



The Ukraine Crisis

Much More than Natural Gas at Stake

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The Pattern: A Classical Greek Tragedy

- The actors, out of hubris, overestimate their strength and inflict unnecessary harm on their adversaries, disregarding consequences and risks
- The adversaries, initially victims, respond reciprocally, in the same way, also inflicting unnecessary harm, compromising their own positions
- Mutual harm and revenge lead to escalating conflict
- In the end, everyone suffers, not by necessity, but by choice

The Relevance

- A new cold war seems to develop between Russia and the West. The current crisis in Ukraine should be analysed within the context of the triangular relations between the EU, Russia and the United States; in this game Ukraine is both the joker and the blackjack
- The geopolitical and geo-economic significance of the crisis surpasses that of natural gas trade. The Ukraine crisis is potentially a catalyst for major changes.
- In the worst case, the current confrontation could escalate into a major conflict that would be in nobody's interest and that could have been avoided, just like in 1914

The Stakes

- A question of spheres of influence
- Since 1991, Ukraine had been an area of mixed EU and Russian influence
- Russia's ambition: to gain influence in Ukraine through a Eurasian common market
- The EU ambition: to gain influence in Ukraine, but without overtly provoking Russia
- The US ambition: to remove Ukraine from Russia's sphere of influence, eventually secure a NATO presence, and isolate and encircle Russia
- Ukraine's ambition: to get closer to the EU, but to benefit from Russian money and natural gas

The Setting

- Ukraine's economic calamity caused a political crisis that erupted in January 2014, with the Yanukovich government losing legitimacy
- Russia offered money and natural gas on the condition of Ukraine not signing the EU association agreement, but open to a three-party deal, in order to secure its strategic interests by economic means, underestimating Ukrainian nationalism and anti-Russian sentiment
- The EU responded by forcing Ukraine to choose between itself and Russia, ignoring Russia's interests and historical position, and without offering much money or any natural gas
- The Kiev coup, supported by the United States, provoked Russia
- Russia responded by annexing Crimea, breaking international law and the 1994 agreement guaranteeing Ukraine's integrity, but ,
- Russia has underestimated the Ukrainians' desire to integrate Europe

The Salience Of Ukraine

- Ukraine is Russia's soft underbelly, important in both economic and strategic terms
- About one half, 63 bcm, of Russia's gas exports to Europe transits Ukraine to Central and South-East Europe; the remainder transits Belarus into Poland, or goes directly through the Baltic Sea Nord Stream into Germany
- The Baltic pipeline has considerable spare capacity, so that the net EU dependence on Ukrainian transit is only 19 bcm, but its utilization requires an EU permit
- Russia has invested in pipelines to bypass Ukraine, indicating an intention not to conquer it
- The coup and a hostile government in Kiev changed Moscow's reasoning; it suddenly appeared more risky *not* to annex Crimea than to do it

Ukraine to Russia: From Friend to Foe

- The outlook before February 2014 was that Ukraine was being more firmly attached to the Russian economy
- Ukraine benefited from a discount on natural gas prices, paying less than \$300/1000 bcm, against a standard export price of about \$400/1000 bcm
- Russia sees no reason to give price discounts or economic aid to a hostile neighbour.
- The friendship discount has been replaced by an enemy surcharge, with prices close to \$500/1000 bcm, applied retroactively to past deliveries!

Russian Gas Export Routes to Europe

bcm/year

Route	Capacity bcm/year	Volume 2012	<i>Spare capacity</i>
Ukraine	72	63	9
Nord Stream	56	22	34
Belarus	38	27	11
Baltics/Finland	5	4	1
Total with Ukraine	170	116	55
Total without Ukraine	98	53	46

Ukraine Instability, Russia and EU Gas

- Ukraine is a problem for Russia as much as for the EU; non-payment by Ukraine triggered natural gas supply crises for the EU in 2006 and 2009.
- The parliamentary elections have given a moderate, centre-right outcome, with a clearly pro-EU profile, but the most urgent task is to mend relations with Russia
- Uncertain to what extent the new parliament will be more willing to reform than the old one and whether oligarch power will be curbed
- There is a risk of gas disruptions unless Ukraine should receive sufficient economic assistance to pay the gas bill, or get Russian gas on favourable terms; Ukraine has made such threats

Russia's Predicament

- Historical invasions have made Russia, regardless of regime, wary of key strategic issues and encirclement
- Crimea is essential, Russian since 1783, the port of the Black Sea fleet
- Russia had accepted an independent and neutral Ukraine, assuming the naval base was secure, but the 2014 Ukraine regime change provoked Russia causing an instant annexation, out of fear of NATO
- Russia is highly dependent on oil and gas sales to Europe and has no interest in a conflict
- Investment in the Baltic Sea Nord Stream and the planned Black Sea South Stream pipelines indicate Russian intentions to bypass Ukraine to secure market access, not to conquer it, but the EU Commission is an obstacle

Norway No Alternative to Russia

- Norway does not have the capacity to replace Russian natural gas supplies.
- Norway has no interest in driving out Russian natural gas from European markets; the risk is retaliation and compromising long-term political relations.
- Germany, would not welcome a Norwegian move to push Russian natural gas out of the market.
- For Germany, there is more at stake than energy supplies. Russia is an important export market for German industry, with substantial German direct investment in Russian industry.

US Interests

- Some of the same forces and personalities that prepared the Iraq War were active in Ukrainian affairs up to the crisis (e.g. Victoria Nuland)
- To tie Europe more closely to the US through military, financial and trade cooperation, as well as military operations outside the core NATO area
- To prevent the EU from developing close bilateral economic and trade links with Russia and the gradual emergence of a Eurasian constellation
- To prevent the EU from emerging as a coherent and competing power and to prevent the euro from becoming a real rival to the US dollar
- To prevent the EU from siding with emerging powers to change the international financial system

European Options

- To continue business-as-usual, observing token sanctions on Russia, most likely if the crisis does not escalate, and prepare for Ukraine as a member by 2025
- In case of crisis escalation, impose harsher sanctions at higher cost and take a large share of the financial burden
- The gain of political influence should be weighed against the cost of supporting Ukraine's economy
- The risk for Europe is to be left with the bill for Ukraine, while the US will gain political influence
- Alternatively, actively work for a settlement between Ukraine and Russia
- Europeans might opt out of sanctions on Russia and refuse to pay for Ukraine; not impossible

Cui Bono? (Who benefits?)

- The Ukraine crisis is not spontaneous, it appears as designed, exploiting the collapse of the Ukrainian economy and the Yanukovich government, by the West as well as Russia
- Ukraine does *not* benefit; it would be better off as an intermediary between the EU and Russia
- Russia does *not* benefit from the crisis, sanctions and strained relations with Europe, but it has overplayed its hand
- Europe does *not* benefit from sanctions and strained relations with Russia, but the EU has no vision for dealing with Russia
- In the USA:
 - The military-industrial complex and anti-Russian ideologues, the neoconservatives, and may be the shale gas industry, *do* benefit from tension with Russia
 - the large US oil companies and supply industries do *not* benefit
- China *does* benefit from an enhanced bargaining position with Russia, whose gas export preferences shift away from the EU

Back to Geopolitics

- EU energy policies cannot be isolated from relations with Russia, the Middle East and North Africa
- The neighbours' main assets are oil and gas, which they must sell in order to buy EU goods and services
- So far, EU energy policies have been introvert, assuming rising oil and gas prices; the reality may be different
- In 2014, Russia may have gained Crimea, but lost Ukraine; Europe may have gained Ukraine, but lost Russia; China may have gained Russia as a bonus

Conclusion

- In Ukraine, the EU and the US have challenged Russia, so far without success. This failure is likely to have an impact on relations between the EU and Russia, as well as between the EU and the US.
- German industry and banking do not want confrontation with Russia
- French right-wing opposition leader Marine Le Pen has publicly blamed the EU for the Ukraine crisis
- Advancing economic integration between Russia and the EU would gradually foster a large constellation in the northern part of the Eurasian continent, the great US fear of the Cold War era. This time, however, the epicentre is not Moscow, but Berlin.
- Indeed, the US neoconservative engagement in Ukraine may have been motivated by a desire to drive a wedge between the EU and Russia to halt any further integration and to ensure US global primacy.

Questions & Answers

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