

Putin's Oily Politics

Energy in the executive, Kremlin-style.

BY IRWIN M. STELZER

What do Mikhail Khodorkovsky, Mikhail Gutseriev, and John Browne have in common? They all thought their desire for profits from Russia's vast oil reserves trumped Vladimir Putin's lust for power. Khodorkovsky now languishes in a Siberian jail. When his sentence is served, he will be rearrested and charged with crimes that will get him another 28 years in a prison from which he is unlikely ever to emerge. Gutseriev, head of mid-sized oil company RussNeft, was recently charged with "large-scale tax evasion" and conducting illegal activities as part of an "organized group," the same charges laid against Khodorkovsky. It seems that Kremlin deputy chief of staff Igor Sechin, the onetime KGB agent who heads state-owned Rosneft, which took over Khodorkovsky's Yukos oil company, "is extremely ambitious in regard to [RussNeft's] assets," according to press reports.

Which brings us to Lord Browne, the recently retired chief of British Petroleum who also thought there was money to be made in Russian oil. He set up TNK-BP, a joint oil and gas venture with a group of Russian billionaires. It is Russia's fourth largest oil company, accounts for about 25 percent of BP's global production, and is developing the huge Kovykta gas field in eastern Siberia. Or not. Oleg Mitvol, deputy head of Russia's Federal Resource Management Agency, and the man who magically acquired Boris Berezovsky's newspaper assets

when that "oligarch" decided that residence and asylum in Britain would contribute more to his longevity than would continued residence in Russia, has decided that TNK-BP is in violation of its license to develop the Kovykta field. It seems that TNK-BP is not producing the quantities specified in its contract because—get this—it can't get a permit from the Russian government to export Kovykta's gas to China; that market is now reserved for Gazprom.

This ratchets up the pressure on the three billionaire partners of BP in the joint venture to sell out to state-controlled Gazprom—several former KGB agents grace its board—especially after an appeals court in the east Siberian city of Irkutsk ruled last week that "it is out of our jurisdiction to review the submitted documents." A banker familiar with the matter told the *Financial Times*, "This is just going to be a phone call. If they are told to sell, they will sell." Which might be soon: Late last week the Natural Resources Ministry postponed a final decision because of the "complexity of the issue," which means the government is deciding on the precise form of the inevitable takeover.

Browne was not alone in planning a strategy around Russian resources. Royal Dutch Shell was induced to cede control of its \$22 billion Sakhalin-2 natural gas project to Gazprom after environmental authorities—namely Oleg Mitvol, now the scourge of TNK-BP—threatened to levy a \$30 billion fine and even close down the project. Control goes to Gazprom, and a special dividend of about \$1 billion per year goes to Russia's treasury.

One way or another, the state's share

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of Russian oil production has risen from about 28 percent to more than 50 percent—and that does not include the TNK-BP assets, ticketed for state control. Control of gas production now also rests with the state. Russia rakes in \$600 million every day from the sale of its oil and gas, most of it from sales to the European Union. Half of the E.U.'s gas imports come from Russia, with newer members Hungary and the Czech Republic just about completely dependent on Russian gas.

Worse still, Russia has successfully gained control of the pipeline networks that deliver fuel to the West. Last month, Putin persuaded the presidents of Turkmenistan and Kazakhstan to send their gas through a pipeline being built along the Caspian Sea coast en route to Western markets via Russian and Russian-controlled territories. It seems like only yesterday that I was briefed at the State Department on plans to build a new pipeline under the Caspian Sea that would hook up with existing lines through the Caucasus and Turkey, bringing Central Asian gas to Europe without passing through a Russian bottleneck. Those plans are now all but dead.

Putin is still taking no chances that the United States and the E.U. might revive that plan. So Gazprom has bought a significant stake in the Central European Gas Hub (CEGH) from an Austrian energy group, OMV, that operates gas storage facilities in Baumgarten, close to the Hungarian border. Any gas that bypasses Russian territory would pass through that hub en route from the Caspian area and the Middle East. The memorandum of understanding between Gazprom and OMV quite correctly describes the facility that has fallen under Russian control as “the most important gas hub in continental Europe.”

Putin also recently approved plans by Transneft to build an oil pipeline to the Baltic port of Primorsk, bypassing Belarus, the Czech Republic, Hungary, Poland, and Slovakia.

Russia's president has managed, brilliantly it must be conceded, to use his nation's oil and gas resources in a way that his predecessors never man-

aged to use the Red Army—to gain huge influence in Western Europe. “If power is measured by the fear instilled in others—as many Russians believe—[Putin] is certainly winning,” observes the *Economist*.

None of this would matter if we were dealing with ordinary commercial transactions, aimed at maximizing the value of Russia's natural endowments. But that is not the case. When Sergei Kuprianov, press spokesman for Gazprom, described its natural gas operations as “normal business,” former British ambassador to Uzbekistan Craig Murray commented, “Normal business is the last thing Gazprom is involved in.”

First, Gazprom is an important weapon in Putin's program of eliminating dissenting voices in Russian media. Gazprom Media took over what had been the country's only independent television channel after Putin closed it down. The company also bought two of Russia's large and once-independent newspapers, and Alisher Usmanov, chairman of Gazprominvest Holdings, the company's financial arm, bought the remaining one—after which the editor was fired and the defense correspondent had a fatal fall from a third-story window. Gazprom's control of the media is so complete that Ambassador Murray reports, “The era of free speech . . . is now over.”

Second, the takeovers of Shell, BP, and other assets hardly represent transactions at market prices between willing parties. Putin takes his instruction from Mario Puzo's *The Godfather* rather than Adam Smith's *Wealth of Nations*, and makes potential sellers offers they can't refuse: my price or nothing if you are a foreign corporation with billions already sunk in Siberia, and my offer or a long visit with Khodorkovsky if you are within my reach.

Third, Putin's goal is not profit maximization. It is to gain substantial influence over the foreign policies of European countries and the United States. He has already shown that he is willing to cut off gas supplies to Europe, and he cooperates with OPEC to damage the American economy by

keeping oil prices at cartel-set levels. Cruise missiles and a nuclear umbrella might have prevented the Red Army from rolling across Europe, but they are no match for supply cutoffs that can throw Western economies into recession and freeze consumers.

Consider just one example. Russia wanted to buy Lithuania's Mazeikiai oil refinery, but the former Soviet prisoner-state decided to sell to a Polish group. So Russia closed the pipeline to that refinery, allegedly for maintenance—which has been going on for a year and promises to continue indefinitely. If Russia sought to reassert control over its former satellite, would NATO countries risk a cutoff in their vital fuel supplies by opposing that move? Don't bet on it.

Russia has achieved this dominant position for two reasons. The first is that the world's capitalists behave as Lenin knew they would: “They will furnish credits . . . supply us materials and technical equipment which we lack, . . . restore our military industry for our future attacks against our suppliers.” (That is not as memorable as the usual paraphrase—“The capitalists will sell us the rope with which to hang them”—but then Lenin wasn't given to pithy prose.) The Russian state was able to take control of Gazprom only because Western banks saw fit to lend over \$7 billion, collecting appropriate fees. The gaggle of investment bankers, lawyers, and lobbyists in London, New York, and Washington who represent Russia in its financial transactions constitute a lobby of “useful idiots,” to borrow again from Lenin, ready to speak up on behalf of the international thuggery that has become Putin's signature operation.

The West has supplied Russia with the technical skills needed to exploit oil and gas resources in largely inaccessible areas, poured capital into Russian-controlled companies, and sold important bits of Western energy structure to Gazprom, which aims to be “the biggest energy company in the world,” according to Dmitry Medvedev, the company's chairman and, not incidentally, the first deputy prime minister of the Russian Federation. Never mind

that Russia will not allow such foreign investment in its infrastructure, or that it is using the proceeds of its oil and gas wealth to beef up its obsolete military. "Our military is the second-most-powerful force in the world after America's," a key Russian official trumpeted on the eve of the E.U.-Russian summit in mid-May.

The second reason Russia has gained such a dominant hand in all of its negotiations with energy-dependent countries—it has, for example, refused to discuss reducing the \$400 million it charges Europe's commercial airlines to overfly Siberia—is the inability of the West to forge a common strategy. "It is not a sustainable system—the Germans siding more with the Russians than with their own E.U. partners," says Katinka Barysch, an analyst with the Centre for European Reform.

The ingredients of such a Western strategic response are obvious: Increase storage facilities as insurance against gas-supply interruptions; finance (subsidize if necessary) pipelines that avoid Russian-controlled territories; refuse to sell infrastructure facilities to Gazprom; reduce the monopoly profits of E.U. distributors by liberalizing domestic markets; remove impediments to the construction of terminals that would receive liquefied natural gas from Africa and the Middle East; and unite to create countervailing buyer power, rather than deal individually with Russia.

Tony Blair is surely right that "energy policy is creating . . . new tensions in international relations." Russia is "prepared to use [its] energy resources as an instrument of policy." But the West is unprepared to use its financial and technical resources in the same way. German chancellor Angela Merkel, who grew up in East Germany when Putin was a KGB officer there, has had some harsh words for Putin, but what really counts is that a German group is providing 49 percent of the financing of a \$9 billion project to increase Germany's reliance on Russia even more. It is no coincidence, as the left was wont to say, that Gerhard Schröder arranged this deal while chancellor, and immediately upon los-

ing to Merkel was hired by the venture to serve as its chairman at what is said to be a handsome salary, indeed.

Failure to look ahead and resist the comforting warmth of the Rus-

sian bear hug, warns Britain's outgoing prime minister as he heads off into the sunset, "could be as crucial to our country's [and, the West's] future as defense." No one is listening. ♦