Azerbaijan, Georgia and Turkey. See C. Frappi & M. Valigi, *Patterns for Cooperation in the Southern Caucasus Area. Azerbaijan, Georgia and Turkey: Triangular Diplomacy in the Shadow of Energy Strategy*, ISPI Working Paper No. 57, July 2015.

provisions and current actions. Under this perspective, energy cooperation schemes made no exception to the primarily ‘declarative nature’ of cooperation and integration frameworks in the area, particularly manifest during the 1990s.<sup>16</sup> Generally speaking, such a trend has primarily been the result of the already mentioned high degree of politicization characterizing CEA’s multilateral framework for cooperation – whereby more often than not membership was interpreted by its participants’ instrumentally, as an end in itself rather than as a tool to enhance cooperation and/or sectorial integration.

As far as the hydrocarbons sector is concerned, the weakness of multilateral frameworks resulted in energy cooperation remaining essentially a matter of bilateral relations. As a matter of fact, pivotal energy actors – with Russia leading the way – displayed a natural aversion to devolving sovereign prerogatives to supranational bodies in a highly strategic sector like energy. Moreover, the preference given by producing countries to bilateral relationships over multilateral ones reflects the latter’s will to better exploit the higher bargaining power enjoyed in direct energy negotiations with transit and/or client countries. Paradoxically, this implied that energy, while being a key vector for inter-state cooperation, often represented a hurdle over the path toward economic integration.<sup>17</sup>

On this backdrop, the last round of integration process in the CEA – initiated in 2010 with the Customs Union, transited in 2012 in the Single Economic Space and culminating with the entry into force of the EAEU in January 2015 – showed some important novelty in comparison to previous frameworks for cooperation.<sup>18</sup> First and foremost, it put forward a much stronger institutional base and a much sounder legal framework, reflected by the creation of institutional bodies responsible for the management of the integration project. The reference applies to the establishment of the Supreme Eurasian Economic Council at the level of heads of state and governments, the Eurasian Economic Commission, as the permanent supranational regulator body,<sup>19</sup> and the Court of Eurasian Economic Community. Second, the process initiated in 2010 marked an attempt to go beyond the *de jure* reception of the *de facto* power asymmetry characterizing the area, through the provision

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16 See Y. Vymyatnina & D. Antonova, *Creating a Eurasian Union. Economic Integration of the Former Soviet Republics*, Palgrave Macmillan, New York, 2010, pp. 9-12.

17 For instance, Kembayev notes for example that the Russian refusal to ratify the CIS Agreement on the Establishment of a Free Trade Area (1994) stemmed primarily from the reluctance to open up its markets and to supply hydrocarbons at its domestic prices outside a full-fledged economic union. Kembayev 2009, p. 87.

18 For a deeper analysis see C. Atilgan, G. Baumann, A. Brakel, C. Crawford, J. Devcic & A. Helms, ‘The Eurasian Union: An Integration Project Under the Microscope, Konrad Adenauer Stiftung’, KAS International Report, No. 2, 2014; R. Dragneva & K. Wolczuk, ‘Eurasian Economic Integration: Institutions, Promises and Faultlines’, *The Geopolitics of Eurasian Economic Integration*, London School of Economics, LSE IDEAS Reports, No. 19, June 2014, pp. 8-15.

19 The Commission, which represents the core and the main engine of the integration effort, works through 23 thematic departments under the direction of one chairman and nine Ministers. Among these, the Energy and Infrastructure departments are pooled under the direction of one Minister.



of weighted votes or qualified majorities, which was used to crystallize Moscow's dominant position. The impression among scholars and practitioners was, therefore, that through the EAEU framework Russia was effectively 'limiting itself'.<sup>20</sup>

Moreover, with specific reference to the energy sector, the Treaty on the Eurasian Economic Union put forward for the first time an ambitious vision for a supranational integration as it prescribed that "the member states shall develop long-term mutually beneficial cooperation in the energy sphere, conduct coordinated energy policy and gradually create common energy markets".<sup>21</sup> Accordingly, the Treaty foresees the gradual establishment of a common market in sectors of electricity, oil and gas, along with unhindered access for economic entities of member states to the energy transportation systems located in their territories.<sup>22</sup>

However, turning from the legal and institutional provisions to the concrete evolution of the integration project, the EAEU seems to replicate its predecessors' above-mentioned shortcomings, both in general as well as with specific reference to the energy sector. As far as the latter is concerned, the two main novelties of the integration project – *i.e.* the limitations of national sovereignty and the formal equality among its members – did not bear any concrete result.<sup>23</sup> That is, the prevalence of bilateral over multilateral relations and the consequent reassertion of bargaining power asymmetry to the benefit of Russia remained unaffected. As a matter of fact, instead of pushing forward sectorial integration trends, Moscow kept on capitalizing on the upper hand in the energy sector in order to pursue a 'stick and carrot' strategy *vis à vis* its partner. Accordingly, energy – and in particular bilateral agreements over prices and custom duties – remained one of the key pillars upon which Moscow based its power of attraction. This trend was evident in the Belarus case and, to a lesser extent, in the Armenian one. As a consequence, in both cases the participation to the EAEU framework seems to follow an old instrumental – if not declaratory – logic, rather than a clear commitment to the integration path.<sup>24</sup>

Moreover, the real qualitative change in energy cooperation envisioned by the EAEU Treaty – *i.e.* the foreseen establishment of common markets – rests so far merely on the paper, notwithstanding the provision of a timetable for its accomplishment.<sup>25</sup> The problem here arises from the consideration that the envisioned common oil and gas markets are

20 See Atilgan *et al.* 2014, p. 9.

21 Treaty on the Eurasian Economic Union, Section XX, Art. 79.

22 *Id.*, Arts. 81-84.

23 The same can be said with reference to the wider EAEU functioning. See Dragneva & Wolczuk 2014, pp. 12-13. See also I. Wiśniewska, *Eurasian Integration. Russia's Attempt at the Economic Unification of the Post-Soviet Area*, OSW Studies, July 2013.

24 See Atilgan *et al.* 2014, pp. 34-47.

25 As far as the electricity is concerned, the common market – according to a decision taken last year by the Supreme Eurasian Economic Council – shall be implemented by 2019. As per the oil & gas one, the timetable – subject to a forthcoming ruling of the Supreme Council – shall be implemented in stages by 2024 and 2025 respectively, with a progressive dismantling of infrastructure, commercial and regulatory barriers.

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not just *still-to-come* projects, but also *still-to-be-negotiated* ones. That is, the most important agreements necessary to provide substance to the general aim of establishing common markets – *i.e.* price formulas, nondiscriminatory access to the pipeline system, a relationship with third countries – are still to be negotiated and achieved. However, besides the difficulties naturally endowed in the diverging energy strategies and aims of member states, such agreements appear quite difficult to reach under the current circumstances – characterized by the evident weakening of the economic and political bonds keeping together EAEU member states.

Indeed, the regional contingency that accompanied the EAEU's first year of existence clearly did not help the project to advance toward its institutional goals. Quite the contrary, the Ukrainian crisis had two negative and far-reaching consequences on the integration process. On the one hand, by worsening the economic hardship already faced throughout the CEA as a consequence of the fall in oil prices, the crisis resulted in loosening of internal ties as well as highlighting the economic contradictions of the EAEU space. Simultaneously the crisis signaled once more the primacy of politics on economy, the preeminence of the EAEU geopolitical essence which, in turn, tends to alienate partners – like Kazakhstan – traditionally wary of a Russia leaning toward a neo-imperial posture.

### 7.3 A PAPER TIGER? EAEU IN THE CURRENT WORLD AND EURASIAN ENERGY SCENARIOS

While the EAEU domestic scene does not leave much room for optimism as per the coherent and efficient development of energy cooperation, at the same time the current global and regional energy scenarios seem to pose as much relevant hurdles to the CEA's integration path, strengthening the disintegration trends.

Current energy scenarios are shaped by two connected trends. The first has to do with the changing geography of energy consumption: whereas the East Asian markets are opening up due to growing energy demand, the European one is being squeezed by falling consumption and, finally, the American one is definitively shutting off by virtue of the growth in domestic oil and gas production.<sup>26</sup> These modifications in regional hydrocarbons demand concur in bringing about an Eastward shift of the Eurasian energy center of gravity, which naturally impinge upon CEA producers' energy policies.

The latter are simultaneously influenced by the second trend detectable in energy scenarios, *i.e.* the current excess of hydrocarbons production and, therefore, the excess of hydrocarbons' offer over demand. Whereas this trend may prove to be merely conjunctural, nonetheless it has far-reaching implications, at least in the short and mid term, over the

<sup>26</sup> See M. Nicolazzi, 'Geopolitica dell'Abbondanza', in M. Verda (Ed.), *Energia e geopolitica. Gli attori e le tendenze del prossimo decennio*, ISPI, Milan, 2014, pp. 1-8.

energy sector in general and over regional integration projects in particular. Indeed the excess of production seems to preside over the reversal of the classical *consumer syndrome* fostering an opposite *producer* one. That is, while traditionally consumers were competing for access to the production, in the current scenario the competition seems rather to develop primarily among producers intent on gaining access to markets or safeguarding market quotas.

On this backdrop, the Eastward shift of the Eurasian energy center of gravity, coupled with the unfolding producer syndrome, has already had a relevant impact over energy cooperation in the CEA and, especially, in the Caspian area – which has traditionally been the core of regional energy cooperation. Such an impact is best embodied by – and primarily linked to – the Chinese *going abroad* energy strategy, which over the last decade broke Russian quasi-monopsony over the purchase of Central Asian hydrocarbons and instilled a significant degree of competition between Moscow and others regional producers. Indeed, driven by the steady growth in energy consumption, Beijing has reached out since 2005 to Eastern Caspian producers, with a resolute oil and gas procurement strategy. The latter has enabled China, in a very limited time frame, to establish deep roots in both regional midstream and upstream sectors, extracting concessions over the main regional fields<sup>27</sup> as well as setting up oil and gas import pipelines between the Caspian area and Xinjiang.<sup>28</sup> At the same time, capitalizing over the Russian will to diversify its export markets, China signed relevant deals and a memorandum of understanding aimed at opening a gas supply channel from Siberian fields.<sup>29</sup> The magnitude of contracted and foreseen gas volumes may however conflict with the agreements already signed with Central Asian producers, deepening competition among CEA producers and fostering regional disintegration trends.

The scope of the Chinese challenge to energy integration projects in the CEA is no less significant in qualitative terms than in quantitative ones, primarily as a result of Beijing's way of doing business in Central Asia as elsewhere. As a matter of fact, the typical convergence of interests and policies among Chinese governmental, banking and energy institutions provides the target countries with a business model that has no parallel in Russia (let alone in Western countries). Such a model – embodied by the so-called *oil-for-loans policy* – provides Beijing with a competitive advantage, which, over the last decade, bore the

27 In 2013, the China National Petroleum Corporation became shareholder (8.4%) in the Kashagan giant field in Kazakhstan – where Chinese national companies' share of the overall oil annual production reached 24% in 2014. Moreover, China today absorbs the great part of the gas export (60%) originating in Turkmenistan, where Chinese companies were the first foreign actors to get exclusive rights over significant onshore gas fields.

28 The reference goes to the Kazakhstan-China oil pipeline originating in the port of Aktau, and to the Central Asia-China Gas Pipeline, a four-line infrastructure originating in Eastern Turkmenistan and crossing four out five Central Asian countries on its way to China.

29 As per the rationale behind current Sino-Russian entente and per the specific role of energy see A. Gabuev, *Friends with Benefits? Russian-Chinese Relations after the Ukraine Crisis*, Carnegie Endowment for International Peace, Moscow, 2016.

above-mentioned fruits in the race for Caspian energy resources. Moreover, the Chinese *no-strings-attached policy* – which postulates doing business without interfering in political issues – provides Beijing with a degree of flexibility and adaptability to local conditions hardly achievable either by Western countries or by Russia itself. That is, Chinese adhesion to the principle of noninterference in partners' domestic political issues ensures Beijing's policies a sound advantage not only *vis à vis* European competitors, whose projection is somehow affected by the principle of 'democratic conditionality', but also *vis à vis* Moscow, whose regional policy more often than not generates the perception of a hidden neo-imperial agenda among partner countries.

While incentives to enhance CEA's energy cooperation and integration frameworks do not come from Eastern and Southern Asia, the picture appears to be no less gloomy in the West, *i.e.* in relation to the European Union. Indeed, although the possibility for the EU to encourage a positive development from the outside and to exploit the energy interdependencies is not lacking,<sup>30</sup> nonetheless it appears to be a prisoner of older geopolitical drifts, exacerbated by the Ukrainian crisis.

Generally speaking, two trends seem to run counter to the possibility of the EU becoming an incentive for energy integration within as well as cooperation with the EAEU. At a wider look, the first has to do with the persistent incapability of both Brussels and Moscow in subscribing to a common vision of a 'wider Europe', *i.e.* to put forward win-win arrangements for the so-called shared neighborhood. The lack of agreement on a long-term vision tends, in turn, to put Russian and EU sponsored regional initiatives on a collision course, notwithstanding the wide room for mutual beneficial initiatives. Moreover, as far as energy cooperation is concerned, the diversification of supply sources and channels away from Russia still represents the main pillar of EU external dimension of energy security strategy. Therefore, in courting CEA minor energy producers with a view to inaugurating new energy corridors, Brussels seems to push forward existing disintegration trends in the CEA rather than fostering integrative ones. Needless to say, the EU tendency to enforce the CEA disintegration trends in energy sector and to widen the gap between Russian and minor regional producers' interests is even more pronounced in times of excess in hydrocarbons production, since it tends to deepen the producer syndrome and the competition for the access to final markets.

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30 See, for instance, M. Pastukhova & K. Westphal, *A Common Energy Market in the Eurasian Economic Union. Implications for the European Union and Energy Relations with Russia*, Stiftung Wissenschaft und Politik, SWP Comments, No. 9, February 2016. As per the potential advantages to the EU, Atilgan *et al.* 2014, p. 14.

#### 7.4 CONCLUSIONS

In comparison to the previous cooperation and integration schemes, the EAEU has more ambitious projects as far as the energy sector is concerned. However, at the same time, it seems to replicate the former's traditional shortcomings.

In general, the first year and a half of the EAEU's existence has not brought the envisioned step change in relations among its member states, notwithstanding the ambitious goals envisaged by its Treaty in regard to the energy sector. Certainly, the ostensible failure of the EAEU framework has a lot to do with the difficult times the newly formed block had to face in both economic and political terms – as a result of the 'perfect storm' resulting from falling energy prices, Ukrainian crisis, economic sanctions on Russia and devaluation of both the Russian Ruble and the Kazakh Tenge. It is equally true, however, that many of the mentioned issues resulted primarily from Russia's aggressive stance toward its 'near abroad' and, in particular, from the muscular attempt to counter what Moscow perceived as a geopolitical threat to its own national interest and security – *i.e.* the subtraction of Ukraine from its own regional-building projects. As such, the EAEU replicated a traditional shortcoming of previous regional cooperation and integration attempts, *i.e.* the primacy of geopolitical above economic considerations.

At a wider look, it may however be said that the Ukrainian crisis revealed the contradictions and weakness inherent to the project itself, which remained halfway between the loose form of Russian-centric integration of the 1990s and the attempt to move toward a full-fledged economic integration, in the energy sector as well as beyond it. The gap between EAEU *de jure* framework and *de facto* functioning is quite evident: far from being a voluntary political and economic integration of equal sovereign partners into a supranational organization, the Union is still dominated by intergovernmental and bilateral negotiations, while the premise of equality among all of its members is clearly bypassed – wherever not violated. This is especially true in regard to the energy sector, where Russia keeps on exploiting its dominant position through a 'stick and carrot' strategy and where its partners, in turn, tend to abide by a rent-seeking behavioral logic. Under these circumstances, the perspective for the EAEU to move toward a full integration in the energy sector – as envisaged by the creation of a single market for oil and gas – appears at least bleak.

The picture is no less gloomy when looking at the EAEU framework from the outside – *i.e.* from the perspective of the main energy poles of attraction, on the East and the West. Indeed, the regional energy policies of both China and the EU seem to foster disintegration trends, rather than integration ones. As a matter of fact, notwithstanding the availability of their own multilateral framework for cooperation,<sup>31</sup> both China and the EU tend to

31 EU relations with regional countries are primarily framed within the 'European Union's Strategy for Central Asia', adopted in 2007 and involving multilateral cooperation on energy and transport, among others. As

relate primarily with individual actors of the CEA and EAEU area and, in doing so, they are delegitimizing local integration frameworks and decoupling single partners' interests and policies from the Russian ones. Such an attitude has two main consequences on the evolution of integration attempts in the CEA. First and foremost, Chinese and EU's regional initiatives in the energy sector – while not being necessarily incompatible with Russian ones – tend to foster competition rather than cooperation with Moscow-led initiatives, ever the more so since they tend to capitalize on the unfolding producer syndrome discussed above. Second, they undermine one of the EAEU's main aims, *i.e.* Russian attempt to set up a negotiating block, legitimate and capable of providing its members with a 'single voice' in international affairs – consistently within the Kremlin's view of a multipolar international system in which the EAEU could stand as “an independent centre for global development, rather than remaining on the outskirts of Europe and Asia”.<sup>32</sup>

Summing up, the EAEU seems to be characterized and affected by the same dichotomy between integration and disintegration forces that shaped the older regional cooperation schemes in the CEA. At the same time, looking at the Union either from an internal or an external perspectives, the disintegration forces seem to be stronger than the integration ones. Therefore, the potential for the EAEU to take a real step in the direction of change on the path toward regional integration appears to be scarce – both in general and with reference to the energy sector – as long as, internally, its institution remains weak and prone to dominant Russian position and unless externally, the competition logic is supplanted by a win-win approach to regional development based upon functional interdependences.

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per China, Beijing is among the founders (along with Russia) of the Shanghai Cooperation Organization and the initiator, and main founder, of the 'Silk Road Economic Belt'.

32 V. Putin, "Transcript: [Putin at] Meeting of the Valdai International Discussion Club", Johnson's Russia List, 19 September 2013, available at: <<http://russialist.org/transcript-putin-at-meeting-of-the-valdai-international-discussion-club-partial-transcript/>> (accessed on 18 October 2016).