Natural Gas in the Mediterranean: More than Just a Commodity, Less than a Factor of Interdependence?

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The Mediterranean energy picture captures in microcosm many of the issues facing the global energy market today. Growing demand in the economies of energy consumers and suppliers alike, depleting (European) reserves and limited supplies, socio-political instabilities and geopolitical tensions are all factors squarely weighing into the considerations of policy-makers, often creating a nexus between the commercial and the political dynamics of the energy market. Nowhere is this reality more prevalent than in the natural gas market, particularly so in the Mediterranean.
As the fastest growing source of primary energy among the major fuels, used in large part for electricity generation, natural gas is traded mostly by pipeline connections and increasingly in liquefied form through liquefied natural gas (LNG) vessels. Its increasing attractiveness as a fossil fuel is driven largely by its efficiency and growing environmental awareness on the part of consumers. Producers, for their part, besides capitalising on large and under-explored reserves, are seeking to secure shares in the booming gas markets and acquire further technical and commercial know-how. In the Mediterranean, existing and expanding pipeline infrastructure linking major players like Algeria, Egypt and Libya to southern European shores, supplemented by LNG export and import terminals, has come to reinforce the traditional supply-demand interdependent relationship that has characterized the region. More recently, however, mounting tensions between consumers and suppliers, including in the Mediterranean, have exposed the double-edged nature of their interdependence, accentuating resource nationalist reflexes on both sides.

The European Union's (EU) normative confrontation with Russia since the former's 2004 enlargement, which extended its frontiers well beyond the remains of the iron curtain, has spilled over into their energy relationship, leading to European fears over the extent of the block's dependence on Russian gas supplies. Subsequently, southern Mediterranean producers were turned to as potential alternative suppliers for the EU. The concept of "strategic energy partnerships" between the EU and these suppliers was then advocated by policy-makers as a means of operationalising the EU's new security of supply strategy.
On the other hand, the growing confidence and sophistication of major Mediterranean gas sellers, owing to record-high prices and unprecedented relational strength, have brought their ambition of seeking added-value elsewhere, such as in the downstream of the European market, at loggerheads with the EU's sense of vulnerability and policies. The resulting state of play falls short of reflecting the oft-rhetorically celebrated interdependence between the two shores and risks failing to optimise their (energy) relationship. 2007 was the year in which the coming together of these old and new dynamics of the Mediterranean energy scene upset its traditional configuration.

2007, a Turning Point?

The EU's energy dependence on foreign supplies is forecast to rise from 50% today to more than two-thirds by 2030. Of those imports, gas is likely to grow significantly in the European energy mix, with more than 80% of the EU's gas consumption provided by a handful of major suppliers. Russia, which currently supplies the EU with a little more than 25% of its gas consumption, will, *ceteris paribus*, remain the major supplier of gas to the Union.

To this extent, Russia's energy policies are of immediate relevance to the EU's energy security concerns. In this context, Moscow's 2005 decision to revise upwards the price of its gas for its former satellite republics – now decidedly turned westward – and the ensuing dispute which pitted it against Ukraine in January 2006, brought home two startling realities for the EU. First, it became clear that depending for vital energy supplies on one single source exposes energy security vulnerability even to unintended supply disruptions. More importantly, however, the "Ukraine episode" raised the dual question of whether Russia was a reliable energy partner and whether energy now became for Moscow what the normative *acquis* had been for Brussels – in other words, if energy was becoming Russia's new foreign policy tool.

The sense of urgency for action on an EU energy policy set in motion by the 2006 winter crisis was exacerbated by the Russian-Algerian gas rapprochement during the same period. The signing of two memoranda of understanding (MoU) between the EU's biggest gas suppliers, Gazprom and Sonatrach respectively, in August 2006 and in January 2007 caused furore in European and, to a lesser extent, transatlantic policy circles. The discretion and opacity surrounding the conclusion of the first MoU in particular spurred anxious reactions to the putative prospect of cartelisation of the gas market, under the strategic impetus of Russia and Algeria. Subsequently, the warming to the idea of a "gas OPEC", expressed in sequence during the first three months of 2007 by the political leaders of Iran, Russia and Algeria, drew excessive attention to the 6th ministerial meeting of the Gas Exporting Countries Forum (GECF) that took place in Doha, on 9th April. Established in 2001, the GECF has been a loose structure, bringing together some fifteen of the world's largest gas producing countries, whose vocation is unlikely to be turned into that of a gas cartel simply under political impetus. In fact, many commentators have advised that, given the nature of the gas market(s) on the one hand and the triadic relationship Russia-EU-Algeria on the other, a gas OPEC was an unlikely short- to medium-term evolution of the GECF and more so under Russian-Algerian collusion (Hallouche 2006; Darbouche 2007; Stern 2007). The expiry in August 2008 of the first MoU between Gazprom and Sonatrach and the apparent explicit decision of Algerian officials not to renew it corroborated the view that Russian and Algerian interests were far from the level of convergence necessary for any collusion on their part to result in a gas cartel.

This gas saga aside, the momentum that emerged in 2006 among European government and Commission (EC) officials for a firmer collective energy policy commitment culminated in 2007 in a series of strategy documents stressing, inter alia, the establishment of international (energy) partnerships with neighbouring producers, based on "shared rules or principles derived from the EU energy policy." In this vein, the high-profile September "unbundling" proposal (separation of gas and electricity production and distribution networks) is seen in Brussels as conducive not only to better internal competitiveness and efficiency but crucially as a means of influencing the normative frameworks of third producer countries (Youngs 2007: 2). However, the Commission's inability so far to surpass enduring divisions within member states over the liberalisation of the internal market has botched its efforts "to speak with one voice" with third-supplier interlocutors. Member states like France, Spain and Germany still prefer bilateral approaches to negotiating access and reciprocity. Besides sending confusing "normative" signals to producers, this attitude precludes the very predictability of interdependence that the EC's 2007 Strategy Review aims to attain and which, from a supply stand point, is of equal importance. As a result, the partnerships proposed by the EU to its energy suppliers are missing an explicit geopolitical element that takes account of the nature of the energy market, the preoccupations of its suppliers and the properties of their energy relations with the EU.

Nouvelles donnes, nouvelles mœurs in Euro-Mediterranean Cooperation?

The Mediterranean segments in the policy documents of the EU's recent energy strategy reviews identify the strategic need for more comprehensive partnerships with countries like Algeria, Libya, Egypt and Qatar as a priority. Indeed, these countries sit at the forefront of the regional gas supply scene. While their export capacities and structures vary, these producers share an undisputable potential in meeting growing European gas demand. As such, the EU's heterogeneous prioritisation of strategic energy partnerships in its relations with these countries reflects not only their export potentials, but also the type of the existing policy frameworks governing their broader relations with the EU. Accordingly, Algeria tops the EU's priority list as indicated notably by declarations in 2007 of Commission officials, such as Andris Piebalgs and Benita Ferrero-Waldner and the European Parliament President Hans-Gert Pöttering. Indeed, helped by geographical proximity, Algeria has traditionally been one of the major supplies of gas to Europe. About 95% of its 65 billion cubic meters (bcms) of gas exports is destined to the European market. Decisions taken in 2007, furthermore, regarding the realisation of strategic pipeline infrastructure, notably Medgaz (linking Algeria directly to Spain), Galsi (a direct submarine connection to Italy) and the Trans-Saharan Gas Pipeline (transporting Nigerian gas to be exported via the Algerian network), can only consolidate this position.

Egypt comes second in this European pecking order. The recent expansion of natural gas production has endowed Egypt not only with a vital economic growth engine, but also with an additional factor for deepened cooperation in its relationship with the EU, already governed by a Euro-Med association agreement and a Neighbourhood Action Plan. Through its support for the Arab Gas Pipeline, which will transport Egyptian gas, through Jordan and Syria, to Turkey and potentially to Eastern Europe via the planned Nabucco pipeline, the EU is hoping to dip further into the country's 17 bcms of gas exports. Qatar, for its part, has since 2006 surpassed Indonesia as the world's largest LNG exporter and is predicted to supply as much as 30% of the world LNG market by 2010. As such, Qatar offers a viable alternative for the EU in its efforts to reduce its heavy reliance on pipeline deliveries. However, both the EU's preference for a regional approach towards the Gulf Cooperation Council (GCC) in relation to energy (and other) matters and the absence of a European LNG policy that allows it to compete with the Asian and American markets – both Qatar's traditional consumers – have so far trumped Community aspirations for a more strategic partnership with the latter. As to Libya, despite its recent attempts to normalize its relations with "the West," especially after the resolution of the Bulgarian nurses' crisis in July 2007, no framework has been established yet to streamline its relationship with the EU. With 1,500 bcms of gas reserves, Libya exports a little over 7 bcms of gas to Europe via the Greenstream pipeline which joins it with Italy via Sicily. The scope for an enhanced role for Libya in satisfying the EU's increasing demand is evident, but until the country adopts a clear energy export policy the prospects for a comprehensive strategic partnership remain rather meagre.

At the macro level, besides the EU market's lack of competitiveness relative to the growing and liberalized North Asian and American markets, the energy interdependence in the Mediterranean space that the EU's proposed partnerships purportedly aim to reflect and consolidate is challenged by the fact that the extant energy-markets governing principle of "buyer brings market, seller brings supply" is withering under the effect of new and intertwined economic and political realities. Firstly, recent economic growth in most producer countries, fuelled by record-high energy export revenues, is in turn driving domestic energy demand upwards, leading to a situation of pressure on these countries' abilities to simultaneously meet their growing gas export commitments. Indeed, with this situation and their eager efforts to diversify their economic activities and create employment opportunities for their often-disillusioned youths, producer countries in the Mediterranean are increasingly faced with a difficult choice: to divert resources away from hydrocarbon investments in favour of other economic sectors at the expense of rentierism; or, to expand energy production and exports, even through foreign direct investment (FDI), at the expense of real economic growth and rationalisation of exploration of reserves. In the present conjuncture, most Mediterranean producers, especially those with sizeable populations and heavy economic reliance on hydrocarbons, such as Algeria, appear to have opted for the former course of action.

Secondly, and relative to the properties of the current juncture, namely high energy prices and a race for access to reserves, gas sellers are growing in sophistication and are as a result seeking to integrate vertically along the value chain, such as through the downstream of the European market. However, such policy orientations, witnessed in particular in the case of Algeria's Sonatrach, are almost antipodal to the EU's proposal for a strategic energy partnership with the country, which appears limited to attempting to export the EU's *acquis* in this area to Algeria. Notwithstanding the confusing normative signals of the EU's "unbundling" proposal, these EU strategic partnership proposals not only reinforce the asymmetrical interdependence described above by failing to take account of the economic and political preoccupations of producers, but they also seem to duplicate the regional multilateral work of the EU in this policy area. More specifically, the Euro-Mediterranean Energy Partnership (EMEP), launched in 1996 under the umbrella of the Barcelona Process, provides the optimal framework for the materialisation of a global Euro-Mediterranean strategic energy partnership, especially after its reinforcement by the Ministerial Conference of 17th December 2007 which adopted an ambitious 5-year "priority action plan", aimed at:

- The implementation of energy market reforms and the gradual harmonisation of regulatory frameworks amongst Euro-Mediterranean partners;
- Engaging in more sustainable energy policies and
- Improving investment climate to ensure the diversification of energy sources.

For the sake of rationalisation of policy, the EMEP ought to be integrated into the newly proposed "Union for the Mediterranean" to constitute a concrete element of a strategic regional partnership, taking account of the *nouvelles donnes* that are now prominent in the Mediterranean energy scene.

The Geopolitics of Gas in the Mediterranean: A Conclusion

The closest materialisation so far of the growing asymmetrical interdependence that characterizes the Mediterranean gas scene manifested itself in 2007 in the form of a multi-facetted gas dispute between Spain and Algeria. As the closest energy partners in the Mediterranean, the two countries have hitherto enjoyed an exemplary supply-demand relationship. However, Sonatrach's aspirations to penetrate the Spanish market and commercialize its share of gas that will be transported by the Medgaz pipeline (3 bcms) were circumscribed by apparent Spanish protectionism. Indeed, Spain's Repsol and Gas Natural, two companies heavily present in the Algerian upstream, formed an opposing front to Algeria's state-owned company for no rational pretext. After thorny negotiations, however, the issue was resolved but only to give way to another bitter discord. This time, it was Sonatrach that decided to terminate the two Spanish companies' joint contract for the development of a $5 billion LNG project in Gassi Touil, after major delays and rising costs, leading to an (pending) international arbitration procedure. Despite the commercial and economic reasons invoked by the Algerian party, the timing of its decision inevitably led to interpretations positing that the move is at best retaliatory and at worst politically motivated. In this vein, Algeria's move in March 2007 to publicly announce a decision it had made two years back to revise upwards the price of its gas sold to Spain and the enduring Western Sahara dispute were referred to as possible hidden motives behind this dispute.
If anything though, the Hispano-Algerian gas crisis demonstrates that, while remaining more than just a commodity, natural gas in the Mediterranean is proving to be less than a factor of interdependence. Relations between consumers and producers are growing in complexity owing mainly to the shifting dynamics of the energy and particularly gas market. While legitimately seeking to secure their energy supplies and satisfy their growing demand, European consumers are failing to take account of producers' interests in their efforts to that end. The latter, on the other hand, while ever more dependent on their energy export revenues are growing in confidence and starting to look beyond immediate commercial interests. The Mediterranean gas picture shows that, while interdependent in many ways, consumers and producers in the region have to look for novel ways in order to sustain that interdependence and redress its inherent asymmetry. The EU needs to engage in meaningful partnerships with its southern suppliers, assisting them more effectively in their political and economic reforms and allowing them access to its market and technologies. Suppliers, for their part, need to adopt more transparent regulatory frameworks and show more openness to political and economic liberalisation. It will take more than just a bunch of "strategic energy partnerships" – perhaps a Union for the Mediterranean is what is needed?

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