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EU's Energy Union Strategy: Challenges and Opportunities

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Introduction

The Juncker Commission, which was inaugurated on 1 November 2014, has set up ten priorities for its term, with the Energy Union and climate being among them. The objective of the Energy Union of the EU is to ensure that Europe gets 'secure, affordable and climate-friendly energy'.

The main catalyst for launching the new strategy was the Ukraine crisis, which escalated with the Russian annexation of Crimea in March 2014 and with the subsequent evolution of the crisis into a military conflict in the east of this country.

Pipelines delivering Russian gas to Europe through Ukraine with the detrimental contract that saw Ukraine paying far too high a gas price to its Eastern neighbour in one of the biggest corruption scandals in recent years, and Ukraine's attempt to get closer to the European Union through the Association Agreement (AA) with the European block, are at the core of the Ukrainian-Russian conflict. 'Wake-up calls' for Europe could first be heard during the winter of 2006 and then again in 2009 when the Russians severed the gas supply for Europe through Ukraine, exposing the EU's vulnerability to its big neighbour to the east.

For this reason the EU laid out its European Energy Security Strategy in May 2014, and then the new Juncker Commission adopted the EU's Energy Union strategy in February 2015, with supply security at its core.

The annexation of Crimea and the conflict in Ukraine that followed had served as a catalyst for the EU's Energy Union strategy, and since 2014 the European block has viewed Russia more as a challenger in the energy field, rather than a partner. After the deterioration of

relations following the Crimean annexation, the EU is now seeking to diversify its energy sources outside its borders, leaving Russia as one of the supply routes, and not the dominant energy source supplying Europe with more than 30% of its demand for gas. The European energy addiction to Russia has so far had negative impacts on the EU's credibility regarding peace brokering in Ukraine, and the EU's protection of member states in the East, and it has put Europe in an unfavourable position in its bilateral relations with Russia, thwarting the EU's attempts to be a credible player on the global scene, with a thaw between the two sides not likely to occur soon.

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A year since the new Commission was installed, some progress has been achieved, but in terms of diversifying its sources of energy as one of the five pillars of the Energy Union, Europe still has a long way to go.

German-Russian cooperation in energy projects dilutes EU's common position

The EU's efforts to boost its Energy Union and diversify its supply routes could be seriously hampered by an agreement on the Nord Stream 2 gas pipeline project, signed in September 2015 by the Russian energy giant Gazprom and other stakeholders, including E.ON, BASF/Wintershall, OMV, ENGIE and Royal Dutch Shell, which form the European part of the energy companies' consortium.

The new pipeline Nord Stream 2, lines 3 and 4, are to be constructed by 2019, transporting an additional 55 billion cubic metres (bcm) of gas annually underneath the Baltic Sea, an enormous increase on the 22 bcm of gas being imported through the current Nord Stream pipeline opened in September 2011.

This agreement comes at a time when hostilities between pro-Russian rebels, backed by regular troops of the Russian Federation, and Ukrainian troops in the Donetsk/Lugansk regions, have not fully ended, regardless of the Minsk 2 package of measures, along with the recent Russian deployment of air forces in Syria, as well as 'boots on the ground' shifted from Ukraine to the Middle East.

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Europe's gas imports from Russia have surged above 30% during the past five years, and only in 2014 gas imports from Norway reached the level of Russian imports, with both countries contributing around 30% of Europe's gas supply, respectively. But nearly half of the gas coming from Russia to Europe is transferred through Ukraine, around 80 bcm of gas

annually, and now Russia is bolstering its efforts to bypass the gas transmission through this country.

So far, the European Union has been able to resist Russian initiatives to further link Europe to its energy orbit. Due to the EU's Third Energy Package, which stipulates the separation of companies' production and sales operations from their transmission networks, the European Commission has been successfully hampering Gazprom's attempts to construct the 'South Stream' pipeline, which was conceived to bring the Russian gas, bypassing Ukraine, beneath the Black Sea to Bulgaria and the EU. Finally, Russian President Vladimir Putin abandoned the project in December 2014, only to instigate a new pipeline project, the 'Turkish Stream', during his visit to Turkey's President Erdoğan. Soon, the idea of constructing the 'Turkish Stream' was brought to a halt, and with the Turks shooting down the Russian bomber aircraft near the Turkey-Syria border on November 24th 2015 and subsequent unfolding escalation between Moscow and Ankara, the future of this project looks rather bleak.

However, all European attempts to curb Russian domination of the energy supply in Europe were watered down with the decision of Germany and its energy companies to sign the agreement with Gazprom as a key stakeholder in the consortium. The EU's Energy Union strategy thus exposed the vulnerability of the European Union as Germany, with its status as the central and at the moment most powerful EU member state, has decided to help Russia bypass Ukraine, without consultation with other EU member states in Central and Eastern Europe, which strictly oppose the Nord Stream 2 project.

Opposition of central and eastern European countries to Nord Stream 2

At the same time Poland and the three Baltic states are stepping up their efforts to reduce their dependency on energy imports from Russia. These countries have experienced trauma under Soviet control and have been vocal advocates of Ukraine's efforts to slip away from Russian influence and to forge stronger ties with the EU. Further to this, the Baltic political elite, and especially Polish President Andrzej Duda, have been urging a unified and strong NATO platform toward Russia's military involvement in Ukraine and sought the deployment of NATO, namely American and British, troops on their territory.

> *The gas flow from the Polish LNG terminal could be linked to the planned LNG terminal on the Croatian island of Krk in the northern Adriatic. The gas for central European countries will not, in this scenario, be transmitted from the closest and 'most natural' choice, the Russian Federation, but rather from distant Qatari natural gas fields*

Just two months after the agreement on Nord Stream 2 had been signed, seven countries from Central and Eastern Europe rallied around their position that this project is not in line with the EU's Energy Union strategy, and was hampering

efforts to stabilize Ukraine. The Czech Republic, Estonia, Greece, Hungary, Latvia, Lithuania and Poland, backed by the United States, opposed the Nord Stream 2 and signed a letter addressed to Maroš Šefčovič, Vice-President of the European Commission in charge of energy Union, asking for the project to be stopped and called for a regulatory scrutiny and 'an inclusive debate' of EU leaders on this issue.

The volatility of energy supplies from Russia and the fear of being isolated in the midst of German-Russian energy cooperation enticed Poland to seek new routes for its energy supply. In October 2015, Poland opened its LNG terminal at the Baltic port of Świnoujście with a contract being previously signed with Qatargas as a supplier. When the terminal reaches its full utilisation by 2018, Poland will be able to meet around a third of its gas demand from it, and from Poland gas will be transmitted to the neighbouring Baltic states, the Czech Republic, Slovakia and even Ukraine, in an attempt to make a reverse flow of gas in Europe, rather than have the continent in the grip of the Russian energy giants. The gas flow from the Polish LNG terminal could be linked to the planned LNG terminal on the Croatian island of Krk in the northern Adriatic. The gas for central European countries will not, in this scenario, be transmitted from the closest and 'most natural' choice, the Russian Federation, but rather from distant Qatari natural gas fields or from the United States, which last year took over the position of the leading global oil and gas producer.

At the same time, in October 2015, a grant agreement on GIPL (Gas Interconnector Poland–Lithuania) was signed, and GIPL will be the first pipeline connecting the two countries, while the EU hopes that it will reduce the energy isolation of the Baltic region. The pipeline will be finished by 2019 and the European Commission is financially and politically supporting the project, stating that interconnectors like GIPL are 'missing links in the energy infrastructure'. The LNG terminal and the GIPL pipeline in Poland proved that supply security, including diversification of sources, and full integration of the energy market within Europe are central elements of the EU's Energy Union.

The importance of the Southern Gas Corridor for the EU's Energy Union strategy

The European Union is trying to lessen its dependence on energy imports from Russia not just through LNG terminals importing gas from the Persian Gulf and the United States, but also by opening new supply corridors linking southern Europe to northern Africa and the Middle East. After the Nabucco pipeline project was watered down, the new Trans Adriatic Pipeline (TAP) project stepped in as the key project of the EU's Southern Gas Corridor initiative. TAP will basically be an extension of the Trans-Anatolian Natural Gas Pipeline (TANAP), which will stretch across the whole of Turkey from the Georgian to the Greek borders, and which will be the central part of the Southern Gas Corridor of the EU.

TAP's shareholders are British Petroleum (20%), the Azeri oil and gas giant SOCAR (20%), the Norwegian company Statoil (20%), the Belgian company Fluxys (19%), the Spanish Enagás (16%) and the Swiss Axpo (5%), making a vast Azeri-European energy consortium. TAP will bring gas from the Azeri

gas-filled Shah Deniz 2 in the Caspian Sea to the market of southern Europe, and will extend to southern Italy, crossing Greece, Albania and the seabed of the Adriatic Sea. TAP's length will be 870 km and the construction of the pipeline is expected to start in 2016.

Ever since TAP won the definite support of the EU, replacing the competing Nabucco West project in 2013, the project has aroused a lot of attention and big European energy companies have sought their place in the consortium, leaving others out of the game, at least for the time being. In May 2014, TAP appeared on the list of priority energy projects of the European Energy Security Strategy.

The advantage of the TAP project is that it connects the Caspian Sea and Turkey on one side and the European market on the other. Apart from its main route to Italy, which is the biggest European gas market after Germany, interconnectors can be built to Bulgaria from Greece, as well as a new pipeline to Montenegro and Croatia along the Adriatic coast from the tie-in in Albania, the Ionian Adriatic Pipeline (IAP).

TAP project could significantly contribute to the energy security of the EU and its Energy Union strategy, providing that the EU succeeds in its efforts to fully integrate its internal energy markets

On this, Italy has a well-developed gas transmission grid, with interconnectors to Switzerland and Austria, and further to the major EU market, Germany. Croatia has almost completely finished the gasification of the country with a pipeline reaching the coastal city of Split in 2013, and has interconnectors to Slovenia and Hungary, which need a minor investment of a compression station that would enable a reverse flow of gas from Croatia to central European countries. Croatia, with its gas consumption of below 3 bcm annually, might not be an attractive market per se, but the country could be an interesting transmission point for the huge central European market.

TAP could supply gas not just to southern Italy and South-East Europe, which is a small market as ex-Yugoslav countries together with Albania consume less than 10 bcm of gas annually, but also to central European countries including Ukraine. This way, the TAP project could significantly contribute to the energy security of the EU and its Energy Union strategy, providing that the EU succeeds in its efforts to fully integrate its internal energy markets, including the reverse flows enabling the transmission of gas from the West of the continent to the EU member states in the East and Ukraine.

But a major issue of the TAP project and its role in the EU's energy strategy is that its initial capacity will be 10 bcm of gas annually, expandable only to 20 bcm/y of gas, from the Shah Deniz 2 project on the Caspian Sea that will start running in 2020. These quantities are far below the gas quantities that Europe imports from Russia alone, which stand at over 160 bcm/y at the moment, and could surge further with the construction of Nord Stream 2, which is to be concluded even before the first cubic metres of Azeri gas make their way to

Europe. It is evident that gas from Azerbaijan will not be a sufficient replacement for Russian gas, and that Russia will retain a huge stake in the EU's gas market in the perceivable future, making Europe vulnerable to Russia's geostrategic agenda in eastern Europe.

TANAP will connect the southern Caucasus region with the South-East of Europe, but interconnectors to Iraq and Iran could also be constructed, and additional quantities of gas could be transported via Azerbaijan, which has limited gas resources, from Turkmenistan through the Trans-Caspian Gas Pipeline.

The TAP project should be viewed through the prism of the vital importance of the TANAP project as the capacity of the pipeline will reach 60 million bcm/y in the final stage. With the construction of TANAP, Turkey will become a major energy hub and a great portion of TANAP's gas will be transmitted to the European market. TANAP will connect the southern Caucasus region with the South-East of Europe, but interconnectors to Iraq and Iran could also be constructed, and additional quantities of gas could be transported via Azerbaijan, which has limited gas resources, from Turkmenistan through the Trans-Caspian Gas Pipeline.

Iran has the world's biggest proven gas reserves, and Turkmenistan is ranked number four globally in terms of gas reserves. Together, the two neighbouring countries, located in the richest swathe of land in the world in terms of energy resources, between the Caspian Sea and the Persian Gulf, have some 25% of the world's gas. With the European Union and the United States lifting sanctions against Iran on 16th January 2016, the EU will gain access to a second major gas market in the world, beside Russia, and combined with the soaring LNG imports envisaged in the next few years, the EU's Energy Union's strategic goal to diversify Europe's energy supply could be reached.

The European Commission published in November 2015 its State of the Energy Union Report in which the Commission reported on the progress made for the first time since the EU launched its Energy Union Framework Strategy in February 2015. At the same time, the European Commission adopted a list of 195 key energy infrastructure projects, known as the Projects of Common Interest (PCIs), which will enable the build-up of the Energy Union by integrating the energy markets in Europe, and by diversifying the energy sources and transport routes.

Conclusion

It remains to be seen how the European Commission will react to the gauntlet thrown down by the Nord Stream 2 initiative, especially with the harsh opposition from the central and eastern European countries that rallied around Poland. Nonetheless, at this moment it is certain that the EU will support projects related to the Southern Gas Corridor, as clearly indicated in its list of PCIs issued in November. With the Turkish-Russian row over Syria, and

ever closer cooperation between Turkey and Azerbaijan on the TANAP project, it is clear that the EU will increasingly eye the eastern Mediterranean supply route in an attempt to boost its Energy Union.

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