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Article

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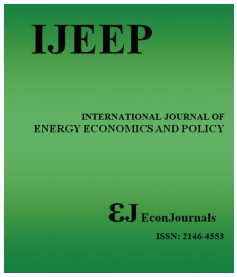

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The Role of Fuel and Energy Sector in the Eurasian Economic Community Integration Process

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ABSTRACT

The article focuses on creation of the common energy space among the customs union (CU) and the common economic space countries. We analyzes energy markets in Russia, Kazakhstan and Belarus, natural resources potential of these countries and their energy exports, as well as pays particular attention to the current oil and gas supplies regulation within the CU. The main problems emphasized in the article are the common oil and gas market establishment, harmonization of the national energy legislation, effective transit potential use, development and adoption of common rules for the oil and gas industry access, removal of duties and establishment of common tariff policy. In conclusion, recommendations for development of Russia's Eurasian integration strategy are presented.

Keywords: Energy, Eurasian Integration, Common Economic Space
JEL Classification: F020

1. INTRODUCTION

Implementation of the single energy space strategy is one of the most important stages of the Eurasian economic integration. Today the custom union (CU) and single economic space (SES) energy legislation is largely shaped and governed in accordance with the agreement 2010 and the additional bilateral agreements which are to be signed before the common oil and gas market creation (Ministry of Economic Development of the Russian Federation, 2017). However, progress in this area is slowed by huge divergences between the existing intergovernmental agreements and internal laws of the Eurasian union. The oil and petroleum products common market agreement and gas infrastructure access agreement are among the most important agreements for the CU and SES common oil and gas market creation (Eurasian Economic Commission, 2014).

The Eurasian common hydrocarbon market is assumed to be created by 2025. As Viktor Khristenko, the chairman of the Board of the Eurasian Economic Commission said: "All the oil and gas related issues will be settled in full accordance with the agreement 2010 and relevant bilateral agreements which guarantee proper status of interaction in these areas during the entire period before the formation of the single market. The common gas, oil and petroleum products markets will be launched no later than 2025, and the Presidents will approve the concepts by 2016" (Eurasian Economic Commission, 2014).

The Eurasian economic union was expected to be established without exceptions and limitations by 1st January, 2015. However, while signing the Eurasian Economic Community treaty, it was decided to stick to the principles of gradual common energy markets formation up to 2025. This decision also affected the electricity market, which is scheduled for launch in 2019.

Considering the energy cooperation issues within the CU countries, it is necessary to analyze the distinctive features of the regional energy markets development.

2. ENERGY MARKETS OF THE CU AND SES COUNTRIES

Russia is one of the leading countries in the world energy trade, which makes it an important element in ensuring energy security, especially in Eurasia.

According to the foreign estimates, Russia takes the seventh place in the world in terms of oil reserves (accounting for 6% of world reserves), the first place in terms of annual oil production (13% of world production) and provides over 15% of the world's oil exports. Russia ranks first on proven reserves of natural gas (23% of world reserves), takes the second place after the USA in terms of annual gas production (18% of world production) and is the world undisputed leader in terms of gas export, providing more than 20% of world gas trade. Russia also ranks world's second for coal reserves (18% of world reserves), takes the sixth place in terms of annual coal production (4%) and provides 13% of global coal power trade and up to 7% of coking coal trade (BP, 2016).

Russian energy complex and energy infrastructure are even more important for the Eurasian space.

More than four-fifths of Russian oil is exported to Europe, and Russia accounts for about 30% of that market. The leading importers of Russian oil are Germany, Italy, France, Poland and Netherlands. Russia is engaged in the process of oil export diversification as it develops oil exports to China. However, the main direction of Russian oil export is still the European market.

The whole Russian gas pipeline export is also limited only by European and CIS markets.

Russia is also present on the North-East Asian market (Japan, Republic of Korea, in some negligible quantities in Taiwan and in China) due to liquefied natural gas supplies, with the export share of 8.3% in these countries in 2011 (Belogoriev et al., 2011).

According to BP, Russia remains the dominant natural gas supplier in the CIS market, as well as in the all post-soviet states, accounting for 91.9% in regional trade. It should be noted that Russia traditionally is a major gas importer on the CIS market; however, the import volumes are at the historical low, which is caused by the ongoing Turkmen gas import reduction since 2009. According to BP calculations Russia imported 30 billion cubic meters of natural gas from Kazakhstan, Uzbekistan, Turkmenistan and Azerbaijan in 2011, which accounted for 2.9% of global trade, or 13.5% of Russian exports. Moreover, nowadays natural gas supplies to Russia are critically important for Kazakhstan (almost 100% of total exports), Uzbekistan (78%) and Turkmenistan (30%) (BP, 2016).

European countries (including Turkey) account for 70% of natural gas export from Russia. However, the EU dependence on Russia's gas suppliers is only 30%, while some countries are fully dependent on Russia's gas deliveries.

Russia ranks world's third in terms of coal export, which makes Russia significantly inferior to Indonesia and Australia. Russia's share in world power coal generation trade is 12.9%.

Electricity export from Russia (accounting for 1.8% of Russian total production) does not play a significant role on a global scale, but it is important for energy cooperation with the Eurasian Economic Space countries. The main consumer of Russian electricity is Kazakhstan (50%), which uses the purchased electricity for the energy supply in its northern regions. Belarus also purchases Russian electricity, although the volume of purchases has been recently reduced following the decline in electricity demand in the country.

Kazakhstan with its rich energy resources plays an important role in the Eurasian energy sector. Thus while the country's gas reserves are in the initial stage of development, oil, coal and uranium are the main energy exports from Kazakhstan.

The total estimated recoverable hydrocarbon reserves in Kazakhstan reach 17 billion tons.

Major oil reserves in Kazakhstan (90%) are concentrated in the 15 largest oil fields, which are Tengiz, Kashagan, Karachi-Hanák, Uzen, Zhetybai, Janajol, Kalamkas, Kenkiyak, Karazhanbas, Kumkol, North Buzachi, Alibekmola, Central and Eastern Prorva, Kenbai, Korolevskoye.

Kazakhstan exports more than 87% of its produced oil. The main export routes are the following: The Atyrau – Samara pipeline, the Caspian Pipeline Consortium (CPC), the Atasu – Alashankou pipeline, the port of Aktau.

The largest volume of Kazakhstan oil is exported via the CPC pipeline and the Atyrau – Samara pipeline through Russia and South Caucasus to Europe. Kazakh oil export to China is rapidly growing and now accounts for 15% of the total volume of Kazakh oil exports.

Natural gas production and exports are rapidly growing in Kazakhstan, mainly due to the development of new and existing major fields such as Karachaganak, Tengiz, Janajol, Tolkyn. In just a few years, the share of Kazakhstani gas in the total volume of pipeline gas supplies in Eurasia has increased from 0 to 2.3% in 2011[1] and continues to steadily grow[2].

As well as this, Kazakhstan plays an important role as a transit country. In 2010 the volume of international gas transit through Kazakhstan exceeded 82 billion m^3 (including Russian gas - 55.2 m^3, Turkmenian - 10.8 m^3; Uzbek - 11.7 billion m^3) (Ministry of Energy of the Republic of Kazakhstan, 2017).

Coal remains an important energy source for Kazakhstan. With significant proven coal reserves of all grades, which account

1 For comparison: Russian share in total pipeline gas exports in Eurasia is 40%.

2 Until 2007 Kazakhstan was not a gas exporter and imported gas from Uzbekistan (for its southern regions) and from Russia (for northern regions).

for 3.5% of world reserves and more than 11% of Eurasian coal reserves, Kazakhstan is an important coal supplier to the world market, and primarily to the markets of neighboring countries such as Russia, China and European countries.

Uranium is a strategically important export resource of Kazakhstan (primary for Russia). Kazakhstan has almost 20% of the world's resources of this strategic raw material, which is necessary for nuclear power operation. In addition, Kazakhstan has ranked world's first in terms of natural uranium production since 2009. Given the expected growth of nuclear power in the world and the depletion of uranium resources in a number of countries with developed nuclear power the role of Kazakhstan as one of the leading uranium suppliers will increase.

Due to the common electric power infrastructure between Russia and neighboring Central Asian countries, Kazakhstan is actively involved in interstate energy flows by actively purchasing electric power from Russia for its northern regions and from Kyrgyzstan for the southern parts. At the same time Kazakhstan itself also supplies electricity to its neighbors in almost equivalent amounts (2.6-2.8 billion kW/h, which equals to 3% of the total electricity production in the country).

Belarus has no significant energy resources. Its needs in oil and gas are covered at almost 100% by imports, mainly from Russia.

However, Belarus is a key transit country for oil and gas export from Russia, Kazakhstan and other Central Asian countries to Europe.

3. PERSPECTIVES AND RISKS OF THE EURASIAN ENERGY INTEGRATION

Up to date, the main problems in creating a single oil and gas market within the CU and common economic space are the following:

1. Effective transit potential use;
2. The common energy mix creation;
3. Development and adoption of common rules for oil and gas industry access;
4. Duties abolition and common tariff policy;
5. Petroleum products protectionist measures removal;
6. Single information field for all market participants;
7. Unification of rules and standards for oil, petroleum products and gas through adoption of technical regulations;
8. National energy legislation harmonization.

The current regulating system of hydrocarbon supplies within the CU is described hereafter. Russia supplies oil to Belarus duty-free under the quota. The oil products, exported from Belarus should be subject to duties which go to the Russian budget. On the contrary, Kazakhstan supplies oil to Russia, export duties remain in the Russian budget in return for duty-free oil products supplies to Kazakhstan. In the coming years, the majority of questions on the restrictions removal and the oil products export duties reduction are to be agreed.

On the other hand, there is an open issue with Belarus which is constrained by the compensation prices received for duty-free hydrocarbon supplies from Russia and Kazakhstan. The fact that the date of common oil and gas market creation with the CU was shifted caused disappointment and critical remarks by its president, who said that the integration became "the process for the sake of the process" and "the CU should be full-scale, without any restrictions, including the sphere of energy" (President of the Republic of Belarus, 2014). As a result, all the restrictions on the Russian goods supplies for Belarus, primarily oil, should be removed before the creation of the Eurasian Economic Union in 2015. According to the estimates of local experts, the negotiations will be difficult and will be agreed until the very last moment. Otherwise, the losses for Russian budget can reach up to 30 billion dollars per year. As the treaty on the Eurasian Economic Union was signed on 29th of May 2014, it was decided to postpone the implementation of duty-free energy trade with Belarus to 2016. The parties also adopted the agreement stating that next year 1.5 billion dollars previously transferred by Belarus to the Russian budget as petroleum products sales taxes would remain in the budget of Belarus, and the Belorussian gold reserves will receive a loan of 2 billion dollars. Thus such large money infusions into Belarusian economy are incomparable with the equivalent return for Russia which is less important and less expensive than the Eurasian Union maintenance costs.

As for the oil and gas duty-free trade between Russia and Kazakhstan, it can be noted that the parties have already reached the agreement on oil swap deals in 2014. Russian oil companies assume the obligation to export duty-free up to 1.5 million petroleum products to Kazakhstan, and Kazakhstan shall be obliged to export crude oil to China on behalf of Russia. However, there is still a difficult issue for petroleum products duty-free trade which is very often subject to the protectionist measures aimed at protecting the local monopoly in the domestic market.

The fact is that due to the duty-free petroleum products supplies to Kazakhstan Russia is annually short of about 700 million dollars from its budget. This year, there were negotiations between Russia and Kazakhstan on the issue of the potential scheme implementation according to which Kazakhstan supplies oil to Russia in exchange for oil products. The oil goes for export, and the export duty received covers the losses of Russian budget from the duty-free supply of petroleum products. However, this scheme was not implemented as the agreement on oil price had not been reached.

4. CONCLUSION

Thus the ongoing integration of the CU and SES countries in the energy sector will increase the need for coherent policy aimed at increasing energy efficiency and the unified infrastructural development strategy creation of the CU economies.

Among the directions within the CU and SES which Russia should focus on, it is possible to identify the following:

1. Creation of the common energy export diversification strategy with Central Asian countries;

2. Use of the Russian transit advantages and competitiveness by actively promoting the CU and SES transcontinental projects;
3. Establishment of the CU and SES countries' transnational companies at the certain stage of economic integration or the international production cooperation, legal restrictions elimination in the CU countries which deter competition and restrict the arrival of foreign companies in the strategic industries;
4. Transport infrastructure in the Eurasian space;
5. Increased presence of Russian energy resources, energy equipment and technologies on the CU and SES markets;
6. Participation of Russian investments for oil fields development in the CU countries, as well as participation of Russian businesses in the fuel and energy facilities privatization process.

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