

Bringing Russian and Iranian Gas to the Georgian Market: Technically Challenging, Economically Unfeasible and Politically Costly?

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After the disintegration of the Soviet Union, the three South Caucasus countries found themselves in a power vacuum, which led to various geopolitical events and even catastrophes (such as territorial conflicts and separatism). However, this vacuum also enabled two of the newly independent South Caucasus countries – Azerbaijan and Georgia – to jointly implement major oil and gas projects, the Baku-Tbilisi-Ceyhan oil pipeline and Baku-Tbilisi-Erzurum gas pipeline, both of which bypassed Russia. Initially, the two states were dependent on Russia which was a key transit country for Azerbaijan and a major gas supplier to Georgia. After August War in 2008, Georgia suspended its gas imports from Russia, except the volume received as a ‘transit fee’ for the gas supplied to Armenia. Since 2007, Azerbaijan, by virtue of its vast energy resources, has been supplying the majority of Georgia’s oil and gas demand and almost completely met its strategic ally’s energy needs when the Russian supplies were cut down during 2008 war. However, a statement by Georgia’s Energy Minister Kakha Kaladze in September 2015 on the purchase of Russian and potentially Iranian gas by Georgia raised some questions. This article will examine the extent to which the purchase of Russian gas is realistic and compatible with Georgia’s national interests and to what extent it poses the risk to its relations with Azerbaijan, as well as the feasibility of bringing the Iranian gas to Georgia given the technical shortcomings and political backlash displayed by Russia. The author’s arguments are based on the reliability of Azerbaijan as both supplier and neighbor, as well as the technical difficulties and political repercussions respectively of bringing Iranian and Russian gas to Georgia.



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Azerbaijan-Georgia Energy Relations

After gaining independence from the Soviet Union in 1991, both Azerbaijan and Georgia launched their independent energy policies. The energy cooperation between Azerbaijan and Georgia through the realization of the Baku-Tbilisi-Ceyhan (BTC), Baku-Tbilisi-Erzurum (BTE), Baku-Supsa pipelines and other energy projects had a significant impact on the wider region.¹ The BTC, BTE and Baku-Supsa are essential components of the East-West Transport Corridor, which created deep and strong economic and political ties between Azerbaijan and Georgia.²

For the West, finding the alternative routes to bring Caspian oil and gas to Europe was crucial. For the West, finding the alternative routes to bring Caspian oil and gas to Europe was crucial. The strategic vision of the government of Heydar Aliyev created the initial foundations of the East-West corridor, the development of which is proceeding smoothly today with new energy projects and initiatives. Today, this strategy is led by President Ilham Aliyev, who has paved the way for the implementation of the Trans-Anatolian Pipeline (TANAP) and the Trans-Adriatic Pipeline (TAP).

An additional potential gas project that will link Azerbaijan and Georgia is the so-called Azerbaijan-Georgia-Romania-Interconnector (AGRI), which envisages bringing Azerbaijani gas to Georgian ports, converting it to LNG in liquefaction terminal and transferring it to Romania's Constanta port in the Black Sea. The Memorandum of Understanding was signed back in September 14, 2010 between the presidents of Azerbaijan, Georgia and Romania in order to create a Joint Company to study the export possibilities from Azerbaijan and Georgia via Black Sea to Romania. The Azerbaijani gas will be delivered from Azerbaijan via pipeline to the Georgian port of Kulevi, where it will be liquefied and delivered to Romania and re-gasified.³

1 Suleymanov, E. (2004) "Emergence of New Political Identity in The South Caucasus", Master thesis, *The Fletcher School*, 2004, Available at: http://wh.agh.edu.pl/other/materialy/678_2015_03_17_22_03_33_Emergence%20of%20New%20Political%20Identity%20in%20South%20Caucasus.pdf (Accessed: 15 August 2015).

2 Petersen, A. (2007) "Integrating Azerbaijan, Georgia, and Turkey with the West: The Case of the East-West Transport Corridor", CSIS Commentary, *Centre for Strategic and International Studies*, Available at: http://csis.org/files/media/isis/pubs/070910_petersen_commentary.pdf (Accessed: 15 September 2015).

3 Ibrahimov, R. (2010) "Azerbaijan Energy Strategy and the Importance of the Diversification of Exported Transport Routes", *Journal of Qafqaz University*, Number 29, Available at: <http://journal>.

The nationalist vision and territorial irredentism of Armenia means that Yerevan has been excluded from regional integration while Georgia and Azerbaijan have been developing their relations in many areas, especially in the energy sector. This pragmatic approach has deepened Georgian-Azerbaijani relations, while Armenia remains isolated due to its bellicose policy toward Azerbaijan and occupation of Nagorno-Karabakh region (including seven adjacent districts) of the latter. Thus far, Azerbaijan and Georgia have consolidated their bilateral energy relations through projects and investment initiatives by Azerbaijan's State Oil Company (SOCAR) in Georgia. Georgia annually receives millions of dollars from the tariff payments for the BTC and BTE pipelines. SOCAR Georgia Petroleum, a subsidiary of SOCAR, is one of the largest taxpayers in Georgia and a major investor in Georgia's oil/gas terminals and warehouses, as well as the retail and wholesale of oil/gas and their products.⁴ SOCAR owns hundreds of gas stations, operates the natural gas distribution network, and owns and operates the Black Sea port of Kulevi. It is currently Georgia's main supplier of crude oil, oil products and natural gas. SOCAR has invested billions of USD in the Georgian economy, including the development of the Kulevi terminal and port.⁵

Moreover, Azerbaijan, Georgia and Turkey are in the process of realizing the Baku-Tbilisi-Kars (BTK) railway project. The BTK will effectively open a new railway corridor from the Caspian Sea through the territories of Azerbaijan, Georgia and Turkey to Europe, eventually precluding the need for sea transportation, once the planned railway tunnel under the Bosphorus Strait in Istanbul is complete.⁶ Following the BTC and BTE pipelines, the BTK project will be third trilateral project between Azerbaijan, Georgia and Turkey that isolates Armenia in terms of transport routes.

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qu.edu.az/article_pdf/1039_452.pdf (Accessed: 15 August 2015).

4 Soltanov, E. (2012) "The Emerging Patterns of Azerbaijan's International Energy Policy: Continuities and Changes", *Caucasus International Journal*, 2(2).

5 Tsereteli, M. (2013) "Azerbaijan and Georgia: Strategic Partnership for Stability in a Volatile Region", *Central Asia-Caucasus Institute and the Silk Road Studies Program*, Silk Road Paper, Available at: <http://www.isn.ethz.ch/Digital-Library/Publications/Detail/?lang=en&id=173440> (Accessed: 15 August 2015).

6 Georgian Railway (2015) 'Baku-Tbilisi-Kars Railway', Available at: http://www.railway.ge/?web=0&action=pageandp_id=290&lang=eng (Accessed: 15 August 2015).

It will also form part of the network of routes that connect Asia and Europe, known as the Iron Silk Road.⁷

However, political transitions in Georgia in 2003 and 2012 have tested bilateral relations between Azerbaijan and Georgia. Both of the previous governments of Georgia had very close relations with Azerbaijan. The power transition from the United National Movement to Georgian Dream coalition in 2012 led by billionaire Bidzina Ivanishvili created an uneasy political environment in Georgia. Ivanishvili's political inclinations and decisions, including request for a price discount on Azerbaijani gas imports, a statement on the alleged inefficiency of Baku-Tbilisi-Kars railway, comments on the restoration of the transit railway system through Abkhazia to Armenia,⁸ plus former Economy Minister George Kvirikashvili's statement on the revision of oil and gas contracts with SOCAR, could harm Georgia's national interests and bilateral relations with Azerbaijan. The possible opening of railway system through Abkhazia would only serve Armenian interests, and is not compatible with Azerbaijan's 'isolation policy' towards Armenia, due to the latter's occupation of Azerbaijan's territories. Meanwhile, it would endanger Georgia's preferred partner status in the region for Azerbaijan. In 2013, Ivanishvili visited Baku to repair the situation, and Baku was able to demonstrate a stronger position on the impossibility of opening Abkhaz railway, and did not make any compromise regarding the price of gas.⁹

Importance of the South Caucasus Region for Russia

In the early 2000s, after inheriting the Russian presidency from Boris Yeltsin, Vladimir Putin prioritized the post-Soviet space as a key region in Russian foreign policy doctrines which remained so during his two presidential terms. During Putin's third presidency, Russian foreign policy has been primarily focused on the promotion of the Eurasian Economic Union, which is intended to encompass the former Soviet republics. During the Cold War

7 Jarosiewicz, A. and Matusiak, M. (2013) "Ivanishvili goes to Azerbaijan – a visit overshadowed by misunderstandings", *The Centre for Eastern Studies*, Available at: <http://www.osw.waw.pl/en/publikacje/analyses/2013-01-09/ivanishvili-goes-to-azerbaijan-a-visit-overshadowed-misunderstandings> (Accessed: 15 September 2015).

8 Rferl.org, (2013) *Ivanishvili And The Russians*, Available at: <http://www.rferl.org/content/analysis-georgia-ivanishvili-and-the-russians/24733895.html> (Accessed: 1 August 2015).

9 Jarosiewicz and Matusiak, *Ivanishvili goes to Azerbaijan*.

and after the post-Soviet era, Russia's concerns mainly stemmed from NATO's presence in its neighborhood, which Russia considered its historical area of influence. Notably, Georgia's Euro-Atlantic aspirations, its strong ties with the US and the EU, and the recent opening of NATO's training centre in Georgia have displeased Russia. Similar factors led to the Russia-Georgia war in 2008, which was followed by Moscow's recognition of the 'independence' of the Abkhazia and South Ossetia regions of Georgia. However, rather than diminish Georgia's pro-Western aspirations, this military conflict consolidated this strategy.

The Russia-Georgia August War in 2008 and subsequent Russian policy aimed at pressuring Tbilisi had negative implications for Georgia's energy security and Azerbaijan-Georgia energy transportation partnership as well. During the war Russian military jets dropped several bombs in the proximity of BTC and Baku-Supsa oil pipelines. Although the bombing did not damage the pipelines,¹⁰ Azerbaijan halted oil delivery for several days in order to avoid the risk of economic losses. Another blow to the Georgian energy security was the loss of the Enguri Hydro Power Plant. After the war, the main grid and switchyard of Georgia's major electricity provider, Enguri Hydro Power Plant, remained in Abkhazia, while the dam and reservoir remained on Georgian-controlled territory.¹¹ Russia has been continuing threatening the vulnerable energy infrastructure of Georgia ever since. In early July of 2015, the de-facto 'borders of South Ossetia' were moved few kilometers inside Georgian-controlled areas and this 're-borderization' left a small section of Baku-Supsa oil pipeline inside of South Ossetia's newly enlarged 'borders'.¹² The Georgian government stated that in case there are problems with the breakaway territory, and if the de-facto 'South Ossetia leadership' wants to obstruct the flow of oil through Georgian territories, a new section of Baku-Supsa pipeline might be built.

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10 Dailymail (2008), *The Pipeline War: Russian bear goes for West's jugular*, Available at: <http://www.dailymail.co.uk/news/article-1043185/The-Pipeline-War-Russian-bear-goes-Wests-jugular.html> (Accessed: 1 August 2015).

11 Margvelashvili, M. and Mukhigulishvili, G. (2012) "Energy Security Georgian Perspective", Available at: http://weg.ge/wp-content/uploads/2012/12/energy_security_georgia_perspective.pdf

12 BBC.com (2015) *EU warning over Russia 'land grab' in South Ossetia border row*, Available at: <http://www.bbc.com/news/world-europe-33549462> (Accessed: 1 August 2015).

Challenges of Restoring Russian Gas Exports to Georgia

On September 25, 2015, the Energy Minister of Georgia, Kakha Kaladze met the Chief of Gazprom Alexei Miller in Brussels. After a private meeting, Kaladze announced that Georgia may buy additional volume of Russian gas through Georgia's commercial enterprises, if the price of Russian gas is sufficiently attractive.¹³ Currently Georgia receives Russian gas as a transit fee (10% of the entire volume, which is 300 million cubic meters) for transporting Russian gas to Armenia through Georgian territories via the North Caucasus-Transcaucasia pipeline.¹⁴ If Russia exports more along this route, Georgia can receive more gas in the form of a transit fee. However, the price is not clear yet, as current prices of Russian gas exports fluctuates between \$190 and \$315 mostly depending on the nature of political relationship between Moscow and the customer countries.¹⁵

It should be mentioned that the subsidized gas prices by Russia (e.g. the discount prices for the Moscow's allies Armenia and Belorussia) is unlikely to be extended to Georgia, therefore Tbilisi will likely get the one of the highest prices from this range. Given

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In fact Russia was Georgia's main gas supplier until 2007, but after the Russia-Georgia August war in 2008, Georgia suspended Russia's gas imports, and Azerbaijan became its main gas supplier. This enabled Georgia to move away from gas dependence on Russia, and to increase the sustainability of its domestic gas consumption.

Georgia's diversification of its gas import, and Azerbaijan's role therein, has helped both countries to strengthen their geopolitical independence as a transit and a supplier state respectively. By diversifying its gas supply away from Russia to Azerbaijan, Geor-

13 Civil.ge (2015) *Georgian Energy Minister Meets Gazprom CEO in Brussels*, Available at: <http://www.civil.ge/eng/article.php?id=28599> (Accessed: 28 September 2015).

14 Kommersant.ru (2015) «Газпром» возвращается в Грузию, Available at: <http://www.kommersant.ru/doc/2827592> (Accessed: 15 October 2015).

15 Gruzia Online (2015) Азербайджан наш стратегический партнер – Каладзе, Available at: <http://www.apsny.ge/2015/eco/1444705001.php> (Accessed: 15 October 2015).

gia limited Gazprom's monopoly over its domestic gas market.

Kaladze's talks with Gazprom and the implications for Georgia-Azerbaijan relations received widespread media coverage in both the Georgian and Azerbaijani media. Georgian Prime Minister Irakli Garibashvili visited Azerbaijan on October 10, 2015 and met with President of Azerbaijan Ilham Aliyev. Prime Minister Garibashvili's visit was followed by the visit of Georgia's Minister of Foreign Affairs Giorgi Kvirikashvili, although Kaladze himself did not pay a visit to Baku yet. Kaladze's arguments for restoring the gas supply from Russia are based on the insufficiency of volume of gas received from Azerbaijan's SOCAR. However, the General Director of SOCAR-Georgia Mahir Mammadov has stated that, "Azerbaijan can completely satisfy Georgia's gas needs"¹⁶.

The Kaladze-Miller gas talks were also criticized by Georgia's opposition parties. The Georgian opposition is resistant to the idea of damaging relations with Georgia's strategic ally – Azerbaijan – as well as to importing Russian gas, while Russian armed forces are still stationed in Georgia's breakaway territories. The United National Movement, an opposition party, has demanded that the government convene the National Security Council of Georgia in order to discuss the security dimension of restarting Russian gas imports.¹⁷ The restoration of Russian gas imports to Georgia will undoubtedly have repercussions for Georgia's foreign policy. After seven years of the August 2008 war, Russia wants to restore its tarnished position by re-entering into the Georgian energy sector.

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Moreover, Russia's penetration into the Georgian energy market has become more evident following the purchase by Russian oil company Rosneft of a 49% stake of the Petrocas International Energy Ltd in December 2014.¹⁸ The company deals with oil transportation and owns the biggest oil storages in Georgia, as

16 Ru.Sputnik.az (2015) *SOCAR Georgia: AP обеспечивает почти все потребности Грузии в газе* Available at: <http://ru.sputnik.az/economy/20151022/402452835.html> (Accessed: 22 October 2015).

17 Gruzija Online (2015) ЕНД требует созыва заседания Совбеза в связи с переговорами властей с «Газпромом», Available at: <http://www.apsny.ge/2015/pol/1444517877.php> (Accessed: 12 October 2015).

18 Rosneft.com (2014) *Rosneft and Petrocas Create a Logistics and Retail Joint Venture*, Available at: <http://www.rosneft.com/news/pressrelease/29122014.html> (Accessed: 12 July 2015).

well as Georgia's Poti port. Furthermore, Russia's presence in the Georgia's electricity market via Inter RAO, through its 75% ownership of the "Telasi" electricity network company, is another concern for Georgia.

Iranian Gas to Georgia: Perspectives and Challenges

Meanwhile, Energy Minister Kakha Kaladze has also declared that Georgia is considering the possibilities of importing Iranian gas. After the withdrawal of the international energy sanctions, Iran will be able to re-start its previous gas and oil exports to the world market. Therefore, in addition to Russian gas, Georgia also seeks to import Iranian gas, apparently with the aim of diversifying country's gas imports.

However, the lack of a common border with Iran means that Georgia must rely on either Armenia or Azerbaijan for transit. Although there are existing pipelines from both Iran and Russia to Armenia, technical problems, such as insufficient pipeline capacity, the lack of an interconnection between both pipelines, and the lack of clarity around the reverse flow capability of the 'Russia-Armenia Pipeline', makes the Armenian option less likely.

Given Gazprom's ownership of gas transportation infrastructure of Armenia and Moscow's overwhelming influence over Yerevan, Russia would easily undermine any project of bringing Iranian gas to the South Caucasus market via Armenia.

Moreover, reverse flow exports of Iranian gas through Armenia via the Russia-Armenia pipeline would not be welcomed by Russia, since Gazprom owns this pipeline through its subsidiary Gazprom-Armenia, and the delivery of Russian gas to Armenia is the priority for that route. Such a project would also threaten to challenge Russian gas monopoly in Armenia, the development that Russia would hardly tolerate in its 'outpost' state. Given Gazprom's ownership of gas transportation infrastructure of Armenia and Moscow's overwhelming influence over Yerevan, Russia would easily undermine any project of bringing Iranian gas to the South Caucasus market via Armenia.

Thus, as Armenia has been isolated by both Turkey and Azerbaijan for more than twenty years due to the conflict with Azerbaijan over Nagorno-Karabakh, for Yerevan it is crucial to improve the sustainability of its economy and avoid the risk of economic collapse. Therefore, Armenia could seek to become a transit country amidst the withdrawal of sanctions against Iran. However, Ar-

menia's weak economic capacity, its dependence on Russia, and internal political restraints makes the "Armenian" transit option unlikely.

In fact, the total volume of gas that Georgia consumes annually is not especially high. Therefore, investing in infrastructure to deliver a small amount of gas to Georgia would not be cost effective for Iran either. If Iran decides to export its gas to Europe, the Turkish route is the best option. Moreover, Iran's geographical location means that it can develop its LNG sector and implement LNG shipments toward Asian markets, where LNG prices are higher than in Europe.

Additionally, despite formal relations between Georgia and Iran, like Russia, Iran is not pleased with the pro-American stance of Georgia. Tehran is deeply opposed to Tbilisi's efforts to bring NATO to the South Caucasus, closer to Iranian borders which can be considered a strategic challenge for Tehran.

Conclusion

The frozen conflict in Georgia's Abkhazia and South Ossetia regions is the main reason why Georgia should refrain from re-opening the path to import dependence on Russian gas. The restoration of Russian gas supplies will have political implications for official Tbilisi, making it easier for Russia to impose its political agenda and put pressure on Tbilisi. This could also threaten Georgia's national security. Expectations of cheaper gas from Russia, i.e. at the price of Azerbaijani gas, would be naïve given that Russia has found itself in a deep economic crisis due to sanctions. Meanwhile, transit of Iranian gas through Armenia to Georgia seems unlikely for the time being because of technical and financial reasons. Moreover, entrance of Iranian gas to Armenia, even for the transit purposes in the initial stage, would be unacceptable for Russia due to challenging sole supplier status of Russia. From Tehran's perspective, LNG transportation of Iranian gas through ports or gas exports to Europe via Turkey is more secure and beneficial for Iran.

Georgia benefits more from SOCAR's presence in its energy sector than it would gain from Russian Gazprom. Azerbaijan provides 90% of Georgia's gas demand, and at cheap prices, the cheapest among SOCAR's clients. Nor does Azerbaijan impose

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any political agenda or threaten Georgia's territorial integrity and sovereignty. Tbilisi's desire to diversify its energy supply is understandable in terms of reducing the country's dependence upon a single supplier. But given the cheap prices of Azerbaijani gas for Georgia without any political cost, importing Russian gas is a fundamentally flawed strategy. Along with being strategically costly and economically unfeasible, ill-considered political decisions and maneuvers by certain political figures in Georgia like welcoming Russian or Iranian presence would also risk triggering a domestic crisis and alienating Georgia from both NATO and the EU.

Azerbaijan could deliver its gas and oil to European markets through both Russia and Iran. However, the Azerbaijani leadership took a risky step in early 1990s to bypass Russia, making Georgia an important part of the East-West energy bridge. Today, ostensibly pro-Western inclination of current government of Georgia, however, with latent favorable gestures to Russia deserves an attention in terms of national security and sovereignty of Georgia. Thus, official Tbilisi should maintain friendly and strategic relations with Azerbaijan. Given the geopolitical situation in the South Caucasus, it is unlikely that Georgia can find an alternative strategic partner in the region. Maintaining this partnership requires Georgia to embark on a more rational policy with official Baku. The majority of Azerbaijan's strategic projects, including oil and gas pipelines and railways systems pass through Georgian territory. This enhances the strategic significance of Georgia, as well as strengthens trilateral relations between Azerbaijan, Georgia and Turkey.