

Is Azerbaijani Gas a Game Changer in Balkan Energy Geopolitics?

Plamen Dimitrov*

Until now, the Russian company Gazprom has been the dominant gas supplier of the Balkan countries. Most of the projects for new gas pipelines in the Balkans have failed or have become stagnant in recent years for two main reasons: lack of gas to feed them (Nabucco, ITGI, Bulgaria's "Balkan" gas hub), or an adverse geopolitical environment (South Stream, Turkish Stream). But it is already clear that Azerbaijani gas from the Shah Deniz field will reach Balkans through the Southern Gas Corridor. This article examines the Balkan routes of the Azerbaijani gas, and answers the question of how this new source of gas will influence the energy geopolitics of Turkey, Bulgaria, and Greece. The conclusion is that the gas from Shah Deniz will trace out a new energy corridor through the southern part of the Balkans. Pursuant to this, an additional gas supply infrastructure could be built around this corridor – LNG terminals, interconnectors and new pipelines to bring gas from Turkmenistan, Iraq, or from the Eastern Mediterranean to Europe. Azerbaijani gas will, to a significant degree, act as a game changer in the Balkan energy geopolitics, although Gazprom will retain its role as a main supplier for the region.



* Dr. Plamen Dimitrov is the Head of the Eurasia Sector at the Bulgarian Geopolitical Society

Introduction

In the spring of 2016, a combination of geopolitical and economic factors created the impetus for projects on alternative gas deliveries in the region of South-Eastern and Southern Europe. These projects are part of the Southern Gas Corridor of the EU. The gas will be transferred through three consecutive pipelines - the South Caucasus (SCP) from Baku to Erzurum in Turkey; the Trans-Anatolian (TANAP) which will cross Turkey from east to west; and the Trans-Adriatic pipeline (TAP), which will start from Greece to bring the gas to Italy through Albania and under the Adriatic Sea. This gas transmission system will be fed by the Azerbaijani Shah Deniz gas field, located in the Caspian Sea.

This article explores the Balkan routes of the Azerbaijani gas, and answers the question of how these new gas supplies will influence the energy geopolitics of Turkey, Bulgaria, and Greece. Until now, the Russian company Gazprom has been the dominant gas supplier for the Balkan countries. It is understandable that Russia will try to retain this position. But the Balkans are also important for Gazprom as a transit route that could bring Russian gas to the Central Europe and Italy, thereby diminishing the transit role of Ukraine. Such a development is not desirable for the European Commission. Brussels prefers to encourage alternative gas supplies, and to some extent plays the role of arbiter in the struggle among the different gas projects in the Balkans.

It is for this reason that the geopolitics of Balkan gas is very dynamic, featuring many unknown quantities. Most of the projects for gas pipelines in the Balkans have failed or have become stagnant in the recent years for two main reasons: lack of gas to feed them (Nabucco, ITGI, Bulgaria's "Balkan" gas hub) or an adverse geopolitical environment (South Stream, Turkish Stream).

It is worth mentioning that with the exception of Turkey (which is a big gas consumer), and Romania (which has its own production, fulfilling more than 90% of its domestic consumption), all other Balkan countries have small or even non-existing gas markets. This is why even comparatively modest new supplies can seriously affect the gas geopolitics in the region.

Table 1. Russian Gas Exports to the Balkan countries in 2015 (in billion cm)

Turkey	Bulgaria	Greece	Serbia	Romania	Bosnia	Macedonia
27	3,11	1,98	1,68	0,18	0,20	0,06

Source: Gazprom Export website; <http://www.gazpromexport.ru/en/statistics/>

The first part of the paper explores the prospects of the Southern Gas Corridor – its potential supply sources, financing, and project schedule. After that it examines the importance and competitiveness of Azerbaijani gas for the Turkish, Bulgarian, and Greek energy markets. The potential synergy between the pipelines from the Southern Gas Corridor and other gas transmission projects in the Balkans (LNG terminals, interconnectors) will also be analyzed. Finally, the paper discusses the influence of Azerbaijani gas on the dynamics of the Balkan energy trade.

The Southern Gas Corridor – problems and perspectives

The structure of the Southern Gas Corridor was shaped back in 2013, when the shareholder in the Shah Deniz project decided that Azerbaijani gas would be transferred through TAP in order to reach European markets.

The TANAP and TAP rely on gas from the Phase 2 of the Shah Deniz field (SD2) development. It is expected that after 2018, SD2 will add 17 bcm/a to the 9 bcm/a produced from the Phase 1 of this field. The gas from SD2 has been already contracted: 6 bcm/a to go to the Turkish market, 1 bcm/a each for Bulgaria and Greece, with the remaining 8 bcm supplied Italy and destined for buyers in Europe.

The main engine of the TANAP project is Azerbaijan. This is understandable as Azerbaijan is the party most interested in bringing its gas to European and Turkish markets. But some large international companies are also involved in the extraction of Azerbaijani gas as well as its transportation to the international markets. The leading company in SD2 is the British BP (former British Petroleum). Azerbaijanis have a majority stake (58%) in TANAP, while BP has 12%. There are three leading companies in TAP: Azerbaijani SOCAR, BP and the Italian Snam.

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Table 2. Distribution of shareholders in the gas production project Shah Deniz and in the South Caucasus (SCP), TANAP and TAP gas pipelines as of August 2016

	Shah Deniz	SCP	TANAP	TAP
SOCAR (Azerbaijan)	16,7%	16,7%	58%	20%
BP (UK)	28,8%	28,8%	12%	20%
LUKoil (Russia)	10%	10%	-	-
Petronas (Malaysia)	15,5%	15,5%	-	-
TPAO (Turkey)	19%	19%	-	-
BOTAS (Turkey)	-	-	30%	-
NIOC (Iran)	10%	10%	-	-
Snam (Italy)	-	-	-	20%
Fluxys (Belgium)	-	-	-	19%
Enagas (Spain)	-	-	-	16%
Axpo (Switzerland)	-	-	-	5%

The gas extraction from SD2 and the three pipelines that have to bring the gas to Europe are an elements of an undivided business chain. This means that all these projects should be synchronized with each other.

According to the latest estimates, the total cost of all projects of the Southern Gas Corridor is a little over \$39 billion – \$23.8 billion for SD2, including the SCP planned expansion (SCPx); \$9.3 billion for TANAP; and \$6 billion for TAP. Before the sharp fall of oil prices the cost of the Southern Gas Corridor was expected to be about \$45 billion, due to the impact of energy prices on the prices for material and services used for the development of SD2 and the pipelines.¹

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The SD2 and subsequent pipelines will be built on the basis of project finance, which means the majority financing will be accumulated on the financial markets. There are two main challenges regarding the financing of the SGC. First, it is very expensive, and second, the low oil prices have made financial institutions very cautious when financing major energy projects.

Azerbaijan has major stakes in all elements of the Southern Gas Corridor, and has to raise \$11.45 billion, which is equal to

¹ Natural Gas Europe (2016) ‘Energy prices allow cost cuts in Caspian’, Available at: <http://www.naturalgaseurope.com/energy-prices-help-cost-reduction-for-sgc-29962> (Accessed: 30 August 2016)

its shares in SD2, SCPx, TANAP, and TAP. For the time being Azerbaijani share in the SGC is financed mainly by the State Oil Fund of Azerbaijan (Sofaz). Until August 2016, Sofaz financed Southern Gas Corridor Co (a special company created in order to unify the Azerbaijani stakes in SD2, SCPx, TANAP and TAP) to the tune of \$2.5 billion, with another \$1.7 billion provided by the Azerbaijani Ministry of Finance and SOCAR.² March 2016 saw a major success in the project's development, when the Southern Gas Corridor Co raised \$1 billion in 10-year Eurobonds on international financial markets. At the end of summer of 2016 Azerbaijan had to raise a little bit more than half of the money needed to finance the country's share in the SGC. Negotiations with lending giants, such as the European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD), the World Bank, and the Asian Development Bank are underway. Bearing in mind the strong commitment of the government, the Southern Gas Corridor Co will likely be able to raise the required \$6.2 billion to finish the projects that will bring Azerbaijani gas to Europe. It should be even easier for a company with a reputation like BP's to secure financing for its share in the SGC.

In June 2016 Azerbaijani energy minister Natig Aliiev declared that Shah Deniz 2 was 71% complete;³ TANAP - 55% complete; and TAP - 10% complete.⁴ In fact, the building of TANAP started officially on March 17 2015. The official groundbreaking ceremony for TAP took place on May 17 2016. According to SOCAR, the first gas from SD2 will be on the market in 2018; TANAP will be completed in the same year, and Azerbaijani gas will reach Europe (Greece and Italy) in 2020.⁵ However, experts and some diplomats in Azerbaijan are a little more skeptical. They do not think Azerbaijani gas will flow through TAP any earlier than 2021-2022.

The two projects that will transport gas from SD2 to Europe – TANAP and TAP - envisage the expansion of their initial capacity, relying on future increases in Azerbaijan's production.

2 Natural Gas Europe (2016) 'Caspian Overview: SD2 Cuts Capex, Baku Optimistic', 25 August, Available at: <http://www.naturalgaseurope.com/caspian-overview-sd2-cuts-capex-baku-optimistic-31235> (Accessed: 30 August 2016).

3 At the end of August 2016 BP said SD2 is "over 77% complete in terms of engineering, procurement and construction". Natural Gas Europe (2016) Caspian Overview: SD2 Cuts Capex, Baku Optimistic.

4 Natural Gas Europe (2016) 'Energy prices allow cost cuts in Caspian', Available at: <http://www.naturalgaseurope.com/energy-prices-help-cost-reduction-for-sgc-29962> (Accessed: 30 August 2016).

5 Author's interview with Vitaliy Baylarbayov, Deputy Vice-president of SOCAR, Baku, 3 June 2016.

Indeed, Azerbaijan's continental shelf has other prospective middle-sized fields. But in the Caspian Sea there is a serious dearth of deep-sea drilling rigs, which delays prospecting and development of the fields.⁶

In the next 10 years only one new Azerbaijani field will start to produce gas. This is Absheron, where SOCAR owns 40%, and the French company Total (operator of the field) also holds 40%. The expected production from Absheron is 5 bcm/a, and it has to start as early as 2022. It is not certain whether this gas will be directed for export, given Azerbaijan's growing domestic consumption. But after 2030, an additional 15 bcm/a of Azerbaijani gas might be brought on stream, through a combination of expansion programs at existing fields along with development of new fields.⁷

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It is doubtful that in the foreseeable future that gas from Iraq, Iran or Turkmenistan will be carried by the Southern Gas Corridor. In Iraqi Kurdistan there are significant gas fields and plans for export to Turkey, but in view of the security problem, export are unlikely to start soon. The 2015 nuclear agreement with Iran put country back on the list of potential gas suppliers for Europe. Iran has strong energy potential, but the oil and gas sector requires massive investments, and these are not forthcoming in the short term. For the time being, the country has no extra gas to export; in addition, Europe is likely not to be a priority direction for exports from the main Iranian field South Pars. It is more probable that in a few years, Iran will start exporting gas to the closer markets of Pakistan, India and Iraq, all of which offer good prospects. Following the successful example of its neighbor Qatar, Iran can invest in the building of LNG terminals.

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So far, the efforts of the European Union towards the construction of the Trans-Caspian pipeline to carry Turkmen gas to Europe have failed. In September 2011, for the first time in its history, the European Commission received a mandate to carry out negotiations for signing a contract with Turkmenistan and Azerbaijan on behalf of the EU.⁸

⁶ The construction of the first floating new generation drilling rig of SOCAR will be completed by the end of 2016. According to the experts Azerbaijan needs at least four such floating drilling rigs. See Azernews (2014) First new generation drilling rig to be finished by late 2016, 1 May, AVAILABLE AT: [HTTP://WWW.AZERNEWS.AZ/OIL_AND_GAS/66642.HTML](http://www.azernews.az/oil_and_gas/66642.html) (ACCESSED: 30 AUGUST 2016).

⁷ Rzayeva, G. (2016) Materializing mega-gas projects in Azerbaijan in the low price environment. Talk at the Natural Resources Forum, London, 28 June, Available at: <http://naturalresourcesforum.com/companies/oxfordinstitute2/> (Accessed: 30 August 2016).

⁸ EU starts negotiations on Caspian pipeline to bring gas to Europe, European Commission web-site, Available at: http://europa.eu/rapid/press-release_IP-11-1023_en.htm?locale=en (Accessed: 30

However, it remains unlikely that a contract for the Trans-Caspian gas pipeline will be concluded in the foreseeable future. Here, the insurmountable obstacle is the Russian resistance to this pipeline and the reluctance of Turkmenistan to undertake more serious geopolitical and financial commitments in regard to the project. In October 2015 Russia attacked positions of the Islamists in Syria with cruise missiles launched from ships based in the Southern part of the Caspian Sea. This demonstration of power aimed to strengthen the position of Moscow as indispensable military factor not only in the Middle East, but also in the Caspian region. In this situation, companies are unlikely to be willing to invest billions of dollars in a project opposed by Russia.

The only realistic option for transporting the modest volumes of Turkmen gas to the SGC is to link the gas platforms in the western and eastern part of the Caspian Sea via subsea pipeline. In this regard, the Malaysian company Petronas can play a major role. Petronas holds a 15.5% share in Shah Deniz, as well as a Production Sharing Agreement with Turkmenistan for the oil and gas in Block-1 in the Caspian Sea. The distance between Shah Deniz and Block-1 is not large, and Russia can probably eventually accept a small-scale pipeline (which I propose to call “Trans-Caspian pipeline-light”, “TCP-light”). This smaller pipeline will enable Petronas to transfer its gas to Azerbaijan and subsequently to the SGC.⁹

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In light of the above, my prognosis is that the Southern Gas Corridor will receive little or no gas (i.e. less than 5 bcm/a) of Iraqi, Iranian or Turkmen gas until 2024-2025 at least. Thus in the short to medium term, Azerbaijani gas will form the backbone of the SGC.

Azerbaijani gas and Turkey's energy dilemma

Turkey has the biggest gas market in the Balkans, and in the period 2009-2014, its consumption grew every year. It is the most commercially suitable market for Azerbaijani gas, due to the shorter transportation distance, expected demand growth, and high prices.¹⁰ At the same time, the Turkish gas market is very

August 2016).

9 Neftegaz.ru (2016) Petronas shows in Azerbaijan an interest to Trans-Caspian gas pipeline, 29 July, Available at: <http://neftegaz.ru/en/news/view/151582-Petronas-shows-in-Azerbaijan-an-interest-to-Trans-Caspian-gas-pipeline> (Accessed: 30 August 2016).

10 Rzayeva, Gulmira (2015) The Outlook for Azerbaijani Gas Supplies to Europe: Challenges and Perspectives. Oxford Institute for Energy Studies, Paper NG 97, June, p.67.

complicated, politically sensitive, and its liberalization is still ongoing.

Azerbaijan began to export gas for Turkey in 2007, and additional 6 bcm/y will be exported after 2018. Turkey has three other options for gas imports – Russia, Iran and LNG. Gazprom has been Turkey’s main gas supplier, providing more than half of Turkey’s imports until the beginning of 2016.

Table 3. Import of natural gas in Turkey in 2015 and the first quarters of 2016 (in bcm)

Year/ Source	Russia	Iran	Azerbaijan	LNG	Total
2015	26,6 (56,4%)	7,8 (16,5%)	5,3 (11,2)	7,5 (15,9)	47,2
Q1 2016	6,35 (48,2%)	2,18 (16,6%)	1,71 (13%)	2,93 (22,2%)	13,17
Q1-Q3 2016	16,7 (49,4%)	5,56 (16,4%)	4,85 (14,3%)	6,72 (19,9%)	27,11

Sources: BP, Azernwes¹¹ and Natural Gas Europe¹²

At the end of 2014, Russian President Putin initiated the Turkish Stream pipeline – the project that could strengthen Russia’s position in the Turkish market. Even a single string of Turkish Stream (15,75 bcm/a) could enable Gazprom to flood the Turkish market with Russian gas; the total transmission capacity of the Blue Stream, the Trans-Balkan pipeline, and Turkish Stream will reach 46 bcm/a. Russia’s intention to use Turkish territory as a gas transit route to the EU is not realistic. Thus the realization of the Turkish Stream project will reflect on Gazprom’s expectations

and ambitions regarding its presence in the Turkish gas market.

The geopolitical conflict between Moscow and Ankara following the downing of a Russian military aircraft in November 2015 has shown that gas dependence on Russia is a threat to Turkish energy security. The availability of four gas import sources is insufficient if the share of the main supplier (Gazprom) is over 50%. Importing Iranian, Iraqi or Israeli gas could also give rise

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11 Azernwes (2006) ‘Turkey ups gas purchase from Azerbaijan, decrease from Russia’, Available at: http://www.azernews.az/oil_and_gas/97376.html (Accessed: 30 August 2016).

12 Natural Gas Europe (2016) ‘Turkey Takes Less Russian Gas’, Available at: <http://www.natural-gasworld.com/turkey-takes-less-russian-gas-34621> (Accessed: 30 November 2016).

to potential geopolitical complications. Therefore, Azerbaijan is not only the biggest, but also the most reliable gas supplier for Turkey, given the deeply rooted relations of the strategic partnership between Ankara and Baku. Turkey will keep trying to reduce Russia's share of its gas imports to below 50%, because major dependence on Russia is perceived as a threat to national energy security. If Ankara will agree to only one string of the Turkish Stream pipeline, it will mean the share of Russian gas on the Turkish market will not increase and the contract for importing gas from Shah Deniz-1 to Turkey will be prolonged beyond its expiration date (which is 2021).

The Greece-Bulgaria interconnector and the synergy between the Azerbaijani gas and the LNG terminal in Alexandroupolis

Table 4. Bulgaria's gas consumption and imports during 2016-2023, Prognosis (bcm)

	2016	2017	2018	2019	2020	2021	2022	2023
Consumption	3,1	3,3	3,5	3,7	3,8	4,0	4,1	4,2
Import	3,035	3,23	3,3	3,3	3,2	n/a	n/a	n/a

Source: Bulgartransgaz¹³

Bulgaria is one of the countries that stands to obtain gas from SD2. This will only be possible if the Greece-Bulgaria gas interconnector (IGB) is built on time. This project is being developed by the joint venture company ICGBAD. The initial capacity of the IGB will be 3 bcm/a, with a possibility of upgrading it to 5 bcm, which could be achieved through the installation of an additional compressor station. The main gas flow in the IGB will be from Greece to Bulgaria, but the pipeline will also be equipped to offer physical reverse flow.

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The IGB has two weak points – its economic feasibility, and the shareholder structure, in which Bulgarian Energy Holding (BEH) has 50%, and the remaining 50% is held by IGI Poseidon – a joint venture company between the Greek state controlled company DEPA and the Italian Edison. The majority owner of Edison (with 99,4% of shares) is the French Electricite de France (EdF), controlled by the French government.

¹³ Bulgartransgaz (2016) 'Ten-year Networking Development Plan of Bulgartransgaz', 31 March, Available at: http://www.bulgartransgaz.bg/files/useruploads/files/ITO/10YP/TYNDP_31-03-2016-en%201.pdf (Accessed: 30 August 2016).

The more active partner in the ICGB is the BEH. The Bulgarian government decided to issue 109 million Euro worth of guarantees for the IGB project in 2016.¹⁴ The gas interconnector Greece-Bulgaria is the only state-guaranteed investment project included in the Law for the State Budget of Bulgaria for 2016. Bulgaria's partners in ICGB – DEPA and Edison - have never expressed uncertainty about the project, but do not play active roles. Their participation is the result of diplomatic pressure from the European Commission and the US (through Amos Hochstein - Coordinator for International Energy Affairs at the US Department of State), who are interested in the implementation of the IGB project.

In February 2016, DEPA and Edison signed a Memorandum of Understanding (MoU) on natural gas deliveries “across the Black Sea from Russia via third countries to Greece and from Greece to Italy in order to establish a southern route to deliver Russian natural gas to Europe.”¹⁵ Bearing in mind the fate of the South Stream project, it is certain that the European Commission will not support any projects aimed at delivering Russian gas to the EU bypassing Ukraine. This is why the above-mentioned “southern route” for Russian gas is impossible. The aim of this MoU was mainly to discourage projects for alternative gas supplies to the Balkans and Italy, and to support Russian efforts to promote the Nord Stream-2 pipeline project. But the fact that two of the partners in the ICGB agreed to express support for Gazprom indicates close relations with the Russian gas giant. In fact, EdF (the owner of Edison) and Gazprom have a common business venture. In 2012 the two companies reached a deal to jointly invest in gas-fired power plants in Europe. The gas for these power plants should be supplied “exclusively by Gazprom”.¹⁶ It is worth mentioning that EdF was one of Gazprom's three Western partners in the South Stream project.

It is understandable that Gazprom has no interest in the success of the IGB project, because it could bring competitors to the Bulgarian market, and in the medium term, even to the other Balkan markets. The fact that some partners in the ICGB are

¹⁴ Novinite.com (2016) ‘Bulgaria-Greece Gas Link Gets BGN 215 M in State Guarantee’, Available at: <http://www.novinite.com/articles/171550/Bulgaria-Greece+Gas+Link+Gets+BGN+215+M+in+State+Guarantee> (Accessed: 30 August 2016).

¹⁵ Gazprom, DEPA and Edison sign Memorandum of Understanding, Gazprom web-site, 24 February 2016, Available at: <http://www.gazprom.com/press/news/2016/february/article267671/> (Accessed: 30 August 2016).

¹⁶ The New York Times (2012) ‘Gazprom Reaches Deal With EDF to Invest in European Power Plants’, 22 June, Available at: http://www.nytimes.com/2012/06/23/business/global/gazprom-reaches-deal-with-edf-to-invest-in-european-power-plants.html?_r=1 (Accessed: 30 August 2016).

strategic partners of Gazprom does not bode well for the project's success, and its shareholders structure is not very suitable for the expected gas flows in the region.

But the ICGB company was created in January 2011. At that time, the Greece-Bulgaria interconnector was designed as a northern branch of the ITGI (Interconnector Turkey-Greece-Italy) pipeline. That is why the two shareholders of the ITGI - DEPA and Edison – joined the ICGB company. Then in 2013, the Shah Deniz consortium chose the TAP for the transportation of Azerbaijani gas to Italy, and the ITGI was shelved.

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At present, DEPA and Edison have little motivation to implement the IGB project. Bulgaria is eager to build the interconnector with Greece because it will give it a chance to diversify the country's gas supplies, but DEPA and Edison are not obliged to worry about Bulgarian energy security. They are interested in generating profits, but as mentioned, the profitability of the IGB is problematic.

In this situation it is logical for the shareholder's structure of the ICGB company to be diversified and for some of the participants of the Shah Deniz consortium, the TANAP and TAP to join the Greece-Bulgaria interconnector project. Azerbaijan's SOCAR has been invited by Bulgaria to join the ICGB, but for the time being their answer is "no". Entering ICGB can strengthen the SOCAR's strategic positions in the Balkans, but the low oil price means that this is not a good moment. SOCAR's revenues have fallen sharply, and Azerbaijani gas strategists have been carefully calculating every investment expenditure. The same is true for the other big shareholders in the Shah Deniz project – BP and Petronas.

It is clear that until at least the mid-2020s Azerbaijani gas will be insufficient to utilize the full capacity of the IGB. This is why the ICGB has been looking for other sources of gas, first of the planned LNG regasification terminal in Alexandroupolis in Northern Greece. The main driver of this project is the private Greek company Gastrade, but two US companies are also interested in the Alexandroupolis LNG terminal – Chenier Energy, which began exporting LNG from the US in 2016, and Noble Energy, the first operator to discover offshore natural gas resources in Israel and Cyprus. Bulgaria is also interested in the future LNG terminal, as are the shareholders in IGB. DEPA and Edison. Recently Iran has also shown interest in the

Alexandroupolis LNG terminal.¹⁷

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The plans for the Alexandroupolis LNG terminal are very ambitious – the envisaged capacity is 6,1 bcm/a, which is more than the current gas consumption of Greece and Bulgaria combined. According to some sources, the Alexandroupolis terminal is expected to cost \$415 million, although this estimate sounds too optimistic for a facility on this scale.¹⁸ Gastrade's website shares some technical details for the terminal – it will be a floating facility, situated at 17,6 km from the town of Alexandroupolis, and 10 km from the nearest opposite shore. The LNG will be gasified at the regasification units and will be moved to the 24 km subsea pipeline via a submerged turret and a set of flexible risers. The terminal will have a storage capacity of up to 170 000 cub. m of LNG.¹⁹

The fate of the IGB depends on the success of the Southern Gas Corridor and the LNG terminal in Alexandroupolis. In the spring of 2016, the first phase of the market test (Expression of interest) for the purpose of booking capacity in the interconnector was conducted. Nine non-binding Expressions of Interest were received.²⁰ A total aggregate capacity of 4.3 bcm/y was requested for gas transportation services in firm forward mode from Greece to Bulgaria and approximately 1 bcm/y in firm reverse mode from Bulgaria to Greece.²¹ These volumes do not include the 1 bcm/y gas from SD2 which has been contracted by Bulgaria. But almost half of this 4,3 bcm/y (2 bcm) was booked by Gastrade and the final decision of this company will depend on the progress of the LNG terminal in Alexandroupolis. Azerbaijani SOCAR participated in the first phase of the IGB market test, with a very small volume. SOCAR intended to confirm its offer during the second bidding phase of the market test.²² It was launched in

17 Shipping Herald (2016) 'Greece Seeks Role As Gateway For Iran's Energy Exports To Europe', Available at: <http://www.shippingherald.com/greece-seeks-role-as-gateway-for-irans-energy-exports-to-europe/> (Accessed: 30 August 2016).

18 The Maritime Executive (2015) 'Cheniere CEO Dismissed, Company Announces New LNG Investments', Available at: <http://www.maritime-executive.com/article/cheniere-ceo-dismissed-company-announces-new-lng-investments> (Accessed 30 August 2016).

19 Gastrade web-site; <http://www.gastrade.gr/en/the-company/the-project.aspx> (Accessed: 30 August 2016).

20 The nine firms were Bulgarian Bulgargaz, DEPA, Edison, SOCAR, Noble Energy, Gastrade, OMV Petrom – the Romanian subsidiary of Austria's OMV – as well as two Bulgarian private distribution companies, Citygaz and the Black Sea Technology Company.

21 Energy Press (2016) 'IGB developments in October, Romania extension prospects favorable' Available at: <http://energypress.eu/igb-developments-in-october-romania-bulgaria-pipeline-prospects-favorable/> (Accessed: 30 August 2016).

22 Author's interview with Vitaliy Baylarbayov, Deputy Vice-president of SOCAR, Baku, 3 June

August 2016 and was completed in the end of November. Five binding offers were received with total aggregate capacity of 1,57 bcm/y. All five companies want to transfer gas in firm forward mode from Greece to Bulgaria. The company ICGB considers the possibility to initiate a procedure for allocation of the remaining capacity of the interconnector, hoping new shippers will express interest in the IGB²³. If a new procedure is going to be launched, it means the building of the pipeline will be postponed and will not start in 2017.

The capacity of the IGB and the planned LNG terminal in Alexandroupolis will not be used fully, and its commercial viability is doubtful. But the new facilities for gas deliveries should be examined in the context of the overall picture of Balkan gas trade. Gazprom has a monopoly in Bulgaria, and dominant positions in Greece and Turkey. The breakup of this monopoly will strengthen the negotiating positions of Balkan countries and could result in better prices for imported gas. This is also consistent with the EU energy strategy, according to which each European country should secure gas supplies from at least three sources. But for the small Balkan countries, this goal is impossible if the governments rely exclusively on the mechanisms of the free market. This is why the EU is ready to allocate limited financial aid for some energy projects of critical importance. Both IGB and Alexandroupolis LNG terminal are on the EU's list of projects of common interest.²⁴

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The IGB is eligible for financial support through the European Energy Program for Recovery, in the amount of 45 million Euro. The decision for this financial support was taken in 2010 and the deadline for the utilization of these funds has been extended to 2018.²⁵ But this is only 20% of the expected budget. The ICGB company is applying for an additional grant of 35 million Euro from the European Commission, but the chances of receiving this sum are slim. Most probably, construction of the IGB will not start until the middle of 2017 because the IGB shareholders are

2016

23 Five binding offers were submitted in the binding phase of the market test for the Gas Interconnector Greece-Bulgaria. ICGB AD Press release, 02 February 2016, Available at: <http://www.icgb.eu/press> (Accessed: 03 December 2016).

24 Official Journal of the European Union (2016) 27 January. Commission Delegated Regulation (EU) 2016/89. Available at: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:JOL_2016_019_R_0001&from=EN (Accessed: 30 August 2016).

25 Author's interview with Teodora Georgieva, Executive Officer ICGB AD, Sofia, April 2016.

waiting on the progress of the project for the Alexandroupolis LNG terminal. This terminal itself can expect even greater percentage of financing from the EU, but here the required amount is even greater compared to that of the IGB.

The IGB can be a gateway for the Azerbaijani gas to Romania, and even Ukraine and Moldova. It will be possible thanks to the Bulgaria-Romania interconnector (between the towns of Ruse and Giurgu), which was completed in November 2016. The initial deadline for the completion of the Ruse-Giurgu pipeline was June 2013, but the completion was delayed due to technical problems during the construction of the underwater section of the pipeline. The total length of this interconnector is 25 km including 2,1 km under the Danube River. The capacity of the Ruse-Giurgu pipeline is 1,5 bcm/a from Bulgaria to Romania and 0,5 bcm/a from Romania to Bulgaria. The estimated total value of the project is 24 million euro, 8,9 million of which have been provided as a grant by the European Commission.²⁶ Owing to the lower pressure in the Romanian gas transmission system, in the initial stages only the flow of gas from Bulgaria to Romania will be possible. In order to enable the reverse flow – from Giurgu to Ruse – a compressor station will be built later on.

Possible role for SOCAR in the Greek gas market

Greece already has one LNG terminal in Revithoussa, not far from Athens. It began to operate in 2000 but only small part of its capacity has been used recently, because the pipeline gas delivered to Greece by Gazprom has been cheaper than LNG.

The Revithoussa LNG terminal belongs to the Greek gas transmission system operator DESFA. In 2013, SOCAR won the international tender for the privatization of DESFA offering 400 million Euro for 66% of the company. But after that the deal was delayed when the European Commission insisted that SOCAR to surrender a 17% share and offer it to a certified European operator. This would limit SOCAR's stake to 49%. The view in Brussels was that SOCAR should not control the gas transmission system of Greece at the same time as being its gas supplier. In the spring of 2016 it seemed the deal for DESFA was close to completion and Italian Snam was ready to acquire the 17% from SOCAR. But in July 2016 the parliament in Athens adopted an amendment proposed by the Greek energy minister Skourletis, which revised

26 Energynomics.ro (2016) 'Bulgaria-Romania gas interconnector may be ready this September', 25 July, Available at: <http://www.energynomics.ro/en/bulgaria-romania-gas-interconnector-may-be-ready-this-september/> (Accessed: 30 August 2016).

DESFA's asset base and limits the operator's earning potential. In this situation the price that SOCAR agreed for 66% of DESFA in 2013 was no longer reasonable.²⁷ Tough negotiations between SOCAR and the Greek government started in the summer of 2016. The letter of guarantee that was set to expire at the end of September 2016 has been extended twice by the Azerbaijani company, but until the end of November the outcome of the negotiations remained unclear. Finally, the negotiations failed and DESFA has not been sold.

The failure of DESFA's privatization will have serious repercussions for the Greek gas market. Recently SOCAR has become a big international trader with many overseas offices that buy and sell energy resources, including resources not produced by Azerbaijan.²⁸ SOCAR entrance into the Greek market could add a new dynamic to the gas industry in the country and the region as a whole. Now the Greek government has little chance of finding a new reputable buyer for the gas transmission operator.

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Summer of 2016 saw another important change in the conditions for the gas trade in South-East Europe. In a period of two months, three interconnection agreements were signed – between Bulgaria and Greek gas network operators Bulgartransgaz and DESFA; between the Bulgartransgaz and the Romanian Transgaz; and between the Transgaz and the Ukrainian UkrTransGaz.²⁹ The agreements became effective on October 1 2016. Theoretically, this means that from this date it is possible to use the existing Trans-Balkan pipeline delivering Russian gas to the Balkans in the reverse direction, and that the gas will be able to flow from south to the north, from Greece to Ukraine. “These agreements are a crucial step towards opening the Trans-Balkan pipeline system between Greece and Ukraine to transport gas and trade in line with EU rules,” the European Commission said in a press release.³⁰

27 Energy Press (2016) ‘Socar now one step away from exiting delayed DESFA sale’, Available at: <http://energypress.eu/socar-now-one-step-away-from-exiting-desfa-sale/> (Accessed: 30 August 2016).

28 Trend News Agency (2016) ‘SOCAR intends to export LNG’, Available at: <http://en.trend.az/business/energy/2656224.html> (Accessed: 3 Sept. 2016).

29 Bulgaria-Romania and Romania-Ukraine sign gas agreements; European Commission web-site, 19 June 2016, Available at: <https://ec.europa.eu/energy/en/news/bulgaria-romania-and-romania-ukraine-sign-gas-agreements> (Accessed: 3 Sept. 2016).

30 Ibid.

In practice, it is too early to say that all the barriers to gas trade between Greece, Bulgaria, Romania, and Ukraine have been removed – capacity trading platforms and capacity release mechanisms are in their initial phases, and the different transmission system operators operate under different tariff regimes.³¹ But the trend is towards the liberalization of the gas market in the region and the main impetus for that is coming from Brussels. The coincidence in the timing of signing and the overlaps in the content of the interconnection agreements between the four aforementioned transmission operators indicates that these agreements were inspired and even dictated by the European Commission.

Conclusions - The new dynamic of Balkan gas trade

The diversification of gas supplies for the Balkan countries is a game with many variables. The prices of the LNG and pipeline gas change repeatedly, and global gas demand is also very dynamic. After 2018, a sharp rise in the global supply of LNG is expected, mainly because of the opening of new export terminals in Australia and the US. According to the International Gas Union, in 2021 the total capacity of LNG producing facilities will be 46% bigger than it is in 2016.³² A real price war between gas exporters is possible, and the suppliers of pipeline gas could be also involved. That is the rationale behind the projects for LNG regasification terminals in the Balkans. In the new situation, the winners will be the gas buyers - but only those of them that have a diversified system of deliveries, allowing them to switch between suppliers. Azerbaijani gas, together with the LNG, is the most important opportunity to achieving a diversified supply system in the Balkans.

From a geopolitical point of view there are three major factors for the gas trade in the Balkans: the strained relations between the European Commission and Russia; sudden turns in the Russia-Turkey relations; and Azerbaijan's ambition to turn its geo-energy vector toward South-East Europe and Italy.

From a geopolitical point of view there are three major factors for the gas trade in the Balkans: the strained relations between the European Commission and Russia; sudden turns in the Russia-Turkey relations; and Azerbaijan's ambition to turn its geo-energy vector toward South-East Europe and Italy. The Balkan energy

31 Vassilev, I. (2016) 'The intersystem agreements and the Trans-Balkan pipeline – a game change', *Bulgaria Analytika*, 30 July, Available at: <http://bulgariaanalytica.org/en/> (Accessed: 30 August 2016).

32 2016 World LNG Report. International Gas Union, 12 April 2016, Available at: <http://www.igu.org/publications/2016-world-lng-report> (Accessed: 30 August 2016).

geopolitics should be examined against the backdrop of the relatively low global price of the energy resource, and gradual transition from regional to global gas trade.

One important factor for gas exporters to consider is the increasing role of the European Commission in the Balkans. In June 2016, the European Council (in the format of the Energy Ministers) decided that all gas-related intergovernmental agreements between EU member states and third countries must be examined by the Commission before they are signed. This decision is expected to be confirmed by the European Parliament.³³

In 2017, the transitional period for applying the Third Energy package of the EU in the countries from the Western Balkans that are members of the Vienna-based Energy Community will expire. It is expected that Georgia will become a member of the Energy Community by the end of 2016, and thus the European Commission will gain greater influence over the route of Azerbaijani gas to Europe.³⁴

In conclusion, there are numerous factors that will influence the dynamic of the Balkan gas trade over the next several years. The only certain new supplier of gas in the region is Azerbaijan. The gas from Shah Deniz will trace out a new energy corridor through the southern part of the Balkans. Later on, additional gas supply infrastructure could be built around this corridor – LNG terminals, interconnectors and new pipelines to bring gas from Turkmenistan, Iraq, or from the Eastern Mediterranean to Europe.

As a supplier of gas for the EU, Azerbaijan has two main advantages. Firstly, the gas from Shah Deniz can reduce dependence on Gazprom for the weakest part of the European energy security system – the Balkan states. Secondly, there is not that much Azerbaijani gas available, and its proportional share in EU consumption will never reach double-digits. Due to this there is no risk of new over dependency, as we currently see with Gazprom.

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33 Euractiv.com (2016) 'EU to vet member states' gas deals with Russia' Available at: <http://www.euractiv.com/section/energy/news/eu-to-vet-member-states-gas-deals-with-russia/> (Accessed: 30 August 2016).

34 Georgia Plans for Energy Overhaul. Natural Gas Europe, 13 June 2016, Available at: <http://www.naturalgaseurope.com/georgia-plans-for-energy-security-30077> (Accessed: 30 August 2016).

Returning to the initial question posed by this article, the answer would be that yes, Azerbaijani gas will be a game changer in the Balkan energy geopolitics to a significant degree, because of the expected deliveries from Shah Deniz. Most probably after the beginning of the 2020s, Azerbaijan will fulfill more than 20% of Turkey's gas needs, and for Bulgaria and Greece the share of the Azerbaijani gas will be even higher – a quarter of total consumption. But it is important to remember that Azerbaijan will never be a main gas supplier for the region – this is a role that Gazprom shall retain.