THE GEOECONOMICS OF THE SOUTH STREAM PIPELINE PROJECT

By Antto Vihma and Umut Turksen

Energy trade has developed into one of the most contentious and divisive issues between Russia and the EU in the post-Cold War era. It reflects a broader geoeconomic struggle in which economic means are used to advocate geopolitical goals. This article argues that the case of the South Stream Pipeline Project (SSPP)—a grand project abruptly cancelled by Russian President Vladimir Putin in December 2014—epitomizes these power politics. In 2014, Russian leadership advanced both geopolitical and geoeconomic strategies towards the EU: pursuing the former by conducting a military campaign in Crimea and Eastern Ukraine; and pursuing the latter by pushing the construction of SSPP in spite of the EU's legal and political objections. Due to Russian military aggression in Ukraine, however, the EU was able to harden its line on SSPP. Russian geoeconomic activity has long been successful as a centrifugal, dividing power within the EU. The geopolitical campaign in Ukraine, in stark contrast, has been a centripetal force, resulting in increased EU unity that contributed to the SSPP's demise. This is evidence that claims of geoeconomics as a continuation of war by other means are potentially misleading. The means of geopolitical power projection and geoeconomic power projection thus have notably different effects in today's contemporary, interconnected world.

In the post-Cold War era, energy security and trade between the European Union and Russia was projected to be the glue that bound the two powers together in peaceful and prosperous trade relations based on mutual benefit and interdependence.[1] This partnership was projected even despite the growing asymmetry between liberal approaches to energy sector development in the EU and the illiberal, state-centric Russian approach.[2] Today, however, energy trade between these powers reflects a broader geoeconomic struggle in which economic means are used to advocate geopolitical goals. The concept of geoeconomics rivals both economic liberalism and traditional geopolitics as a paradigm of foreign and economic policy and national interests.[3] Geoeconomics challenges the liberal interdependency paradigm by under-

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Journal of International Affairs, Fall/Winter 2015 Vol. 69, No. 1.

scoring the strategic interests—zero-sum power political interests that do not function in the logic of commerce—in economic relations between states.[4] Further, in a departure from traditional geopolitics, which connotes conventional military projections of power, geoeconomics highlights softer, economic versions of balancing behavior, something which traditional geopolitical perspectives often overlook.[5]

This paper argues that the case of the South Stream Pipeline Project (SSPP) epitomizes the geoeconomics power politics involved in the energy relations between the EU and Russia. The SSPP was designed to bring large amounts of Gazprom's gas across the Black Sea to the Balkans and onward to Hungary, Slovakia, Austria and Italy. The project was launched by Russia in 2006 after intense dispute with key transit state Ukraine.[6] After years of political turmoil between Russia, the European Commission, and member states, President Putin abruptly cancelled the SSPP in December 2014.

For Russia, the SSPP has been an instrument of a geoeconomic strategy to advance specific goals: to secure Russian influence in Ukraine; to maintain Gazprom's dominant market share in the EU; to maintain Russian influence on the EU member states which rely on Russian energy; and to undermine European unity in energy and foreign policy. For the EU, the opposition towards the SSPP stems from the long-term policy goal of limiting the Russian geoeconomic influence within the EU, framed as concerns over energy security.

The process tracing presented in this article examines the demise of the SSPP against the hypothesis that the EU-level opposition to the project and member state adherence was strengthened as a result of Russian military aggression in Ukraine. The process tracing draws on public sources and establishes the key trajectories of change and causal sequence both on the EU and the Russian sides. Careful description is the foundation of process tracing, and a crucial building block for analysis.[7] First, the article discusses geoeconomics as a framework for foreign policy analysis, outlining the main drivers of current scholarly interest in geoeconomics. It then turns to the geoeconomic divide et impera, or "divide and rule," strategy of Russia toward the EU, principles behind EU-level gas policy, and the conflicting interests of member states.[8] Subsequently, the paper presents a detailed case study of the SSPP, seen by analysts as epitomizing geoeconomic conflicts in the energy sector, focusing on the political struggle of 2014.[9] Lastly, some conclusions are drawn.

The Rise of Geoeconomics

In post-Cold War Europe, growing economic integration and interdependence, together with advances in multilateralism and rule of law, were seen as creating the foundation for a new, peaceful security environment.[10] The expectation was that such trends would drive closer political cohesion, both within the EU and in its neighborhood.[11] The deepening of interdependency and solidarity was also seen as promoting a "European model," relegating political authority to the supranational sphere and redefining power as surveillance in different networks. As policy analyst Mark Leonard writes in his 2005 book *Why Europe Will Run the 21st Century*, "Europe will not run the world as an empire, but the European way of doing things will have become the world's way."[12] Simultaneously, in Russia, its integration in international trade increased export revenues, and Russia became a major host for foreign direct investment.[13]

While Gazprom benefits from its privileged position, it is also restricted by politically-driven gas pricing.

However, after the U.S.-centric "unipolar moment" of the 1990s, there has been an increasing tendency for regional powers to consider issues of trade and commerce through the prisms of national security and foreign policy.[14] As such, an emerging body of literature examines geoeconomics as a rising framework of foreign policy analysis.[15] Scholars seem to concur, even if they do not use the term "geoeconomics," and analyze world politics under the general banners of "zero-sum world," "multipolarity," or "multipolar order."[16] The rise of geoeconomics by no means suggests that economic liberalism, rules-based multilateralism with legal treaties, or the geopolitics of conventional military power are concepts of the past. Nor does it claim that geoeconomic conduct is a new phenomenon, as there has always been a significant degree of overlap between policy areas of international economics, foreign relations, and security. The argument simply suggests that geoeconomic conduct is gaining in relative importance, and as a result, scholars and analysts are beginning to pay more attention to it.[17]

The current importance of geoeconomics highlights its differences from and similarities to the traditional geopolitical perspective. Some linkages are clear: For example, geopolitics based on traditional "hard power" elements like military power and spending depends to a great extent on economic strength. At the same time, countries are increasingly reluctant to utilize military force and instead rely on economic influence to drive foreign policies and strategies. This may be achieved through leveraging trade in valuable commodities or resources (i.e., oil and gas), or through direct participation in the state's financial system by trade in services.

The scholar Edward Luttwak has aptly noted that the propensity of states to act geoeconomically will vary greatly, even more than their propensity to act geopolitically.[18] Geoeconomic activity is contextual, and limited and enabled by two broad factors: political ideology and state–private sector interactions.[19] In the field of political ideology, some states resist acting geoeconomically for institutional, doctrinal, and political reasons, especially if they are deeply committed to moral politics or a *laissez-faire* attitude.[20] A political struggle takes place in the domestic sphere of different countries in varied political contexts, in which some constituencies demand geoeconomic activism from the state, and some are against it. On the other hand, traditional geopolitical conduct such as a conventional military power projection will also limit the possibilities of geoeconomic strategies.

Another equally important variable is the nature of the coexistence of state and private economic operators. Their coexistence can be passive—for example, in the case of a large group of small, localized service businesses; or active, as in economies dominated by state-owned firms. The latter is the case in Russia, where the state's energy strategy has been analyzed in terms of a "symbiotic relationship" between the state and leading companies.[21] Gazprom, Russia's largely state-owned gas company, holds a legal monopoly in natural gas exports and is directly under the control of the Kremlin. In the geoeconomic game, Luttwak points out that "the state can be both user and used, and companies both instruments and instrumentalizers."[22]

While Gazprom benefits from its privileged position, it is also restricted by politically-driven gas pricing both domestically and internationally, as well as geoeconomically-motivated hardline policies, as became evident in the Ukrainian gas crisis of 2009.[23] According to analysts, the critical—and for Gazprom, extremely costly—decision to turn off the gas was likely made by then-Prime Minister Vladimir Putin.[24] In February 2010, as Russia was again able to count on a sympathetic government in Kiev, the price of gas was cut by almost 30 percent, and Russia gained a new 30-year contract for Sevastopol.[25] The price cut was so great that the Russian government financed Gazprom directly.[26] These events indicate that Gazprom's commercial interest is overrun by Kremlin power politics.

Geoeconomics in the EU-Russian Gas Trade

Under President Putin's reign, Russia's economic ideology is based largely on national security interests.[27] Accordingly, liberal ideologies are seen as enemies of Russia's nationally minded economy.[28] For Russia, a country with an extensive natural resource base, this geoeconomic *modus operandi* invariably involves natural gas trade.[29] Russia is among world's biggest energy exporters, but without its energy products, the value of Russian exports is smaller than that of Poland.[30]

It is well known that in the 1990s, the EU and Russia were relatively closely in agreement concerning the main features of the European energy order. The early years after the Cold War saw the birth of the European Energy Community in 1990, the European Energy Charter in 1991, the Energy Charter Treaty in 1994, and the Partnership and Cooperation Agreement in 1994.[31] The agenda was to achieve a system functioning under European energy market rules, "encompassing production countries from the Atlantic to Vladivostok."[32] The non-energy-related function of these arrangements was to ensure stability and integration.[33] Against this legalistic and multilateral stance, the emerging Russian position was a profoundly geoeconomic one, based on bilateral, state-centric and sovereignity-bound practices. Many scholars have analyzed Russia's policies, in which it uses the control over energy streams to Europe to enhance its foreign policy, influence, and regional power status.[34]

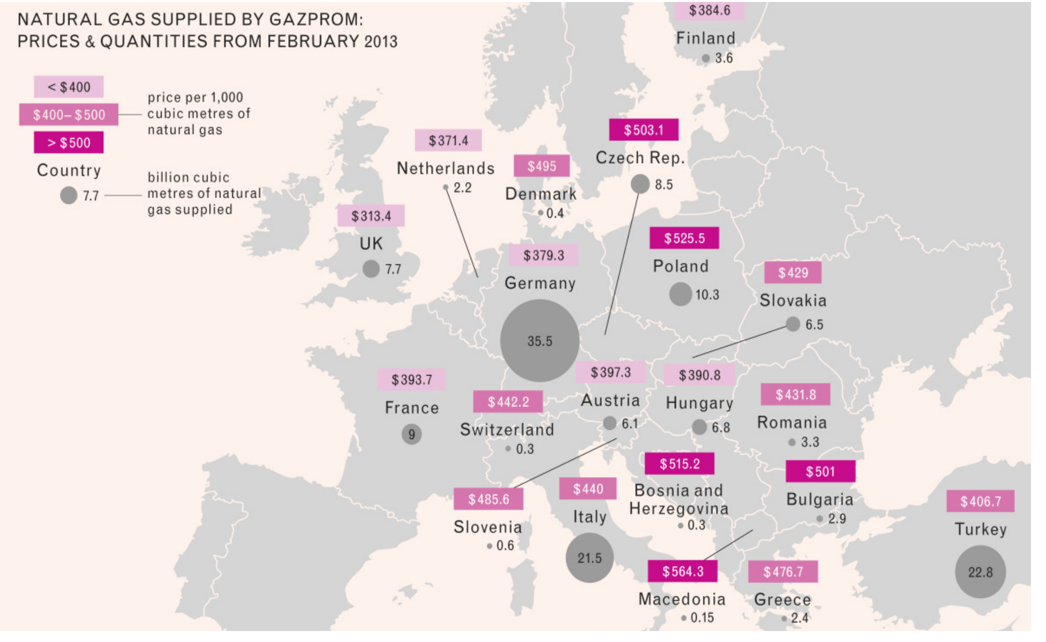
Legal requirement of transparency of prices and quantities in the European gas trade has been a key strategic priority of the EU for years.

European customers negotiate gas prices with Gazprom on a country-by-country basis, and the prices fluctuate with world oil prices according to a formula. Export prices and quantities were made public for the first time in 2013 pursuant to a new EU regulation, one of the legal instruments contributing to establishment of a new, single EU energy market.[35]

Legal requirement of transparency of prices and quantities in the European gas trade has been a key strategic priority of the EU for years.[36] Transparency of pricing is believed to be essential to balance asymmetrical economic relationships between EU member states and Russia, thus improving energy security and predictability. The transparency regulation is also considered a prerequisite for the establishment of a single energy market designed to promote competitiveness and protect consumer interests.[37] In response to increased regulation, Russia has tried both directly and indirectly to curtail EU efforts. In 2011, for example, Putin issued a decree prohibiting "strategically important companies" from providing information to foreign regulators without approval from the Kremlin.[3]

Figure 1 provides a snapshot of Gazprom's natural gas pricing as a divisive, centrifugal force within the EU.[39] Comparing the price paid for 1,000 cubic meters of gas by Hungary ($391) and Poland ($526), or Romania ($431) and Bulgaria ($501), it is clear that the differences cannot be explained by transportation distance or gas quantity.

Figure 1: European natural gas prices and Russian and quantities

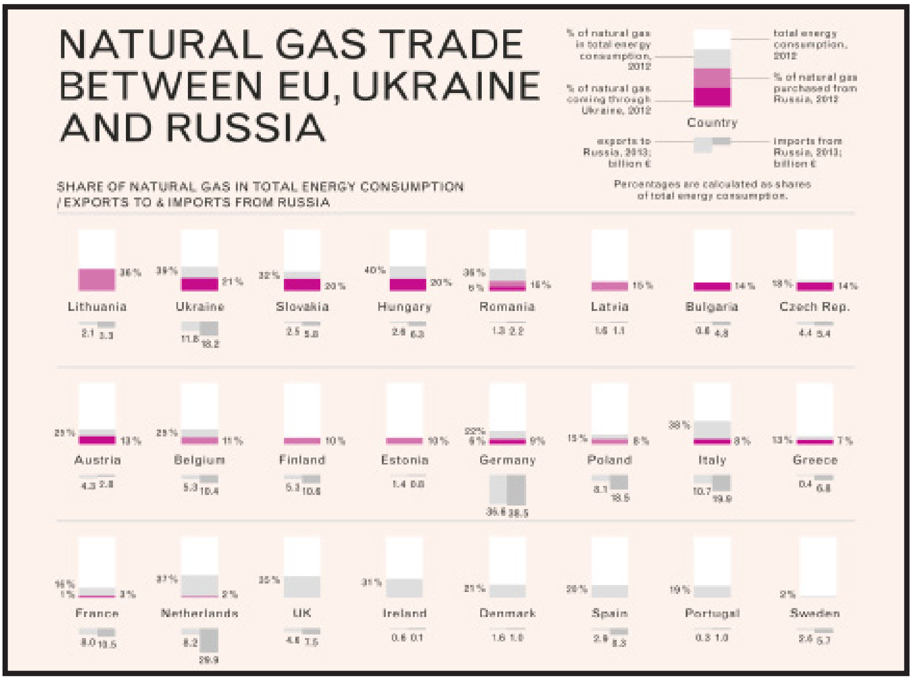


In examining geopolitical and geoeconomic interests, it becomes apparent that prices are formed by an assessment of competition versus degree of dependency, as well as political discounts and status of bilateral negotiations.[40]

Russia has used gas exports as a foreign policy tool, serving both as a "carrot," giving discounts to sympathetic governments in the former Soviet countries and strategic partners in Western Europe; and as a "stick," maintaining hardline contract terms with the most dependent states with unsympathetic governments. Here, the gas trade emerges as a "wedge strategy" in which gas discounts and renegotiated agreements act as an incentive against the EU's unity and solidarity. For instance, Gazprom has given favorable and flexible contracts to its German partners ($379.3 per 1,000 cubic meters, see *Figure 1*), such as E.ON and chemical giant BASF, companies that also hold sizeable shares in Yuzhno-Russkoye gas fields.[42]

Russia's incentive-oriented gas policies have encouraged German politicians not to pursue EU unity and collective action on the energy front.[43] While ex-chancellor Gerhard Schröder joined the board of Gazprom and backed the Russian action in Ukraine, current chancellor Angela Merkel led the effort to block proposed EU regulations to limit the ability of foreign companies to buy

Figure 2: The share of natural gas, natural gas from Gazprom, and natural gas from Gazprom via Ukraine for EU member states.



European energy utilities—a measure aimed at addressing Gazprom's monopolistic position in the EU gas markets.[44] In many other EU states, important national energy champions continue to maintain close ties with the Russian energy sector.

EU political institutions, including the European Council, the European Parliament, and the Commission, have repeatedly taken stands in favor of a common foreign energy policy strategy that looks beyond the single market, underscoring the need for a strategic foreign policy approach in energy relations.[45] Several member states have joined the position. Poland, for example, with an unfavorable gas contract ($525.5 per 1,000 cubic meters, see *Figure 1*) and several other disputes with Russia, has lobbied for "energy solidarity" and the Europeanization of energy security since the 2006 Russia-Ukraine gas crisis.[46] However, while EU institutions have been keen to underscore a more unified policy in external energy relations, this stance has long been countered by Russian energy geoeconomics and bilateral energy agreements with EU members.[47] Even the simplest transparency and coordination measures have been challenging for the EU's external energy policy. For example, the first time Gazprom's gas prices were available publicly was in 2013, as Gazprom had long insisted that gas pricing agreements should be kept confidential.[48]

As Russia began to increase its assertiveness and turn to geoeconomic means in its natural gas policy, the EU focused on developing a competitive single market for gas. This strategy is partly to control Russian geoeconomic influence, expressed in terms of concern over energy security (see *Figure 2*). The EU approach to energy law has been informed by its competition law principles and based on non-discriminative third-party access, the unbundling of production and transport of energy, and regulatory oversight by a public authority.[49]

On-the-ground progress toward EU goals has been slow due to, among other things, reluctant member states, the political clout of the national champions, the market structure, long distances, and failures in regulation.[50] However, EU efforts to limit the role of take-or-pay contracts and liberation of parts of the network capacity paved the way for the events of 2010, when competition in the EU natural gas market was realized. This development took shape as high oil prices coincided with the shale gas boom in North America, with the former pushing long-term gas prices up, and the latter leaving a liquified natural gas (LNG) surplus on the world market and bringing relatively cheap LNG to European ports.[51] Since then, spot-priced gas—gas sold at current market prices, rather than at a pre-set, contracted price—has increased its share in Western Europe, but crucially, eastern parts of the EU are lagging behind (see *Figure 2*).[52]

For several member states the ideological shift has been slow; the geoeconomic motivation of national energy champions and governments to "defend turf" against competition from other member states has been at play. Only in July 2015, 15 EU and Energy Community countries in Central Eastern and Southeastern Europe reached a general agreement to accelerate building missing gas infrastructure links and to tackle the remaining technical and regulatory issues preventing full implementation of the EU vision.[53]

Geoeconomics of the South Stream Pipeline Project

The South Stream Pipeline Project was designed to supply 63 billion cubic meters of gas annually across the Black Sea to the Balkans and onward to Austria and Italy. The project was announced in June 2007, and in September 2012, a consortium was formed in which Gazprom was to own 50 percent of the project, ENI 20 percent, and the French firm EDF and German firm Wintershall each 15 percent.[54] According to the project finance plan, 30 percent of financing would be paid by shareholders, with the rest largely funded through credit financing.[55]

Many analysts opined that the SSPP was initiated not for profit but for a strategic (geoeconomic) advantage. With no growth expected in the EU gas market, and huge infrastructure costs, the business case for the SSPP was weak.[57] It was no secret that Russia sought to increase its leverage over Ukraine; through Gazprom, the SSPP project offered an opportunity for Russia to divert gas transit away from Ukraine's borders, depriving the country of gas transit revenue and of its key lever in Moscow as a transit state between Russia and the EU markets.[58] With the SSPP's alternative route to consumers in Europe, Ukraine would be exposed to unpredictable price increases and gas cutoffs, as Gazprom would be able to switch off supplies without inconveniencing other European markets.[59] Russia has strongly championed the SSPP since the Ukraine-Russia gas crises in 2006 and 2009, and denied Ukraine the possibility of part or full ownership by fully circumventing the country.

In addition, Russia viewed the SSPP as an opportunity to weaken the alliance between Southeastern Europe and the EU by increasing the market share of and dependency on Gazprom pipeline gas. With the SSPP, Russia could solidify its political influence within the countries on the projected route, especially smaller economies like Hungary and Greece with uneasy relationships with the EU.[60] To a lesser extent, further influence could be exerted on bigger, friendlier markets like Italy and Austria. Furthermore, the project contributed to Russia's geoeconomic goals by preventing competing plans to transport gas from Azerbaijan through Turkey into the EU.[61]

A particular political and legal struggle in geoeconomic relations between the EU and Russia was not only the question of whether to build the SSPP, but on whose terms the pipeline would function. This question became politicized in bilateral agreements between Russia and EU member states. These intergovernmental agreements were made with Austria, Bulgaria, Croatia, Greece, Hungary, and Slovenia, as well as Serbia, a candidate country for EU membership.

Similarly, Gazprom signed bilateral agreements on cooperation with the authorized national partners and set up joint project companies in each transit country, usually owned 50 percent by both parties.[62] Signing of the agreements was typically complemented by establishment of a new gas contract, such as the one Bulgarian prime minister Boyko Borisov and Gazprom CEO Alexei Miller announced simultaneously with their South Stream bilateral agreement in 2012, giving Bulgaria a 20 percent price cut for the next 10 years.[63] In 2013, Gazprom hosted official welding ceremonies in Bulgaria and Serbia, as well as a signing ceremony in Hungary.[64] These events have been interpreted by scholars as geoeconomic showcases for Russia's seriousness toward the SSPP, and as geo-economic motivation to impress Ukraine to join the Russian-led Eurasian Economic Union.[65]

In short, the content and diplomatic structure of the SSPP agreements represent the traditional energy order. To move forward, the agreements would require notable exemptions to avoid breaching EU competition rules.[66] According to EU legislation, for example, gas transport system operators must build gas interconnectors in accordance with the regulated third-party access principle, requiring states to establish systems to ensure third-party access to gas and electricity transmission and distribution networks.[67] National authorities may request exemptions from the third-party access rules. When an operator submits a request for exemption, the state regulatory authority assesses the request and makes a decision, which requires Commission approval.

Officially, such exemptions are granted on the basis of criteria.[68] In practice, however, the decision to grant exemptions is largely political. From the Russian perspective, complying with EU legislation adds costs for the investor—for example, by adding extra capacity to the pipeline.[69] More importantly, in geo-economic terms, the application of relevant EU legislation would have hindered Russia's ability to use the SSPP as a political tool, which was unacceptable for the Kremlin.

Early in 2014, the *Financial Times* reported that Gazprom "was on the brink of winning exemption" to supply extra gas to Germany, which was interpreted as a sign that the Commission could be flexible on regulation affecting the South Stream project.[70] But the Commission hardened its stance in late March, as the Ukraine crisis evolved into warfare with evidence of Russian military involvement, and suspended the negotiations on exemptions.

According to a later *Financial Times* article, the Commission was "in no mood to grant Gazprom further exemptions."[71] The Commission bluntly stated that "decisions on exemptions are on ice for political reasons."[72] However, even in the face of the Ukraine crisis, political and legal compromises were expected to move the SSPP forward. Despite legal and political uncertainty, SSPP's momentum would be hard to reverse, especially according to industry analysts.[73]

After the political setbacks in March 2014, Russia reacted to the EU opposition by redoubling its own geoeconomic efforts. In recognition of the depth of the EU's commercial ties to Russia and the conflicted loyalties of member states, Gazprom signed a preliminary deal with the energy company OMV in May to extend the SSPP into Austria.[74] At the same time, Gazprom announced deals with Switzerland's Allseas Group, and Italy's Saipem, to build SSPP's underwater pipelines in the Black Sea.[75]

In June 2014, the European Commission demanded that pipeline construction in Bulgaria be halted until allegations of corruption linked to the construction firms hired to complete the project were resolved. Also in June, the Commission stated that Serbia's EU accession process would suffer if its SSPP agreement with Russia was not aligned with EU law.[76] In July 2014, Italian and Russian foreign ministers reaffirmed their commitment to the SSPP.[77] Hungary demonstrated its support of the Kremlin in September, when it cut off the reverse gas flows from the EU to Ukraine.[78] The same month, the European Parliament passed a resolution calling on member states to cancel planned energy sector agreements with Russia, including the SSPP.[79] Two months later, Hungary confirmed its unconditional support for SSPP, passing an amendment to the procurement rules for pipelines designed to forestall legal objections from Brussels.[80]

The *raison d'etre* for the SSPP was always power politics, and the reason for abandoning the project was the thickening legal and political resistance from the EU due to Russia's geopolitical campaign in Ukraine.

The state of the project during this time was confusing, not only legally and politically, but also at the ground level of construction work. Here, Bulgaria emerged as the main field on which SSPP geoeconomics would play out. (The other possible transit country, Romania, has its own gas reserves and is considered a lost cause politically by Russia; the next countries on the transit route, Serbia and Hungary, could always be counted on to support the project.[81]) The alleged corruption involved in the SSPP construction in Bulgaria dominated the country's election campaigns and its media, with reports stating that a secret meeting took place between the Bulgarian Prime Minister and the head of Gazprom.[82] According to the European Council on Foreign Relations, the projected price of SSPP in Bulgaria, 7 million euros per kilometer, was more than twice what a similar pipeline construction would cost in Germany.[83] The difference between the prices was interpreted as a "sophisticated type of corruption" that would, through subcontractors, benefit different political actors in Bulgaria—and that "same mechanism would work in Serbia as well."[84]

As late as August 2014, Gazprom shipped pipes to Varna harbor in Bulgaria and continued work on construction, in spite of Bulgarian prime minister Plamen Oresharski denying ongoing construction, and the forthcoming prime minister Boyko Borisov underscoring the need for EU approval before launching any work on the pipeline.[85] In September 2014, Gazprom announced that construction work on the Serbian stretch would start soon.[86] The new coalition government elected in Bulgaria one month later was regarded as leaning more towards Brussels than the preceding Socialist government, and Borisov again officially emphasized that agreement between Brussels and the Kremlin would be needed before construction.[87]

On December 1, 2014, there was an unexpected turn of events. Russia's President Putin, in an about-face from previous actions, announced that Russia would abandon the South Stream Pipeline Project.[88] The announcement was met with confusion; even the closest European partners, such as Saipem, a subsidiary of the Italian energy company ENI, noted that it had not received any formal notification that the project had been scrapped.[89] President Putin framed the demise of SSPP as a loss to Europe and named the European Commission as the main culprit, "depriving Bulgaria of the possibility of behaving like a sovereign state."[90] Gazprom's stocks rose slightly after the news broke, indicating that the profitability concerns were widely shared among investors.[91]

This confirmed the strategic geoeconomic motivations behind the SSPP, now verified by the marketplace. The *raison d'etre* for the SSPP was always power politics, and the reason for abandoning the project was the thickening legal and political resistance from the EU due to Russia's geopolitical campaign in Ukraine. The stocks of European contractors involved in the construction dropped sharply, evidence that the decision to abandon the SSPP came as a surprise to analysts.[92]

In January 2015, Gazprom notified the Commission that within a few years, Gazprom would stop delivering gas to the EU via Ukraine, and would only make some amount of gas available at the Greek-Turkish border. According to Gazprom's CEO, Alexey Miller, it is up to the European partners to "put in place the necessary infrastructure."[93] It is difficult to estimate whether Miller's words were aimed at impressing domestic audiences, or at actually launching new negotiations with foreign partners. In February 2015, the blueprint for a $12 billion "Turkish Stream" pipeline project was announced. Gazprom and Turkey's state-owned BOTAS corporation have signed a memorandum of understanding, and will negotiate prices and quantities in due course.[94] However, the current economic environment in Russia, with its post-1990s downturn, low oil prices, serious weakening of its currency, and problems of access to capital due to sanctions, poses challenges to future large-scale investments.[95]

Conclusions

Was the SSPP merely another EU-Russia trade dispute, comparable to railway tariff disputes with the Baltic States or the timber tax dispute with

Finland? The analysis and process tracing presented in this article disagrees with this notion, emphasizing that the SSPP was a strategic priority for Russia that became a victim of Russian leadership's adventurism in Ukraine, or even, as reporter Guy Chazan wrote in the *Financial Times*, "one of the biggest casualties of the east-west stand-off over Ukraine."[96] Furthermore, the geoeconomic perspective underscores that the SSPP case is more than a trivial tug-of-war over a gas pipeline.

As indicated by the process tracing, Russian leadership estimated in 2014 that it could advance two European strategies simultaneously: a geoeconomic one (constructing the SSPP) and a geopolitical one (the military campaign in Ukraine). Here, Putin, frequently described by political commentators as a master strategist, overplayed his hand.[97] The EU is still searching for a comprehensive common policy to confront Russian aggression in Ukraine, but in the pipeline politics, Putin seems to have inadvertently succeeded in increasing EU solidarity. From March 2014 onwards, the EU hardened its line on SSPP. The global energy context, including cheap coal prices, expansion of renewable energies, more liquefied natural gas, and spot trading, cannot fully account for the assertiveness of the European Commission and the allegiance of member states in the SSPP case.

On a broader level, the SSPP case study highlights the incompatibility of geoeconomic and traditional geopolitical strategies. Europe's dependence on Russian gas has been widely viewed as a hindrance to the scope of the EU's response against Russia's military aggression in Ukraine.[98] Further, the harm to Russian gas exports and geoeconomic power caused by the geopolitics in Ukraine has not yet been adequately addressed or analyzed in policy research. Russian geoeconomic activity has long been successful as a centrifugal force, dividing member states and political visions within the EU. The geopolitical campaign in Ukraine, in stark contrast, has been a centripetal force acting to unite EU members and resulting eventually in decisive EU actions, as seen in the SSPP case.[99]

Similar centripetal tendencies caused by a perceived geopolitical threat can be witnessed in the emerging German leadership in EU foreign policy, the economic sanctions imposed against Russia, and the re-emerging wider discussion on an energy union.[100] Although contemporary analysts are keen to evoke the theorist Carl Von Clausewitz in viewing economic sanctions and countersanctions as a continuation of the traditional geopolitics of the Ukraine crisis, these claims of geoeconomics being continuation of war by other means are potentially misleading.[101] The means of geopolitical power projection and tools of geoeconomic power have different effects in the contemporary world.

As the contemporary scholar Andrey Makarychev asserted in 2014, "Russia and the EU build their policies on drastically dissimilar concepts of power and divergent conceptualizations of the state and its functions."[102] If geopolitics and geoeconomics are competing strategies (for Russia), so too are geoeconomics and economic liberalism (for the EU). The heritage of the 1990s, promoting liberal order and interdependency to enhance regional security, may hinder the EU's ability to play geoeconomic games with strategically-oriented, state-capitalist Russia.

For a considerable time, Brussels, operating through the emulation of *acquis communautaire*, or EU law, has pushed Gazprom and its partners to comply with EU rules on energy markets and competition. Among the EU's main concerns has been third-party access to pipelines, the unbundling of network ownership and gas supply, and the tariff structure for pipeline use. The European Commission's efforts to create a resilient single market—or more realistically, a variant of "regulated competition," the second-best outcome after a liberal market-based order—indicates the extent to which it will go to limit Russian geoeconomic power.[103] Russia, on the other hand, has launched a dispute over the latest round of EU energy legislation, known as the "third energy package," at the World Trade Organization (WTO).[104] This is an unusual but positive move for Russia, as the WTO dispute settlement mechanism provides an independent, rule-based system of adjudication that Russia had avoided in the past.

In spite of recent centripetal, unifying tendencies, EU member states have supported various political responses to Russian geoeconomic activity in the energy sector. Different understandings of or disregard for EU solidarity in dealing with Russian geoeconomics will continue to test the Union's internal cohesion in the future. It is crucial to note that the national positions within the EU are not straightforward derivatives of energy trade with Russia. For example, Russian gas makes up a larger share in the primary energy consumption of Finland than that of Poland.[105] Therefore, one can argue that Poland's frequent and vocal criticism toward Russian energy geoeconomics, notably on the Nord Stream project and SSPP, is not about energy security as such, but rather about conventional security policy. Poland considers, to an extent, that the less sovereign Ukraine becomes, the more security concerns Poland will face from the East.[106]

The struggle for the SSPP will leave a scar on EU-Russia energy relations. Geoeconomic wrangling over the rules of the natural gas trade in Europe continues in negotiations between Brussels and the Kremlin, in corporate boardrooms, and in civil litigation across Europe. Although the ultimate outcome hangs in the balance, the idea of Russian energy invincibility has been irrevocably compromised by the demise of the SSPP.

NOTES

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[10] The idea of commerce reducing the likelihood of war dates back to the High Enlightenment and especially the writings of Immanuel Kant, who famously noted, "The spirit of commerce, which is incompatible with war, sooner or later gains the upper hand in every state." See Immanuel Kant, Perpetual Peace (New York: Cosimo, 1795 [2005]), 39.

[11] Philip Stevens, "'Fragmentation' and 'identity' are reshaping the world," Financial Times, December 18, 2014.

[12] Mark Leonard, Why Europe Will Run the 21st Century (New York: Public Affairs, 2005), 245.

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[18] Luttwak, "From Geopolitics to Geoeconomics: Logic of Conflict, Grammar of Commerce," 128.

[19] Luttwak, "From Geopolitics to Geoeconomics: Logic of Conflict, Grammar of Commerce," 128-30.

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[23] Simon Pirani, Jonathan Stern, and Katja Yafimava, "The April 2010 Russo-Ukrainian Gas Agreement and Its Implications for Europe," (Oxford: Oxford Institute for Energy Studies, 2010).

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[25] Pirani et al., "The April 2010 Russo-Ukrainian Gas Agreement and Its Implications for Europe".

[26] Ibid.

[27] V. I. Yakunin, V. E. Bagdasaryan, and S. S. Sulakshin, Economic Policy Ideology (Moscow: Governance and Problem Analysis Centre, 2009), 226–31.

[28] Ibid.

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[31] See Energy Community web pages, available at: https://www.energy-community.org/portal/page/poral/ENC_HOME/ENERGY_COMMUNITY. For background, see the European Energy Charter, available at http://europa.eu/legislation_summaries/energy/external_dimension_enlargement/l27028_en.htm; and Partnership and Cooperation Agreements, available at http://europa.eu/legislation_summaries/external_relations/relations_with_third_countries/eastern_europe_and_central_asia/r17002_en.htm.

[32] Haukkala, "Towards a Pan-European Energy Order? Energy as an object of contention in EU-Russia relations."

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[34] Robert Legvold, ed., Russian Foreign Policy in the 21st Century and the Shadow of the Past, (New York: Columbia University Press, 2007); Marshall I. Goldman, Petrostate: Putin, Power, and the New Russia (Oxford and New York: Oxford University Press, 2010); Dominique Finon and Catherine Locatelli, "Russian and European Gas Interdependence: Could contractual trade channel geopolitics?" Energy Policy 36 no. 1 (2007): 423–42; Bartlomiej Nowak, "Forging the External Dimension of the Energy Policy of the European Union," The Electricity Journal 23, no. 1 (2010): 57–66; Nijaz Dizdarevic, "Regulatory Aspects Behind a Realization of the South Stream," Oil, Gas & Energy Law Intelligence 12, no. 2 (2014); Liuhto, "Energy in Russia's Foreign Policy"; Aalto, ed., The EU-Russian Energy Dialogue: Europe's Future Energy Security; Haukkala, "Towards a Pan-European Energy Order? Energy as an object of contention in EU-Russia relations," 1.

[35] Regulation (EU) No. 994/2010 of the European Parliament and of the Council of 20 October 2010 concerning measures to safeguard security of gas supply and repealing Council Directive 2004/67/EC. For an overview of the energy market legislation in the EU, see "Energy Market Legislation," European Commission, available at: https://ec.europa.eu/energy/en/topics/markets-and-consumers/market-legislation.

[36] Establishment and regulation of the single EU energy market brought into question several pre-existing Gazprom practices, including the use of its dominant position and long-term contracts, property rights for gas transmission pipelines and their exclusive operation, numerous re-nomination rights per day, buying separate entry/exit capacity at cross border points, and others. For years, Russia used its allies such as Germany, Hungary and Bulgaria in rejecting integration, transparency, and cooperation with neighboring countries, and successfully managed to thwart advances and delay the legal process. See, K. C Smith, K. C. 2008. Russia and European Energy Security – Divide and Dominate (Washington: The CSIS Press) p. 17 and Labelle, M. "The Day Hungary Cleaved from Europe: The True Cost of Russian Gas", 23 February 2015, available at: http://energyscee.com/2015/02/23/the-day-hungary-cleaved-from-europe-the-true-cost-of-russian-gas/. For the anti-trust action taken against Gazprom by the European Commission see: The European Commission,

Antitrust: Commission sends Statement of Objections to Gazprom for alleged abuse of dominance on Central and Eastern European gas supply markets, 22 April 2015, available at: http://europa.eu/rapid/press-release_IP-15-4828_en.htm.

37 Price differentials are important especially for the gas-intensive industries. See International Energy Agency, Energy Policies of IEA Countries – European Union, 2014 Review, p. 6; available at: https://www.iea.org/Textbase/npsum/EU2014SUM.pdf.

38 Andrew E. Kramer, "Putin Impedes European Inquiry of State Fuel Supplier," New York Times, September 11, 2012.

39 The term comes from the combination of the Latin words centrum, meaning 'centre', and fugere, meaning 'to flee'.

40 Karen Smith Stegen, "Deconstructing the 'energy weapon:' Russia's threat to Europe as case study," Energy Policy 39, no. 10 (2011): 6505–13. There is also differential treatment among Russia's allies; for example, in 2014, Gazprom delivered gas to Belarus at an average price of $164 per thousand cubic meters, while its European partner, Germany, paid $323.

41 Nijaz Dizdarevic, "Regulatory Aspects Behind a Realization of the South Stream." See also Commission Decision No. 994/2012/EU of the European Parliament and of the Council of 25 October 2012 establishing an information exchange mechanism with regard to intergovernmental agreements between member states and third countries in the field of energy,http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32012D0994:EN:NOT.

42 Umut Turksen, "Euro-vision of Energy Trade with Russia: Current problems and future prospects for EU solidarity in energy trade," Oil, Gas & Energy Law Intelligence 4 (2014): 1-40. See also "Yuzhno-Russkoye field development," Gazprom, http://www.gazprom.com/about/production/projects/deposits/yrm/, accessed July 6, 2015.

43 Ben Judah, Jana Kobzova, and Nicu Popescu, "Dealing with a Post-BRIC Russia," European Council on Foreign Relations (2011): 50; citing Andrew Rettman, "Polish FM in Wikileaks: Germany is Russia's Trojan horse," EU Observer, September 16, 2011.

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45 "Press Release: European Council Conclusions on the Energy Union," European Council, March 29, 2015; European Parliament Resolution of 26 October 2012 on EU-Russia trade relations following Russia's accession to the WTO (2012), 2695(RSP) - 2014/C 72 E/10; Regulation (EU) No. 994/2010 of the European Parliament and of the Council of 20 October 2010 concerning measures to safeguard security of gas supply and repealing Council Directive 2004/67/EC.

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47 Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee, and the Committee of the Regions: Second Strategic Energy Review - An EU Energy Security and Solidarity Action Plan, COM (2008) 0781, European Commission (2008a); and Memo: EU Energy Security and Solidarity Action Plan: Second Strategic Energy Review, MEMO (2008) 703, European Commission (2008b).

48 Dizdarevic, "Regulatory Aspects Behind a Realization of the South Stream"; Turksen, "Euro-vision of energy trade with Russia: Current problems and future prospects for EU solidarity in energy trade."

49 Talus, "Kansainväliset maakaasumarkkinat ja niiden sopimukset: Kehitys, sääntely ja riskit," Defensor Legis, 2013.

50 Ibid.51 Antto Vihma, "The Shale Gas Boom: The global implications of the rise of unconventional fossil energy," Finnish Institute of International Affairs, briefing paper 122, 2013.

52 Jonathan Stern and Howard V. Rogers, "The Dynamics of a Liberalised European Gas Market: Key determinants of hub prices, and roles and risks of major players," Oxford Institute for Energy Studies, paper 94, 2014.

[53] "Press Release: Energy: Central Eastern and South Eastern European countries join forces to create an integrated gas market," European Commission, July 10, 2015.

[54] The pipeline ownership in each transit country would be divided between Gazprom and a national partner with an equal split. Dizdarevic, "Regulatory Aspects Behind a Realization of the South Stream", 2.

[55] Georgi Gotev, "Final decision on South Stream pipeline in sight," Euractiv, July 17, 2012.

[56] Note that the map (published by Gazprom) omits Kosovo and depicts Crimea as Russian territory. See Gazprom, www.gazprom.com.

[57] Anouk Honore, "The Outlook of Natural Gas Demand in Europe," Oxford Institute for Energy Studies, paper 87 (2014); Jonathan Stern, Simon Pirani, and Katja Yafimava, "Does the cancellation of South Stream signal a fundamental reorientation of Russian gas export policy?" Oxford Energy Comment (2015); "Demise of South Stream big setback for Putin," Financial Times, December 2, 2014; Stanley Reed, "A Conduit for Russian Gas, Tangled in Europe's Conflicts," New York Times, June 30, 2014.

[58] Dizdarevic, "Regulatory Aspects Behind a Realization of the South Stream," 3.

[59] Guy Chazan, "South Stream gas project may now be a pipe dream," Financial Times, August 24, 2014.

[60] Liuhto, Energy in Russia's Foreign Policy, 26-28.

[61] Edward C. Chow, "Russian Gas Stream or Dream?" Center for Strategic and International Studies (2015). Gaining another large gas supplier has been a strategic priority for the European Commission; see also "Southern Gas Corridor: Vice-President Šefčovič attended Ministerial Meeting in Baku," European Commission, February 13, 2015, http://ec.europa.eu/energy/en/news/southern-gas-corridor-vice-president-%C5%A1ef%C4%8Dovi%C4%8D-attended-ministerial-meeting-baku.

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[63] Charles Clover, "Gazprom Secures South Stream Deal," Financial Times, November 15, 2012.

[64] "Press Release: South Stream construction starts in Bulgaria," Gazprom, October 31, 2013; "Press Release: South Stream comes to Serbia," Gazprom, November 24, 2013; "Press Release: Contract signed for South Stream design in Hungary," Gazprom, December 12, 2013.

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[10]6 Similarly, see Liuhto, Energy in Russia's Foreign Policy, 12.

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