SECTION 31. Economic research, finance, innovation, risk management.

GERMAN – RUSSIAN COLLABORATION FOR THE NORD STREAM II PROJECT: SACRIFICING THE COMMON EUROPEAN INTEREST?

Abstract: This article looks at special relations between Germany and Russia in terms of gas politics in the European Union (EU). On the one hand the EU seeks to diversify its sources of natural gas supply and reduce the dependence on the Russian Federation. On the other hand, Germany, being one of the leading EU members, supports giant gas pipeline projects such as Nord Stream II to import gas from Russia. Such projects aim at undermining the importance of the traditional transport routes from Russia through Eastern Europe; a strategy which is directly in contradiction with the EU’s overall energy security. This article explores the driving forces behind such problematic relations between the energy superpower Russia and the leading EU member, namely Germany. In this respect, above all, the general tendencies of pipeline politics between the EU and Russia is discussed. And then, competition between specific planned natural gas projects, namely Nord Stream II and Trans-Caspian, is explored.

Key words: German – Russian energy collaboration, Nord Stream II, natural gas politics, Trans-Caspian pipeline project.

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Introduction

This article explores special, yet controversial relations between Germany and Russia in the gas politics. On the one hand, Germany collaborates with Russia in the field of energy resources and on the other, it is one of the EU members who has harshly criticized Russia for the conflict in Ukraine. Without German support Nord Stream II cannot be realized. Such a support has helped Gazprom to stand against the European commission as well as Central and Eastern European countries. In general, the EU – Russia relations is based on interdependence; the EU depends on Russia for nearly 40% of its gas imports, whereas Russia depends on the money it gets for its energy resources. A closer look at the projects such as Nord Stream II reveals the main drivers of the ‘special’ relationship between Russia and Germany.

This article starts with a historical glance at the Russian – German gas cooperation. And it places this cooperation against the backdrop of the EU’s energy dependence from Russia. In addition, interlinkage between the energy projects – both launched and planned – within Southern Gas Corridor and the Nord Stream II project is looked at to gauge the competition thereof. It is important to note that the time frame under scrutiny is mainly from 2015 onwards as that suffices to present the updated developments. However, to display the development of overall trade and gas imports between Russia and EU as well as Germany, data on the preceding years have been also provided.

Overview of the German – Russian gas imports

In this section a brief overview of the German – Russian economic interdependence is provided. The main focus is on the gas imports from Russia in order to explicate how far Germany is indeed dependent from Russian gas. To begin with it is important to give the snapshot of the trade balance between the EU and Russia for the last decade. As can be seen from the Figure 1, over the years between 2008 up to 2017, the EU’s trade balance in goods with the Russian Federation has been in deficit. This deficit peaked around at EUR 90 billion in 2011 and dropped to nearly EUR 60 billion in 2017.
### Impact Factor:

|                | ISRA (India) | SIS (USA) | ICV (Poland) |
|----------------|-------------|-----------|--------------|
| ISI (Dubai, UAE) | 0.829       | 0.156     | 1.940        |
| GIF (Australia) | 0.564       | 5.015     | 4.260        |
| JIF            | 1.500       | 5.667     | 0.350        |
| PCI            | 0.72        | 0.28      | 1.07         |

According to Eurostat (21 August 2018), among the 28 EU members, Germany was the largest exporter and importer of goods to/from Russia. For 2017 Germany’s imports from Russia were worth EUR 29 billion whereas its exports were in worth of EUR 26 billion which is almost 30% of all EU exports to Russia. That means Germany had EUR 3 billion trade in goods deficit with Russia. In general, the EU members have been exporting manufactured goods (90% of the exports) to Russia while importing the energy products (of which one-third represented by natural gas). It is important to note that between 2010 and 2015 gas demands in Europe was in decline. However, since 2015 it has been again increasing. For 2016, Germany imported 106 billion cubic metres (bcm) of gas which made 23% of the nearly 465 bcm total EU gas imports (Market Observatory for Energy of the European Commission, 2017, p.4). Germany’s gas consumption for the same year was 101.5 bcm (BGR, n.d.). In 2017, EU’s total gas demand was 548 bcm, and 408.7 bcm of that volume was covered by imports. By meeting 193.9 bcm, namely over 40%, of this demand, Russia has remained a crucial supplier (Honore, April 2018, p.1; Czajkowski, February 2018; Foy, 3 January 2018).

The structure of trade between the EU and Russia holds true for Germany as well. The below Figure 2a demonstrates the structure of the imports to Germany from Russia, where crude oil and natural gas dominate the list followed by petro-chemicals. Thus, almost 75% of the imports are accounted for by the energy products.

**Figure 2a.** German imports from Russia, 2016 (€26.4 bln.)  
**Figure 2b.** German gas imports, 2016

As of 2016, with 35% of imports, Russia was the largest natural gas supplier for Germany. As presented on the Figure 2b, Norway and the Netherlands followed with 34% and 29% respectively. Germany’s dependence from Russia in terms of gas imports looks moderate if compared...
with the EU’s some of the Eastern European members such as Poland, Slovakia, Hungary, Greece and Finland which are fully dependent from Russian imports (Mearns, 19 November 2014). The Figure 3 illustrates how far some of the EU member countries are gravely dependent on Russian gas.

It is important to point out that in 2017 Russian gas exports to Europe, increasing by 8.1%, reached a record level at 193.9 bcm where Germany took the lion’s share with 53.4 bcm (increase from 42.63 bcm in 2016) (Almost 13% increase in its gas imports from Russia. Germany’s total gas imports were 94.8 bcm for 2017 (Statista, 2018), which was 27.5% of Gazprom’s total exports in 2017 (Foy, 3 January 2018; Keating, 19 July 2018). Therefore, German–Russian relations on gas is a matter of interdependence rather than a dependence as Russia also needs a promising European market for its supplies. In this respect, being a stable economic giant, Germany is an important partner for Russia.

As already have been implied, this can be seen as an interdependence between the two actors. Nevertheless, this interdependence offers Russia an important leverage over the EU. Yet, one issue remains a challenge for Russia in this regard, that is the persisting dependence on transportation routes which is discussed in the next section.

Transportation routes of Russian gas to Europe: role for the Nord Stream II and divides in the EU

Dependence on transport routes that are passing through other countries such as Belarus and Ukraine (See the Figure 4) has been a serious concern for Russia. Especially the route through Ukraine has been troublesome given the rounds of past transport crisis as well as the ongoing separatist conflict in Ukraine where Russia has been taking latent but an active role (Faundes, 2016). The key question is how vulnerable will be the EU after the realization of Nord Stream II? Does it threaten the EU’s energy policy in terms of diversification of energy supply sources? To answer this, firstly it is important to look at the developments around the Nord Stream II pipeline project and map out the actors who are in favour and who are against the project. Moreover, to analyse what stake is at hand for the EU in general and Germany in particular.

Nord Stream II, with $11 billion cost, is the extension of the Nord Stream I project under the Baltic Sea – offshore gas pipeline from Russia to Germany – which became operational in 2011 with the annual capacity of 55 bcm (Nord Stream 2, 14 August 2018). In June 2015, an agreement to launch Nord Stream II was signed between Gazprom, BASF/Wintershall, Royal Dutch Shell, ENON, OMV, and Engie. In 2017 financial agreement for the project was also signed (Nord Stream 2, 14 August 2018). As demonstrated on the below map, the Nord Stream II is planned to be constructed parallel to the already operating Nord Stream I pipeline.
Impact Factor:

| Journal                  | Impact Factor |
|--------------------------|---------------|
| ISRA (India)             | 3.117         |
| ISI (Dubai, UAE)         | 0.829         |
| GIF (Australia)          | 0.564         |
| JIF                      | 1.500         |
| SIS (USA)                | 0.912         |
| PHHI (Russia)            | 0.156         |
| ESJI (KZ)                | 5.015         |
| SJIF (Morocco)           | 5.667         |
| ICV (Poland)             | 6.630         |
| PIF (India)              | 1.940         |
| IB (India)               | 4.260         |
| OAJI (USA)               | 0.350         |
| RIHNC (Russia)           | 0.156         |
| ESJI (KZ)                | 5.015         |
| SJIF (Morocco)           | 5.667         |
| ICV (Poland)             | 6.630         |

Map of Nord Stream I and II pipeline projects.
Source: Gazprom. (24 May 2018).

Even after Nord Stream pipeline started operation in 2011, it has not been able to reduce the Ukraine’s importance as a transit country. As of 2017, nearly 80 bcm gas – 41% of the total Russian exports to Europe – was transited through Ukraine. According to Shiryaevskaya, Krasnolutska and Mazneva (21 March 2018), Russia will not be able to change this dependence in the coming few years.

Figure 4. Russian gas transport routes to the EU
Source: Shiryaevskaya, Krasnolutska and Mazneva (21 March 2018).

The capacity of the Nord Stream pipeline is 55 bcm, and in 2017, 51 bcm was transported through the pipeline (Nord Stream Press Release, 16 January 2018). If realized, the Nord Stream II pipeline project will have the capacity to alleviate the dependence on transportation routes substantially. In other words, the Nord Stream II project is planned to have 55 bcm capacity; thus, both Nord Stream pipelines together will transport 110 bcm (almost 57% of the Russian gas exports to Europe) to Europe bypassing Ukraine and Belarus. Given the fact that Russia has not had any hassle with Belarus in regard to gas transport, this is an optimistic scenario for Russia as its dependence on Ukraine’s transport route will be reduced to nearly 15% from the current level which is 41%; that disapproves Shiryaevskaya, Krasnolutska and Mazneva’s (21 March 2018) assumption that Ukraine will remain a crucial transit country for the Russian gas.
By end of 2019 Nord Stream II pipeline is planned to become operational. However, that scenario depends on how the deepened cuts and divides between the U.S. and some of the EU members on the one side and German – Russian cooperation and some of the EU members on the other side will end up. Indeed, in 2016, the US senators John McCain and Marco Rubio sent a letter to the President of the European Commission Jean-Claude Juncker naming the Nord Stream 2 as a “step back for Europe’s diversification policy and Energy Union plans” (Eurasia Daily, 14 July 2016). That is a sign that the gas politics in the EU is a tip of the bigger iceberg. Put it differently, U.S. has own stakes on the energy deals in Europe; the Trump Administration intends to export LNG to the EU (Blinova 2 August 2018; Eckert, Vukmanovic and Zawadzki, 26 July 2018). In July 2018 during the NATO Summit, the U.S. President Trump accused German Chancellor Merkel for being Russian “captive” referring to the plans on Nord Stream II (Feldman, 12 July 2018).

Paul Corcoran, the chief financial officer of the Nord Stream II named the project “European collaboration” supported and realized by Germany, France, the UK, the Netherlands and Austria (Nord Stream 2, 2018). On the one hand the great players of the EU have been supporting the Nord Stream II, whereas mainly the Central and Eastern European countries such as Slovakia, Czech Republic, Estonia, Croatia, Hungary, Lithuania, Latvia, Poland and Romania as well as Denmark have been against (Gotev, 9 May 2018; Liptakova, 6 April 2018). The main argument in going against the Nord Stream II has been that it “violates principle of diversification and poses another risk of further destabilizing Ukraine” (Liptakova, 6 April 2018). Securing the construction permission from the Baltic countries was an important hurdle for the countries behind the Nord Stream II. However, after Germany and Finland, Sweden has also granted its permission for the construction of the pipeline, leaving Denmark the only country whose permission is still missing (Gotev, 8 June 2018). Indeed, Denmark’s permission is essential to complete the investment scheme and carry out the construction works on the Baltic seabed. As the majority of parties in Danish parliament are against the Nord Stream II, the construction of the pipeline in its territorial waters (south of Bornholm) can be blocked. Yet, the pipeline can be constructed through Danish exclusive economic zone, where only objection would be environmental one (Loskot-Strachota, 12 September 2018).

Having secured the support and construction permission of the key players in the EU, the implementation of the Nord Stream II project is closer. Concerning the implementation of the project, Vaclav Bartuska, the energy ambassador for the Czech Republic stated that: “Nord Stream 2 has now advanced to the stage when it could be stopped only by U.S. sanctions…otherwise it’s going to be built.” (Johnson, 19 July 2018). Interestingly, on 5 September 2018, the construction works of the Nord Stream II has started in the Gulf of Finland, not in Germany. It is also claimed that due to the American pressure the construction works started in Finland (Loskot-Strachota, 12 September 2018).

Due to the persisting American pressure on Germany to halt the collaboration with Russia on Nord Stream, on 18 August 2018 German Chancellor Merkel has had a meeting with the Russian President Putin in Meseberg, Germany to discuss the situation in Ukraine. One of the key issues discussed was the Nord Stream project. Merkel was quoted saying that “Ukraine must continue to play a role in gas transit to Europe, even after the Nord Stream 2 gas pipeline is activated” (Kwiatkowska-Drożdż and Rodkiewicz, 22 August 2018).

Moreover, Merkel’s visit to Azerbaijan was also widely interpreted as due to the EU’s energy interests. To put it differently, it is believed that she has made the visit to Azerbaijan to ensure that Germany is not betraying Trans-Caspian project by supporting the Nord Stream II (JAMNEWS, 26 August 2018; Rinke, 22 August 2018). At the business roundtable on 25 August in Baku, Merkel stated that “Azerbaijan is an important partner in the diversification of our energy supply within the European Union” (Gotev, 27 August 2018). Against the backdrop of the American pressure on Germany and Merkel’s meeting with the Russian and Azerbaijani presidents, a deal about the realization of both Nord Stream II and the Trans-Caspian project cannot be ruled out. That would partially alleviate the cuts and divides in the EU as the Trans-Caspian project is a crucial part of the EU’s Southern Gas Corridor which has been given the ‘priority project’ status. Realization of the Trans-Caspian project can be interpreted as getting the award for granting green light for the Nord Stream II by some of the EU members. Put it differently, support for the Nord Stream II has secured the silence for Trans-Caspian on the part of Russia.

**Two pipelines, the same market: Trans-Caspian pipeline against the Nord Stream II?**

12 August 2018 marked a historical event concerning the legal status of the Caspian Sea; namely the littoral states agreed to solve the protracted delimitation issue. That in return revived the hopes for laying a pipeline under the Caspian Sea to transfer the Kazakh and Turkmen gas through Azerbaijan to Europe which was originally proposed by the U.S. in 1996 (Sputnik, 14 May 2007). Trans-Caspian pipeline aims at freeing Central Asian nations from Russia in terms of energy independence and meantime helping the EU to diversify its energy...
supply sources. This project is considered as an eastern extension of the EU’s Southern Gas Corridor. In 1999, the heads of governments of Azerbaijan, Georgia, Turkey and Turkmenistan signed an agreement of intent to start the construction of Trans-Caspian pipeline to transfer 30 billion cubic meters of gas per year from Turkmenistan (RFE/RL, 19 November 1999). However, given the strong opposition of Iran and Russia who raised the issues of the unresolved status of the Sea as well as the possible environmental hazards, the agreement of intent has not been taken to the next stage. Nevertheless, the EU has kept the issue in its energy policy agenda and continued the meetings with the concerned regional states (Vogel, 14 September 2011; Chaffin, 11 September 2011).

However, resolution of the Caspian’s legal status cannot ensure the construction of the pipeline through the Sea as it will require the consent of all the littoral countries. Even overlooking that challenge, economic and political obstacles might persist. On the one hand the Nord Stream pipeline project has become closer for realization, which has 55 bcm capacity and on the other hand Trans-Caspian pipeline with its 30 bcm planned capacity is yet far from realization, as no financial or construction agreements signed. Both pipelines target the promising European market, through different routes. Additionally, Azerbaijan will be sending its own 10 bcm gas with Trans-Anatolian and Trans-Adriatic pipelines to Europe. And, there are some other alternatives such as Turkish Stream which needs to be taken into consideration. Therefore, the question is if the EU will be still willing to import new supplies of gas. The answer partially also depends on how far LNG imports proceed in Europe and how far the EU will be willing to reduce dependence on Russia by diversifying the transportation routes.

In a retrospect it is the fact that Europe has substantially reduced its dependence on Russian gas for the last 25 years. In early 1990s, this dependence was 75% but by 2017 it was 37% (Rumer, 12 August 2018). The LNG and new sources of gas supplies, e.g. from Azerbaijan, help Europe to decrease the dependence on Russian gas. Trans-Caspian project is classified as one of the EU’s ‘priority projects’. Therefore, the EU will remain willing to realize the project, and accommodate 30 bcm new supplies from the Caspian Basin. Given the decreasing gas supplies in the Europe, it should be not a challenge for the EU to receive supplies both from the Trans-Caspian and the Nord Stream II. However, the main question is how earnest is the EU with the diversification of its energy supply sources. Put it differently, how far national interests of single members such as Germany prevail over the EU’s common interests.

**Conclusion**

German – Russian bilateral relations have controversial nature. On the one hand, Germany collaborates with Russia in the field of energy resources. On the other hand, it is one of the EU members who has harshly criticized Russia for the annexation of Crimea. It is clear that without German support Nord Stream II cannot be realized; this support is the greatest weapon Gazprom has obtained. Such a support has enabled Gazprom to stand against the European commission as well as Central and Eastern European countries. In general, the EU – Russia relations is based on interdependence; the EU depends on Russia for nearly 40% of its gas imports, whereas Russia depends on the money it gets for its energy resources.

As it has turned out, the Nord Stream II pipeline seems to be realized, probably with some delays, despite the resistance from the U.S. and some EU members such as Poland. However, revival of the Trans-Caspian project, as linked to the heated-up discussion on Nord Stream II project, serves the EU’s common energy interests in terms of diversification of supply sources. If realized, Trans-Caspian project will help the Central Asian countries to reduce their dependence from Russian manipulation over the gas export routes. That will also serve the interests of the transit countries such as Azerbaijan, Georgia and Turkey. These countries will be benefiting from the great game over the energy politics in Europe.

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