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A Strategic Challenge: The role of Greece in Europe's Southern Gas Corridor Strategy

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A Strategic Challenge:

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by

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Table of Contents

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A Strategic Challenge: The role of Greece in Europe's Southern Gas Corridor Strategy

Executive Summary

The question of European energy security has brought attention to the strategic significance of Southeastern Europe as a transport hub of natural gas and a key region for European energy security. To meet increasing natural gas demand and reduce energy dependency on Russia, European authorities need to promote the realization of projects contributing to the diversification of natural gas supply, alongside improving Europe's relationship with Russia by diversifying its import routes, two targets which are not necessarily mutually exclusive.

The principal targets of this study are (a) to illustrate the major geopolitical parameters of the European Union's Southern Gas Corridor Strategy which aspires to diversify the Union's natural gas import sources while strengthening the political and economic independence of hydrocarbon-rich former Soviet States (b) to present the general framework and key strategic objectives of Greek foreign policy, and the role Greece's energy policies are expected to play and (c) to evaluate through a strategic lens Europe's options for the Southern Gas Corridor.

Europe's Southern Gas Corridor Strategy is founded on the necessity to maximize the imports of non-Russian gas via non-Russian controlled territory, so as to establish an additional route of supply diversification. Any meaningful discussion on the feasibility of the three remaining Southern Gas Corridor Strategy pipeline projects, namely Nabucco, BP's South East Europe Pipeline (SEEP) and Trans-Adriatic Pipeline (TAP) that vie for the transportation of (initially) Azeri gas to Europe via Turkey, requires an examination of the geopolitical environment which will –to a large extent- determine their eventual implementation.

The study analyzes the geopolitical rationale behind Europe's Southern Gas Corridor Strategy by focusing on the reasons which have led to the weakening of the rather "pharaonic" Nabucco pipeline project compared to its two smaller and more cost-efficient (even when taking into consideration the scaled-down version presented in the last few days by the Nabucco consortium) competitors TAP and ITGI. Understanding why Nabucco has lost significant ground is crucial for securing Greece's role in the Southern Gas Corridor. A special reference is also made to BP's SEEP project, a rather nebulous latecomer in the Shah Deniz-II race and the way its implementation may influence Greek policy and interests. The study then evaluates the likely impact of each project's implementation on Greece's foreign policy.

Main conclusions

Greek foreign policy makers will function, at least for the near future, under the Damocles sword of the country's economic crisis. This imposes a number of constraints and limitations. In addition, as key organizations such as the EU and NATO are changing in an effort to adapt to new global and regional trends, Greece needs to find its own niche in the distribution of regional roles and convince its partners and allies of its own added value in common endeavours. A difficult task, indeed, for a country with limited resources but the alternative is strategic irrelevance in the wider region. The best option would probably be Greece's active participation to the shaping of the EU's new regional policies, without, however, ignoring the need for national initiatives or the further multilateralization of Greece's foreign policy.

While maintaining and even further emphasizing its European orientation, there is no reason why Greece cannot develop its relations with other major powers, including the US and Russia. Past tensions between Washington and Moscow made it difficult –and politically costly- for countries like Greece to cooperate with Russia on areas of common interest (like energy). The 'reset' in U.S.-Russian relations would probably allow Greece more leeway for energy cooperation with Russia.

As mentioned in various parts of the study, ***energy-related projects can be instrumental in Greece's effort to repair its image, re-acquire a leading regional role, increase its influence and accumulate 'diplomatic capital'. In this context, the Southern Gas Corridor can play an important role. Unfortunately for Athens the decision for the pipeline route was not taken by Greece. Despite Greece's initial preference for ITGI, once Shah-Deniz decided in favour of TAP the Greek government must immediately***

embrace the project and facilitate its completion at the earliest possible time [and, of course, under the best possible conditions for Greek interests]. Otherwise, the final decision of Shah-Deniz will be in favour of either Nabucco or SEEP. To prevent such a development, an active diplomatic effort, on the basis of close coordination and cooperation between the Ministries of Foreign Affairs and Energy & Environment should be undertaken by Greece.

It should be mentioned that TAP will be crossing Albania before reaching its final destination (Italy), which raises some questions because of various outstanding issues between Greece and Albania which need to be resolved. Although it would be a mistake to underestimate bilateral problems, it would also be wrong to underestimate the common interests and the potential for bilateral cooperation as Albania is, for a number of reasons, an important neighbour and partner for Greece. The potential benefits of cooperation should also be understood and appreciated in Albania, as well.

If TAP wins the SD2 tender, it should seriously consider the inclusion of a Greek private or state gas company/entity as a partner. Greece should also use the IGB network to Hungary as a means of accelerating the transfer of Arab, Cypriot or Israeli LNG to these states regardless of the competition between TAP, SEEP and Nabucco. These LNG sources, especially the Arab/Qatari one, would be available once IGB is commissioned, circa 2013, and thereby eliminate the commercial underpinning of the SEEP project that in its current form appears to be completely disregarding Greek interests.

In addition to the Southern Gas Corridor, ***Greece should try to enlarge its footprint in the energy map through other projects, including South Stream, Burgas-Alexandroupolis[1], as well as the exploitation of potential oil and gas deposits in various parts of the country, notably in Western Greece and the maritime areas to the south of Crete.*** While Greece should continue and intensify its diplomatic efforts for the delimitation of its exclusive economic zone (EEZ) and other maritime zones with neighboring countries, this should not unduly delay efforts to exploit natural resources in the aforementioned areas.

Finally, if technological and financial conditions allow, Greece could also benefit through the construction of a pipeline to transport natural gas from the Israeli and Cypriot deposits in the Eastern Mediterranean through Greece to Western European markets. Such a pipeline project, as well as a Liquid Natural Gas (LNG) alternative, would make an even larger contribution to European Energy security, especially if combined with prospective Greek hydrocarbons production. ***In a very difficult period for Greece, such energy projects provide an excellent opportunity for diplomatic and economic benefits.***

[1] *As a result of the recent [December 2011] decision by the Bulgarian government, the proposed Burgas-Alexandroupolis oil pipeline may not be constructed, although Russian sources claim that the project is only temporarily "frozen", a position Greece would obviously welcome.*

Introduction: Study purpose and scope

According to the projections of the International Energy Agency (IEA), the European market demand will increase on an annual rate of 2.4 percent and reach 630 billion cubic metres (bcm) annually in 2030. Meeting this demand becomes a difficult task especially if it is to be reconciled with the projected plateau and eventual depletion of Norwegian natural gas over the next two decades. In addition, the crises of January 2006 and – more importantly the crisis of January 2009- between Russia and Ukraine, when a dispute over the price of natural gas led to the interruption of Russian gas supplies to Central and Southeastern Europe, worked as an eye-opener for many policy analysts and media. European energy dependency on Russia was highlighted, and the need to take measures to reduce it became pronounced. As the Russian Federation is already providing approximately 25 percent of natural gas consumption in Europe, the European market will need to find additional quantities of natural gas from alternative sources and via alternative routes.

The question of European energy security has brought attention to the strategic significance of Southeastern Europe as a transport hub of natural gas and a key region for European energy security. To meet increasing natural gas demand and reduce energy dependency on Russia, European authorities need to promote the realization of projects contributing to the diversification of natural gas supply, alongside improving Europe's relationship with Russia by diversifying its import routes, two targets which are not necessarily mutually exclusive.

Understanding the way through which the implementation of the Southern Gas Corridor Strategy will help stabilize or destabilize the regional balance of power in the Greater Black Sea Area is one part of the equation, as both endogenous (Russia, Azerbaijan, Georgia, Turkey, Armenia, Turkmenistan, Ukraine and Iran) and exogenous (EU, U.S., China, Bulgaria, Greece, Romania, Albania) players will recalibrate their strategies accordingly in order to adjust to and influence the potential success or failure of the EU Strategy. The other side of the equation though is to understand the way through which existing "flash points" are likely to affect the success not only of the Southern Gas Corridor Strategy as a whole but of every individual project that composes its most immediate phase, namely, the Nabucco, SEEP, ITGI and TAP projects. In other words, the other side of the equation is to understand the political risk component of the aforementioned projects without overlooking their comparative commercial and technical advantages and disadvantages.

The principal targets of this study are (a) to illustrate the major geopolitical parameters of the European Union's Southern Gas Corridor Strategy which aspires to diversify the Union's natural gas import sources while strengthening the political and economic independence of hydrocarbon-rich former Soviet States and (b) to present the general framework and key strategic objectives of Greek foreign policy, and the role Greece's energy policies are expected to play. In this context, special emphasis will be given to the current state of affairs as well as future prospects for relations between Greece and Albania, as one of the options for the Southern Corridor would involve that country as well. Policy options in the energy field have a geostrategic dimension, in addition to the technical and financial ones. In most cases, there is a complex relationship between foreign and energy policies and Greece is not an exception. Its membership of the EU, bilateral relations with Russia, the US, Turkey, Azerbaijan, Albania, Israel and other countries influence Greece's energy options.

2.Greek Foreign Policy In The Shadow Of The Economic Crisis

2.1. An overview

Greece is located near the crossroads of three continents (Europe, Asia and Africa). According to a RAND Corporation study, Greek strategic space is wide, encompassing Europe, Eurasia, the Middle East and the Mediterranean, as well as transatlantic relations. Greece is an integral part of the Balkans (where it was for a long time the sole member of both the European Union and NATO and still maintains a position of political and economic influence, despite its current economic crisis) and is also in close proximity to the Black Sea. The Aegean Sea is an important shipping route, connecting the Black Sea with the Mediterranean, and a major transit route for the transportation of energy products. The Mediterranean has historically been a body of water of considerable value for Greece, as well as a region endowed with special significance, either as a familiar route of trade and culture, or a fault line between hostile states and civilizations. In the post-Cold War era, the Greek strategic space is a crucial area of contact between the North (a region of stability and affluence) and the South (a region characterized by multiple flashpoints, areas of tension and unequal distribution of wealth).

Looking at the evolution of Greek foreign policy in the period after the country joined the EU, one would notice a general change. In the 1980s, the perception of many western governments and foreign analysts was that "reactionary" policies, unreliability and unpredictability were the dominant characteristics of Greek foreign policy. In the 1990s and early 21st century the pattern has been of a more pragmatic, reliable, rational, multidimensional foreign policy, placing emphasis on multilateral diplomacy (although at different degrees by various Greek governments). One may discern a number of causes for this change but there should be little doubt that this is mainly due to the influence and the impact of the deep "Europeanization" process that has shaped various facets of Greek political, economic and social life and led to an enhancement of Greece's credibility as an international actor.

Although the focus is on the domestic front and the economic crisis has clearly overshadowed foreign policy issues, there is an understanding among policy makers that the 'world keeps turning' and Greece's wider neighborhood continues to change and that the country should strive to maintain most of its regional influence and even seek a new role, both through national means, but also in the context of its membership in the EU (and secondarily NATO). There is also a gradual realization that Greece has regional interests that go well beyond its immediate northern neighbourhood and its regional policies vis-à-vis the South and the East should evolve according to global and regional developments. Although Greek economic and political interests in South-eastern Europe and relations with Turkey will continue to be Greece's top foreign policy priorities, the Mediterranean/Middle East will be a region of growing importance, either at the regional (as, for example, Greek companies will be looking for ways and markets to increase their exports to compensate for the reduction of domestic purchasing capacity as a result of the economic crisis) or the transatlantic context. Greece has the relative luxury of staying in the "sidelines" of transatlantic and Mediterranean chessboards (paying, of course, a price in terms of its regional role, influence and exploitation of political and economic opportunities); or it may choose to play a more active role in a region where instability, fluidity and unpredictability are likely to remain standard features for the foreseeable future, and thus strengthen its "value" to allies and neighbours.

In this context, of potential interest might be Greece's recent geostrategic re-positioning closer to the US-Israeli partnership in a region where there is in fact no other country that is both a reliable partner for Washington and Tel-Aviv and an acceptable interlocutor to Muslim countries. Such an active role will be a difficult task, indeed, for a country with limited resources but the alternative is strategic irrelevance in the wider region. The best option would probably be Greece's active participation to the shaping of the new EU and transatlantic regional policies, without, however, ignoring the need for national initiatives or the further multilateralization of Greece's foreign policy, within, the general Euro-Atlantic framework. The key concept will be the smart use of its –rather limited- national capabilities. In this context, a number of thematic areas

like energy and maritime security may provide opportunities for Greece. A quick tour d' horizon might be helpful in understanding Greek foreign policy objectives and how these may be achieved through the exploitation of opportunities, especially in the field of energy.

Greek-Turkish relations remain, of course, at the top of Greek foreign policy agenda. Greece has moved away from zero-sum game perceptions vis-à-vis Turkey and overall, the two countries are much better off today in terms of bilateral relations (including trade and people-to-people contacts) than they were a few years ago [before 1999 to be more precise]. Having said that, neither country has moved from their firm positions regarding 'high politics' issues and Greece and Turkey continue to perceive each other through a Hobbesian prism. Greek policy-makers are moving away from "zero-sum game" perceptions regarding Greek-Turkish relations, but scepticism and distrust continue to linger. Despite rumours about substantial progress in the exploratory talks, it seems unlikely that there will be an agreement in the near future. It would be wiser if both sides explored ideas for confidence-building measures regarding overflights, violations and dogfights. Among 'success stories' in Greek-Turkish relations, reference should be made to the very dynamic 'citizen's diplomacy', increased trade and energy cooperation (through the construction of the Interconnector Turkey-Greece (ITG) transporting Azeri natural gas to Greece through Turkey, with Italy being the final destination).

Regarding AKP's "zero problems with the neighbours" policy and Turkey's new and quite ambitious foreign policy, there is considerable interest in Athens, mixed with some degree of concern, about the upgrade of Turkey's regional role over the past few years and its implications for Greek-Turkish relations (especially in the context of so-called "Neo-Ottoman" ambitions). Some of the questions debated by the Greek foreign policy establishment include whether Turkey has been transforming itself into an 'Islamic-lite' country, whether its regional policies are compatible with transatlantic interests and whether it is drifting away from the West. The majority of policy-makers persist that it is in the best interests of all sides involved if Turkey remains anchored to Western institutions, although full EU membership remains a distant possibility.

Southeastern Europe and the Black Sea remain regions of very high importance for Greece which needs to return to its economic backyard (or front yard). There are limited expectations, however, for any spectacular developments on the dispute with FYROM. Greece has been quietly improving its relations with Kosovo, but recognition should not be expected in the near future. Finally, there has been a slight deterioration in relations with Albania –due to a significant extent to the domestic situation in that country. This should be a priority issue for Athens to address. Both the issue of Greek-Albanian relations, as well as the evolution of Greece's SEE policies will be examined in greater detail in the next section.

Regarding the role of extra-regional powers, Greece is not in principle uncomfortable with a greater role for Russia and China in the region, provided their presence and activities fulfill the dual criteria of mutual economic benefits and no destabilizing political consequences. China appears to consider Greece as a regional hub for increasing its economic (and perhaps in the future political) footprint in southeastern and central Europe and the current economic crisis cannot but increase the attractiveness of such a prospect for Athens. Chinese companies have invested in the Port of Piraeus, with a promise for additional investment and Greece is hardly in a position to discourage FDI of almost any legitimate origin. As long as China's Mediterranean presence remains basically economic and is not causing any friction with Greece's western partners, Athens will not be faced with difficult dilemmas.

In the case of Russia, there are historical ties as well as current common interests and the two countries have been exploring various schemes for energy cooperation (it should be noted that Greece is heavily dependent on Russia for its oil [46% of total imports in 2010] and natural gas [around 60% of total imports in 2010] needs). Furthermore, Russia has always maintained excellent economic and political relations with Cyprus. Thanks to the recent improvement of relations between the West and Russia (after the Lisbon NATO summit), the related dilemmas for Greek foreign policy appear much more manageable.

Two functional issues are also of great importance for Greek foreign (and domestic) policy. The first is migratory movements from Asia and Africa that constitute a cause for strong concern for Greece –in this context, the "first line of defence" for Europe-, as the Dublin II Agreement creates an obligation for the country

of first arrival to the EU to not allow illegal immigrants to travel to other EU countries. Greece is trying to deal with the problem with a package of measures including a more efficient asylum mechanism, employment of FRONTEX assets in the Aegean and its land border with Turkey, as well as the construction of a security wall in a 12.5 km-long section of that border. Recent developments in North Africa and the increasing number of refugees and illegal immigrants –mainly to Italy- have led to a renewed debate about the revision of the EU's immigration policy.

The second issue of rapidly increasing importance is that of energy. Despite the problems with the Burgas-Alexandroupolis oil pipeline, Greece will continue its efforts to enlarge its foothold in the energy map. Although it is participating in the implementation of the South Stream project-as it is explained in the main body of this study- the immediate priority is the Southern Corridor, where three [formerly four] alternative pipeline projects are competing. Additionally, exploration for national deposits of hydrocarbons will accelerate and foreign companies have already expressed their interest in this context. Greece's rich potential in renewable sources of energy have also been attracting the interest of potential investors, especially in the case of solar power energy as it is illustrated by the project Helios.

Another quite promising field of energy cooperation, where Greece may be a potential player, is the maritime region between Cyprus and Israel. Apparently substantial deposits of natural gas have been discovered inside the exclusive economic zones of Israel and Cyprus and the two countries have been considering various forms of cooperation. One option would be the construction of a terminal for liquefied natural gas in Cyprus and then transportation to Western Europe, which remains strongly interested in alternative energy suppliers in order to reduce its dependency from Russia and the other option –more expensive and technically challenging- would be the construction of an underwater pipeline to Greece and then, perhaps through the Southern Corridor pipeline, to Italy.

2.2 Greece's Southeast European (SEE) policy

Greece's energy prospects and options cannot be fully understood without a presentation of Greek policies vis-à-vis Southeastern Europe (SEE), as both the Southern Corridor, but also the South Stream, have a strong regional dimension. The two decades after the end of the communist regimes in SEE have brought turbulence and policy dilemmas which have enormously challenged the Greek elites and society. In this brief overview of the post-Cold War era period one can identify four different periods defined by the different SEE challenges and/or the different responses by the Greek foreign policy, which will be briefly outlined together with their main characteristics and milestones, with a final section on the current state of Greece's SEE (the term is used interchangeably with the term Balkans) affairs.

2.2.1. Periods of Greece's SEE policy

1. Post-communist transition and Greek maladaptation phase: the first half of the 1990s is characterised by radical changes in the Balkan geopolitical map. The collapse of the communist regimes brought about a revolutionary political, economic and social change in the Balkan countries. This transition was largely peaceful with the most dramatic events initially taking place in Romania. But the seismic events came only shortly afterwards when the Yugoslav Federation violently collapsed. The Yugoslav space became the locus of violent wars for a decade (1991-2001) with the most tragic events taking place in Croatia, Bosnia-Herzegovina and Kosovo.

   This period presented Greece with many opportunities for a positive contribution to the regional developments and increase in its influence. Greece had a stable parliamentary democracy, a healthier market economy, incomparable higher standards of living, and, above all, was the only

Balkan country that was a full member of both EU and NATO, the two organisations that the newly democratised countries aspired to join. Despite Greek aspirations for a new leading role in the Balkans, Greece failed to take advantage of the new situation and instead of contributing to regional stability soon found itself embroiled in new bilateral disputes with neighbouring Balkan countries. Instead of quickly resolving minor problems with its neighbours, Greece entered squabbles with FYROM, over the use of name 'Macedonia', and Albania, over the rights of the Greek minority and the Albanian migration in Greece. Adopting maximalist positions and more often than not influenced by populist media, the public opinion and nationalist circles the Greek foreign policy allowed these minor disputes to fester and consolidate. Thus, Greece was forced to invest political capital in disputes that were not of vital importance for Greek security and could have been resolved to the mutual benefit of the parties involved. More importantly, Greece failed to play the important political and economic role in the region that the position in the Balkan regional system entailed. Instead of being the power broker for the West in the Balkans Greece soon 'gained' in the West the reputation of yet another troublemaker in the region; Greece's Western partners were often enraged to see that Greece instead of helping its neighbours in their difficult transitions it was playing power games for its own benefit.

The rather negative reputation that Greece acquired was also linked to what was seen in the West as an informal alliance or support to Serbia. The latter soon after the start of the Yugoslav wars acquired the image of an aggressive nationalist power that masterminded the Balkan bloodbath that shocked the whole world. Much more could be mentioned about that early post-communist period. It will suffice here to mention that the above-described problematic Greek policy in SEE, and its associated malaise such as the support for Serbia or the dead-end maximalism on the Macedonian question, was produced and reinforced by the confluence on the one hand of a defensive reading of the post-communist developments and mistaken policy choices on the part of the political system and on the other on the stereotypical, populist and often outright nationalist reflexes of the Greek society and some of its important opinion makers (Orthodox Church, media, intellectuals etc.). This early post-communist period was plagued by popular mobilisation and protesting for foreign policy issues, nationalist public discourse, populist media frenzy, outlandish conspiracy theories by influential public figures and several other features that made pragmatic and rational policy making very complicated at the detriment of Greece's true national interests.

2. Softening phase: the subsequent period was characterised by a relative softening of the Greek maximalist positions as well as of those policies that have made Greece unpopular in the West. Without really a genuine change of heart or mindset Greek politicians after 1995 softened their stance on a number of issues mainly as a result of the rational calculation of the effects of the earlier policies. Key among these changes in this period was the Interim Accord of September 1995 when Greece and FYROM found a modus vivendi and a framework for trying to resolve the bilateral dispute without further endangering the transition to statehood and democracy of this newly independent state. Greece has also tried to find some understanding with Albania, especially after 1997 elections and the change of guard in Tirana. Finally, Greece tried to somewhat distance itself from Serbia, which had become a complete outcast due to the horrors of the Bosnian war.
3. Foreign policy shift phase: this period coincides with the change of leadership in the ruling socialist party (PASOK) and the attempts by the new government under Simitis for a more pragmatic foreign policy. The great innovation of this period was the fresh approach in the relations with Turkey, which is a far more important foreign policy concern for Greece compared to the Balkan disputes. The new government attempted to bring a more Western-oriented and rational approach in its SEE policy, often finding itself at odds with the public opinion and influential opinion makers in Greece. The characteristic example of this was the Greek position during the Kosovo war and NATO's military intervention against Serbia.

4. Europeanisation phase: the previous phase was the transition period to a more comprehensive approach on the Balkan affairs which advanced a 'European solution' to the region's problems. The new Greek policy viewed the bilateral disputes with the Balkan neighbours as part of the wider solutions that will be achieved through the process of integrating the entire region in the Western institutions. This vision was fully compatible with both the Western aims and the Balkan countries' aspirations. In fact, Greece became a strong proponent of the EU and NATO enlargement in the region and the advocate of Balkan states in the West. This was epitomised in the 2003 Thessaloniki summit of the European Council and the agreed-upon Thessaloniki agenda which extended a promise to the Balkan countries for their eventual integration in the European Union as well as created a roadmap for the integration process. Not long after the Thessaloniki summit three Balkan countries, Slovenia first and then Romania and Bulgaria joined the EU, the latter two having a significant backing from Greece.

It is characteristic of this new approach in the Balkan affairs that successive Greek governments have been negotiating with Skopje under UN auspices for reaching an agreement on the 'name dispute' on the basis of a composite name that will include the term 'Macedonia'. This is a clear as much as significant departure from the official Greek position of the 1990s when any use of the term 'Macedonia' by FYROM was considered unacceptable. In fact, partly due to the more compromising position of Greece and partly due to the adoption of nationalist rhetoric in Skopje, Western partners seem more receptive to Greek arguments on the dispute. Several initiatives beyond the Thessaloniki agenda also contributed to the new Balkan policy. Among these, the Greek Plan for the Economic Reconstruction of the Balkans (GPERB), an ambitious plan for extending 550 million euro for bilateral aid to Balkan countries (Albania, Bosnia-Herzegovina, Bulgaria, FYROM, Montenegro, Romania, Serbia and Kosovo) was initiated in 2002. The plan was not without its difficulties resulting from the inadequacies of the Greek public administration and the economic downturn of the Greek economy. In addition, it seemed to reflect the earlier special connection to Serbia, for which about 43 per cent of the funds were earmarked even though it represents only about 15 per cent of the Balkan countries' population. But despite the difficulties the GPERB signalled a confident new approach in the manner that the Balkan countries seen by Greece.

More recently, the Greek government's initiative 'Agenda 2014' aims to rejuvenate the EU enlargement process in a period of significant political and economic problems and European 'enlargement fatigue'. The Greek diplomacy's goal to convince that a fresh push for the Western Balkans' accession process is needed in order for the region's EU aspirants to find new faith in their realistic prospects of joining the European club. Last but not least, one has to stress here the 'world apart' of the Greek investment in the Balkans. Greek businesses continue to have an important role in most Balkan economies and have managed to consolidate their position in the local markets and start reaping the fruits of their investment. The benefits of this healthy Greek investment in the Balkans have become even more important as the effects of the Greek economic crisis have started to have a heavy bearing on the private sector in Greece.

What comes next?

The above analysis begs the question of what comes next, especially having in mind the serious troubles Greece finds itself in these days. One is tempted to ask, what is left of the Greek influence in the Balkans after the Greek crisis? Although it would be risky to make any predictions it seems likely that Greece's position in the region will be weakened. The key reason is no other than the serious economic crisis reduces the material leverage of Greece but also weakens the appeal of the country. It is not without significance that Greece sees a reversal of the migration wave from Balkan countries, after being for years a favourite destination for workers from SEE. Greek investment in SEE remains in place for now but a rolling back, especially in the banking sector

cannot be excluded. Needless to say, much will depend on the seriousness and longevity of the Greek recession and economic crisis.

But other reasons may also contribute to the weakening Greek position in the region. Turkey's new foreign policy has also a Balkan dimension. The country's return to the Balkans with a newly acquired confidence that was not in place in the 1990s. This return can be seen at the political, economic and cultural level. And, in contrast to its practice in the 1990s, it does seem to include also countries not traditionally among its orbit of diplomatic influence, such as Serbia. This is not necessarily negative for Greece but it is indicative of the changed geopolitics in the Balkans, in which Greece does not seem to be at the forefront. In addition, the lasting bilateral disputes of Greece still create problems. Greece finds more understanding on the 'name dispute' among its partners but there is not much willingness for compromise in Skopje. The momentum for the resolution of the dispute seems to have floated away several years ago.

Above all, the Balkan environment is today very different from that of the early 1990s. Greece cannot anymore claim the role of the sole Western broker in the region. Not only because of the economic crisis but also because other countries partake the same Western institutions and have aspirations for a Balkan role: Austria, Slovenia, Romania, Bulgaria, even Croatia. And Greece on its part, is still not fully in agreement with all Western policies in the Balkans (e.g. Kosovo independence, FYROM's NATO accession) and also seems to preoccupied with its own troubles to develop confident new activism in the Balkans.

2.2.2. The troubled relationship between Greece and Albania

Since one of the options (TAP) for the Southern Corridor would go through both Greece and Albania, it would be important to examine bilateral relations between Athens and Tirana in order to determine whether this would be an obstacle, a complicating factor, or none of the above with regards to the potential realization of this pipeline project. In the early post-communist period Albania was undergoing a very difficult transition. The migration of thousands of Albanians to Greece relieved some of the transition pains by reducing unemployment and helping the economic recovery through their annual remittances. Additionally, as Greece was at the time the only Balkan country that was a member of both the European Union (EU) and the North Atlantic Treaty Organization (NATO), Greek political support was important for Albania's integration into the Western institutions. And most importantly, the danger of the Yugoslav conflict moving to Albanian inhabited territories required that Tirana maintained good relations with neighboring countries, and especially with Greece.

Key issues in Greek-Albanian relations include [for Greece] the political, human, educational and cultural rights of the Greek community in Albania and the delimitation of maritime borders between the two countries and [for Albania] the property rights of the Cham population, who were expelled from Greece to Albania after the Second World War (after being accused of collaborating with the German occupation forces) and the economic and social rights of Albanian immigrants in Greece.

At the heart of the periodic tensions between Athens and Tirana is often the treatment of the ethnic Greek community in southern Albania. The safeguarding of the Greek minority rights in Albania constitutes a significant foreign policy objective of Greece and Greek officials have repeatedly conditioned the improvement of bilateral relations on the respect of these minority rights.

The official Greek position on the Cham question is that it is a non-issue since it has been dealt with during the 20th century through legal provisions and according to the Greek Constitution. According to the Greek view, the Albanian Chams of Greek Epirus collaborated with the Nazi occupying forces during the Second World War. Many were executed or expelled by the Greek resistance, while their fate was sealed after the end of the occupation when they were tried as Nazi collaborators and found guilty of treason, their properties were confiscated and their citizenship revoked. Another group of people that has been a source of periodic tension between Greece and Albania is that of Albanian immigrants to Greece. Taking advantage of the newly-found freedom of movement following the collapse of communist regime in 1991, a large number of Albanians crossed the porous Greek-Albanian frontier in search for employment and a better life. It is estimated that

approximately 600,000 Albanians currently live in Greece, making up two-thirds of the total number of immigrants in the country. The situation of the Albanian immigrants in Greece has in recent years improved. Since many of these people consider Greece their adopted country, they constitute a significant tie binding the two countries.

In 2009 Greece and Albania signed an agreement to delineate the continental shelf and maritime borders in the Ionian Sea. The agreement signed by Greek Prime Minister Costas Karamanlis and his Albanian counterpart Sali Berisha created a stir of controversy in the Albanian media, especially those supporting the Socialist opposition, which accused the Albanian government of 'giving' 225 square kilometers of its territorial waters of its southern neighbour. The media accused Berisha and the Ministry of Defence of not delineating the continental shelf according to the equidistance principle of the UN Convention of the Law of the Sea (UNCLOS) on which the agreement was based. The opposition Socialist Party contested the accord arguing that the deal lacks transparency and damages Albania's sovereignty. In the end, the Albanian constitutional court annulled the agreement between Tirana and Athens specifying procedural and substantial violations of the Albanian constitution and the UNCLOS. The Albanian government accepted the decision declaring that new negotiations will start with Greece. The leader of the Socialist Movement for Integration and former Foreign Minister, Ilir Meta, accused unnamed extremist circles in Albanian politics for bringing down the agreement with Greece. This incident caused substantial annoyance in Athens and has complicated bilateral relations.

One paradox is that while the Greek-Albanian relationship is marked by periodical tensions over Albania's treatment of the Greek minority and Greece's treatment of Albanian migrant workers business relations between the two countries remain at a very good level. The economic cooperation between Greece and Albania is especially important for the Albanian government and has not been significantly affected by past political tensions. Greece is Albania's main foreign investor, controlling almost 27 per cent of total foreign investments and ranked first in terms of invested capital, which exceeds $800 million. There are almost 270 Greek, or Greek-controlled enterprises in Albania. Greek investment has focused primarily on industrial and consumer products in which there is now significant domestic production. The major Greek investments are in the following areas: telecommunications, commercial banking, constructions, oil and oil products, trading and distribution, food processing, textile and footwear manufacturing. Greek-interest businesses in Albania include the ever-expanding banks – National, Emporiki, the subsidiary of Piraeus Tirana Bank and Alpha – and the mobile operators Albanian Mobile Communications (controlled by Greece's Cosmote) and Vodafone (controlled by Vodafone Greece). Greek banks such as Alpha Bank, National and Emporiki command substantial market shares in term of loans, deposits and profitability.

3. Assessing the Southern Corridor: A Geopolitical Evaluation of the Nabucco, ITGI and Trans-Adriatic Pipeline Projects

Europe's Southern Gas Corridor Strategy is founded on the necessity to maximize the imports of non-Russian gas via non-Russian controlled territory, so as to establish a third, following Russia, Norway and Northern Africa (Algeria, Libya, Egypt), route of supply diversification. The European Commission has recognized as potential sources of supply for the Southern Gas Corridor not only Caspian (Azerbaijan) & Central Asian (Uzbekistan, Kazakhstan and primarily Turkmenistan) but also Middle Eastern gas from Iraq's future production as well as from potential expansion of Egyptian net exports.[2] Any meaningful discussion on the feasibility of the three main Southern Gas Corridor Strategy pipeline projects, namely Nabucco, Italy-Turkey-Greece Interconnector (ITGI) and Trans-Adriatic Pipeline (TAP) that vie for the transportation of (initially) Azeri gas to Europe via Turkey, requires an examination of the geopolitical environment which will –to a large extent-determine their eventual implementation. The examination of the geopolitical underpinning of these multi-billion dollar projects and the way their implementation is likely to affect the regional balance of power is important for three principal reasons:

i. the region these pipelines will have to cross in order to connect the upstream producer(s) (Azerbaijan, Iraq, Turkmenistan) and the main transit states (Georgia and Turkey) with their final consumers in South East & Central Europe is endemically unstable. This endemic instability not only relates to the possibility of disrupting the flow of natural gas through these pipelines after they are constructed – something that has already occurred in the case of Azeri exports to Turkey during the 2008 Russian-Georgian War[3] but is also directly linked to the ability of *some* of the competing consortia, namely Nabucco, to secure the gas quantities necessary for their financial viability.

   In case Turkey is further destabilized internally by the increasing attacks of the Iraqi-based PKK (Kurdish Workers Party) and its Iranian offspring, the PJAK/PEJAK, then the transit risk for both the ITGI and TAP will also increase significantly. This is not an academic consideration, although it remains a low probability scenario, at least for the time being. Turkey's gas imports from Iran have been disrupted three times in the first nine months of 2011 due to PEJAK/PJAK related attacks which occurred in or emanated from Iranian territory.[4]

ii. The region's net energy exporters attribute to their oil & gas exports an important geopolitical significance. These exports are not only an important financial transaction which accounts for a major component of their respective GDPs and budgetary revenues.[5] They also represent a declaration of diplomatic intent, an attestation of the country's geopolitical orientation and an extension of its foreign policy that in the case of Azerbaijan, the principal (if not the sole arbiter) of the Southern Gas Corridor Strategy, represents, according to Dr. Elhur Soltanov of Azerbaijan's Diplomatic Academy, "a

[2] See inter alia, Spyros Paleoyannis, *The Fourth Gas Corridor Gas Pipelines,* IENE Occasional Paper 10, (July 2009).

[3] The flow of gas continued through the Turkish component of the South Caucasus Gas Pipeline that links Baku and Erzurum via Tbilisi. "BP: Gas Still Flowing on the Turkish Side of the South Caucasus Pipe", *DowJones,* 12/08/2008.

[4] Iranian gas exports to Turkey were interrupted following explosions on the Iranian side of the border on 28 July 2001, 11 August 2011 see, "Iran: Gas Exports to Turkey Stopped After Pipe Explosion", *DowJones,* 28/07/2011, "Gas Flows from Iran to Turkey Resume", *UPI,* 19/08/2011. Iranian exports also decreased following an explosion on the three main Iranian trunk lines (IGAT 1,2,3) which occurred on 11 February 2011 25km to the south of the city of Qom, "NIGC Repairs Three Gas Trunklines After Explosion", *Middle East Economic Survey,* 21/02/2011. It should also be noted that the Iranians have blamed PKK/PEJAK and U.S. and Israel for the alleged bombings of the aforementioned pipelines. According to *Global Security.org* the PEJAK/PJAK is "Party for Free Life in Kurdistan (PJAK, though somewhat more commonly PEJAK) is based in the Kurdish region of Iraq, a few miles from the Iranian border". The PJAK operates "under the PKK's security umbrella, PJAK adopted many of the political ideas and military strategies of the PKK. PEJAK ideology is leftist, and includes equality of the sexes, which is unusual in the region. Though the precise relationship is obscure, as of 2006 they shared many of the same facilities and resources in the Qandil / Kandil Mountains", http://www.globalsecurity.org/military/world/para/pjak.htm

[5] In 2010, oil & gas exports amounted to 90% of Azeri exports that according to the CIA World Fact Book (updated to 12/07/2011) amounted to approximately $28,07 billion compared to a state budget of $28,83 billion in 2010. https://www.cia.gov/library/publications/the-world-factbook/geos/aj.html

means of consolidating its sovereignty".[6] Such an understanding on the part of the exporter state may complicate or further delay the final selection process for reasons that do not necessarily relate with the financial, regulatory and technical viability of the contesting pipeline projects.

iii. The above-mentioned geopolitical notion of energy flows as a means of foreign policy and national empowerment is not exclusive to the producing or exporting states. Several of the aspiring transiting states, namely Georgia, Turkey, Greece, and even Albania, do not want to simply secure stable and affordable natural gas supplies. They want to capitalize diplomatically on the transit of these supplies through their own territory for reasons that go beyond their *immediate energy needs*, which in the case of Albania, i.e., are practically non-existent since the country simply does not consume any meaningful quantities of natural gas.[7]

Of course the level of each country's import diversification and the share of natural gas in its primary energy supply mix constitute the major parameters which will determine the nature of each nation's energy security interest. If a country covers the majority of its needs from indigenous production, as is the case with Romania, or is well diversified despite its high import dependency, as is the case with Greece and Turkey, then it is likely to pursue the implementation of the Southern Gas Corridor Strategy in a more "relaxed" fashion.

On the other hand if a country has no import diversification whatsoever, as is presently the case with Bulgaria, then the Southern Gas Corridor Strategy represents a national economic security challenge of the first degree, and a reason why Bulgaria is participating in one way or another in the Nabucco, ITGI (via the IGB-Interconnector Greece-Bulgaria), BP's SEEP (South East European Pipeline), *and* South Stream projects. In any case, the transit states, and most notably Greece and Turkey, which are involved in the implementation of the three aforementioned pipeline contestants, *have a direct diplomatic stake* in the materialization of *some* of these projects and are thus likely to perceive the construction of one particular pipeline as having a negative or positive impact on their relative power position vis-à-vis both their neighbours and their extra-regional allies (E.U., U.S. and Russia).

This chapter will first analyze the geopolitical rationale behind Europe's Southern Gas Corridor Strategy by focusing on the reasons which have led to the weakening of the Nabucco pipeline project compared to its two smaller and more cost-efficient competitors ITGI and TAP. A special reference will also be made to BP's *South East Europe Pipeline* project, a rather nebulous latecomer in the Shah Deniz 2 race and the way its implementation may influence Greek policy. The failure of Nabucco is also crucial from a Greek diplomatic point of view, since it secures that Greece will receive additional Azeri supplies, which would facilitate the decrease of its import dependency from Russia while also "controlling" the transit of the Azeri gas to both Bulgaria (via IGB) and Italy, even if it is "forced" to "share" this advantage with Albania, in case TAP is selected by the Shah Deniz consortium.[8]

The reasons behind the apparent deadlock of the Nabucco project were primarily geopolitical in nature and -interestingly enough- *partly emanated* from the policy choices of state actors, such as the U.S. government, which *favoured* the implementation of the Nabucco project. The chapter will then focus on evaluating the impact of *SEEP*'s entrance in the Shah Deniz 2 tender. It will then assess the likely impact of each project's implementation on Greece's foreign (energy) policy.

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[6] Elhur Soltanov, *Azerbaijan's Energy Policy: Balancing North and East, Going West,* paper presented at IENE's 5th South East Europe Energy Dialogue, (Thessaloniki: 2-3 June 2011), p.2.

[7] The participation of natural gas in the Albanian primary energy supply is under 0,5%. International Energy Agency, *Energy in the Western Balkans: The Path to Reform and Reconstruction,* Paris, (OECD/IEA: 2008), p.125. In 2008 Albania produced around 9 million cubic meters per year from an all time high of 935 million cubic meters in 1983. Black Sea Economic Cooperation Organization (BSEC), *Energy View of BSEC Countries 2008,* (Athens: 2009), pp.64-65.

[8] The Shah Deniz consortium which is led by B.P. as its operating company, is comprised from BP (25.5%), Statoil (25.5%), Total (10%), LUKoil (10%), Socar (10%), NaftIran or Nico (10%) and TPAO (9%). Nico has acquired the 10% equity from OEIC, an affiliate of state-owned National Iranian Oil Co. (NIOC). The field was discovered in 1999 and reached its Phase 1 maximum output of 9 bcm/y in late 2011. Phase 2 aspires to produce 17 bcm/y of which 10 bcm/y will be transited to Europe via Turkey and 7 bcm/y will be consumed within Turkey. The cost for the near tripling of its production capacity and the upgrading of its associated infrastructure is estimated at $23 billion. Shah Deniz 2 is the only available gas source with which to open the EU's Southern Gas Corridor. More analytically see Al Cook's interview, the Vice President for the Development of Shah Deniz 2 for BP Azerbaijan, to Theodore Tsakiris, " Cook: Shah Deniz 2 Consortium Looking For Scalability In Pipeline Proposals", *Middle East Economic Survey,* 13/06/2011, pp.5-7.

Synopsis of Competing Pipelines for Southern Gas Corridor

Nabucco

Description/Status: The Nabucco Gas Pipeline International GmbH was established following the signing of the Ankara Agreement in July 2009 with the purpose of constructing a 31 bcm/y capacity pipeline over a distance of 4.042 km from Turkey's north-eastern city of Ahiboz to Austria's Baumgarten via Bulgaria, Romania and Hungary. There are two main prospective feeding lines. The first is the existing SCP (South Caucasus Pipeline) that connects Baku to Erzurum and the second (to be constructed) that will link the Turkish NGTS (Natural Gas Transmission System) with Iraqi Kurdistan, even though the exact route is not yet clarified.

Consortium Composition: O.M.V. (Operator), R.W.E., M.O.L., Transgaz, Bulgargaz, BOTAS, each with a share of 16,67%. GDF Suez, Poland's PGNiG, Kazakhstan, and Abu Dhabi based IPIC (International Petroleum Investment Company) have in times indicated their interest to join Nabucco as shareholders/shippers. IPIC already owns 19,6% of OMV shares. In late September 2011 Bayerngas was also reported to be interested in joining Nabucco, but no tangible results have been produced by the time of this study's writing.

Potential Gas Sources: Azerbaijan, Northern Iraq (Kurdistan Regional Government) and Turkmenistan for Phase 1 (by 2017) and possibly Egypt for Phase 2, namely after 2020.

Level of Required Investment: €12-15 billion. Nabucco has secured a €0,2 billion Grant from the European Energy Program for Recovery (EEPR). In September 2010, Nabucco signed a MoU with EIB, EBRD, and the IFC, that commits the three IFIs to complete a due diligence evaluation of the project for a potential financial agreement of €4 billion. The EIB may provide up to €2 billion, the EBRD up to €1.2 billion, while the IFC may provide the consortium with up to €800 million.

Estimated Completion Date: Final investment decision should be taken within 2013. The pipeline should be completed in 2015, in order to receive Shah Deniz 2 gas from 2016. All this scheduling has been pushed back by at least 18 months since no gas would be available from Shah Deniz 2 before 2017.

Trans – Adriatic Gas Pipeline (TAP)

Description/Status: The Trans-Adriatic gas pipeline was established in February 2008 as a Joint Venture Company between Statoil (50%) and EGL (50%). TAP aspired to transfer to southern Italy 10 bcm/y of Azeri gas from Shah Deniz Phase 2 across Turkey, Greece, Albania and the Straits of Otranto. The project wants to utilize the existing NGTS (National Gas Transmission Systems) of Turkey and Greece up to Komotini and then construct a 682 km pipeline across Greece and Albania. The pipeline's offshore length is merely 105 km. In 2011 TAP has completed its route refinement survey across northern Greece and applied for all the necessary Environmental and Third Partly Access Exemption (TPA-E) Permits in all three transit states.

Consortium Composition: As of July 2010, TAP is comprised from Swiss-based EGL (42,5%), Norway's Statoil and Germany's E.ON (15%).

Potential Gas Sources: Shah Deniz Phase 2. Statoil controls 25,5% of the Shah Deniz consortium and is the commercial operator of Shah Deniz Phase 2.

Level of Required Investment: €1,5 billion for the 10 bcm/y pipeline.

Estimated Completion Date: Final investment decision should be taken within 2013. The pipeline should be completed by 2016 at the latest in order to receive Shah Deniz 2 gas from 2017.

ITGI (Interconnector Turkey – Greece – Italy)

Description/Status: The ITGI is comprised from three separate components. (i) The existing ITG pipeline (Interconnector Turkey-Greece) which currently has a capacity of 3,6 bcm/y is owned and operated by DESFA as part of the NGTS. (ii) The 590 km of the future onshore component from Komotini to Thesprotia (capacity of 16 bcm/y) will be built, owned and operated by DESFA the Greek TSO (Transmission System Operator), and (iii) the offshore component (capacity of 8-12 bcm/y) that will cross the Otranto Straits over a distance of 217km will be built, owned and operated by the IGI Poseidon Consortium that was established in June 2008 between DEPA (50%) and Edison (50%). DEPA controls 20% of IGI's commercial company while Edison controls 80% of the pipeline's TPA (Third Party Access) exempted capacity of 8 bcm/y.

Consortium Composition: IGI Poseidon is comprised from Greece's DEPA (50%) and Italy's Edison (50%). In June 2010 Edison, DEPA and BOTAS signed a MoU that will examine the possibility of including BOTAS in the IGI consortium.

Potential Gas Sources: Shah Deniz Phase 2.

Level of Required Investment: €1,3-1,5 billion for the 10 bcm/y pipeline. IGI has secured a €100 million through a Grant by the European Energy Program for Recovery. The onshore section is estimated to cost around €1 billion whereas the offshore section is estimated to cost around €400 million.

Estimated Completion Date: Final investment decision should be taken within 2013. The pipeline should be completed by 2016 at the latest in order to receive Shah Deniz 2 gas from 2017.

IGB (Interconnector Greece – Bulgaria) as a Potential Component of the ITGI "System"

Description / Status Quo: The IGB will link over a distance of 170 km the Greek city of Komotini with Bulgaria's Natural Gas Transmission System (NGTS) in Dimitrovgrad and will be constructed with a reverse-flow capacity. The regular flow capacity will be northbound. The initial capacity of the pipeline is estimated to be 1,5-3 bcm/y but will progressively increase to a maximum transportation capacity of 4.5-5 bcm/y.

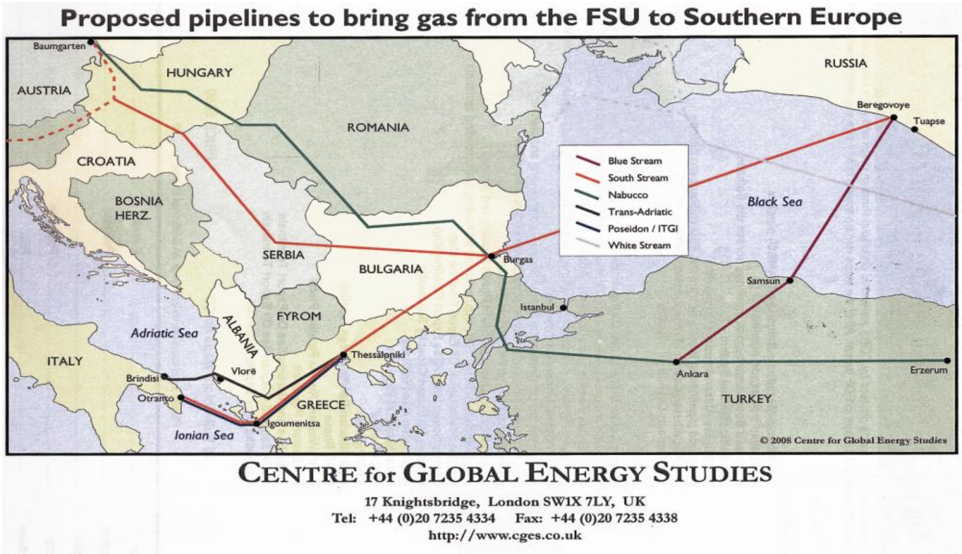
Consortium Composition: IGI Poseidon is comprised from Greece's DEPA (50%) and Italy's Edison (50%) and will control 50% of the JVC that will own, build and operate the pipeline. The other 50% will be controlled by Bulgarian Energy Holding Co. (B.E.H.).

Potential Gas Sources: Commercial gas sources could include a combination of Caspian (Azeri) pipe gas as well as Arab or Cypriot or Israeli LNG. In case of new supply/transit crisis one must add to the aforementioned sources, gas stored in regional strategic storage facilities that are located in Bulgaria, Romania, Hungary and Austria. IGB can be developed both as part of the ITGI project as well as independently.

Level of Required Investment: €160 million

Level of Secured Investment: €45 million through a Grant by the European Energy Program for Recovery

Estimated Completion Date: Late 2013 or early 2014



Source: Centre for Global Energy Studies

3.1. Nabucco: The Geopolitical Demise of a Politically Driven Project

As it has already been mentioned, the implementation of the Southern Gas Corridor Strategy is literally *plagued* by geopolitical traps and sources of risk that are related to security problems both between (Turkmenistan-Azerbaijan, Armenia-Azerbaijan) and within regional states (intra-Iraqi politics, Georgia's ethnic conflicts). There is of course one significant difference regarding the perception of energy security risk(s) on the overall national security position of the involved state actors between the Caspian and Balkan sub-regions of the Greater Black Sea Area. In the Caspian/Caucasus sub-region, energy security is of paramount importance for the regional actors and has a major impact on their relative power position both in terms of economic development and diplomatic influence.

One of the major deficiencies in the planning of Nabucco was that it overemphasized the benefits that project would offer to the European component of the Greater Black Sea Region and underemphasized the way a shift in the regional balance of power in Azerbaijan's immediate neighbourhood would impact on the cost/benefit analysis of Baku, which is the irreplaceable linchpin of the entire Southern Gas Corridor Strategy.[9] Nabucco's planners were not the only ones to make this miscalculation. Elements of the European Commission bureaucracy that supported the project quickly followed suit and tried to combine the timetable of Nabucco's implementation with the Commission's involvement in the resolution of the region's flash points and most importantly the Caspian border dispute between Azerbaijan and Turkmenistan.

Having failed to assist the Nabucco consortium financially, other than securing (March 2009) its inclusion -with a EUR 200 million grant -in the *European Energy Programme for Recovery*,[10] parts of the European Commission bureaucracy have attempted to resolve in close coordination with the U.S. the main geopolitical problems blocking Nabucco's access to non-Azeri gas resources, and in particular Turkmen gas exports. ***It should nevertheless be noted that this geopolitical alliance was neither unconditional nor has it been always harmonious.*** The two sides agreed on the geopolitical goals and the benefits of building

[9] On 17 November 2010, the European Commission adopted the Communication "Energy infrastructure priorities for 2020 and beyond - A Blueprint for an integrated European energy network." This document says that the strategic objective of the Southern Corridor is to achieve a supply route to the EU of roughly 10-20% of EU gas demand by 2020, equivalent roughly to 45-90 bcm/year.

[10] http://europa.eu/rapid/pressReleasesAction.do?reference=IP/10/231. Nabucco received a grant in the order of EUR 200 million while the ITGI/IGB nexus received a combined grant of EUR 145 million, of which EUR 100 million for IGI/Poseidon and EUR 45 million for the IGB.

Nabucco, even though the diversification of European gas imports was *per se* a secondary priority for Washington. ***They did differ though significantly on the geopolitical means through which Nabucco should be promoted. U.S. diplomacy and Nabucco's corporate strategy did not always see eye to eye on the sourcing of the gas and whenever there was a major disagreement, as we will examine below, the U.S. won the case. This disagreement appears to have seriously weakened Nabucco's chances to win the Shah Deniz 2 tender which will initiate the implementation of the Southern Gas Corridor Strategy.***

Agreeing on the Targets/Rationale

The European Commission and the pro-Atlanticist member-states of the E.U. who are either not dependent on Russian natural gas (U.K.) or over-dependent on Russian gas imports (Poland, Baltics, Central Europeans) are in complete agreement with the general political motivation driving U.S. and E.C. energy policy in the Caspian Sea. This has been the case since the early 1990s and the completion of the Baku-Tbilisi-Ceyhan oil pipeline (BTC) that aspired to consolidate the geopolitical independence of the former Soviet states by giving their hydrocarbon resources not only export markets but also transit routes that would both bypass Russia.[11]

Azerbaijan was the first and so far the most successful "case study" of this strategy that clearly antagonizes Russian efforts to establish a hegemonic post-colonial "sphere of influence" along the southern tier of the entire former Soviet frontier in the Caucasus and Central Asia. The rationale of the U.S. strategy was that the elimination of the Russian monopoly on the export pipeline network of those four states (Azerbaijan, Kazakhstan, Turkmenistan, Uzbekistan), and the emergence of Europe as an alternative export market, would seriously curtail Moscow's ability to neutralize any serious pro-western/pro-U.S. orientation on the part of these states.[12]

This of course was only half the answer. The other half was supposed to be given by "conflict resolution" in ways that would drastically diminish Russia's "meddling" in a series of so-called "frozen conflicts" which span the former southern Soviet periphery and are "literally" in the middle of Nabucco's way, from the Turkmen-Azeri dispute over the boundaries of their Exclusive Economic Zones and the sovereignty of the Kyapaz/Serdar field in the Caspian Sea to the Nagorno Karabakh conflict between Armenia and Azerbaijan and the Russia-Georgian War over South Ossetia and Abkhazia.

If the construction of the Nabucco project could motivate these states to resolve their bilateral disputes, that would make the access of Nabucco to the gas resources of these states-especially Turkmenistan-much more attainable. According to U.S. strategic perception, the majority of national income for these four states –with the partial exception of Kazakhstan where oil and gas revenues account for "merely" 45% of GDP-emanates from hydrocarbon exports.

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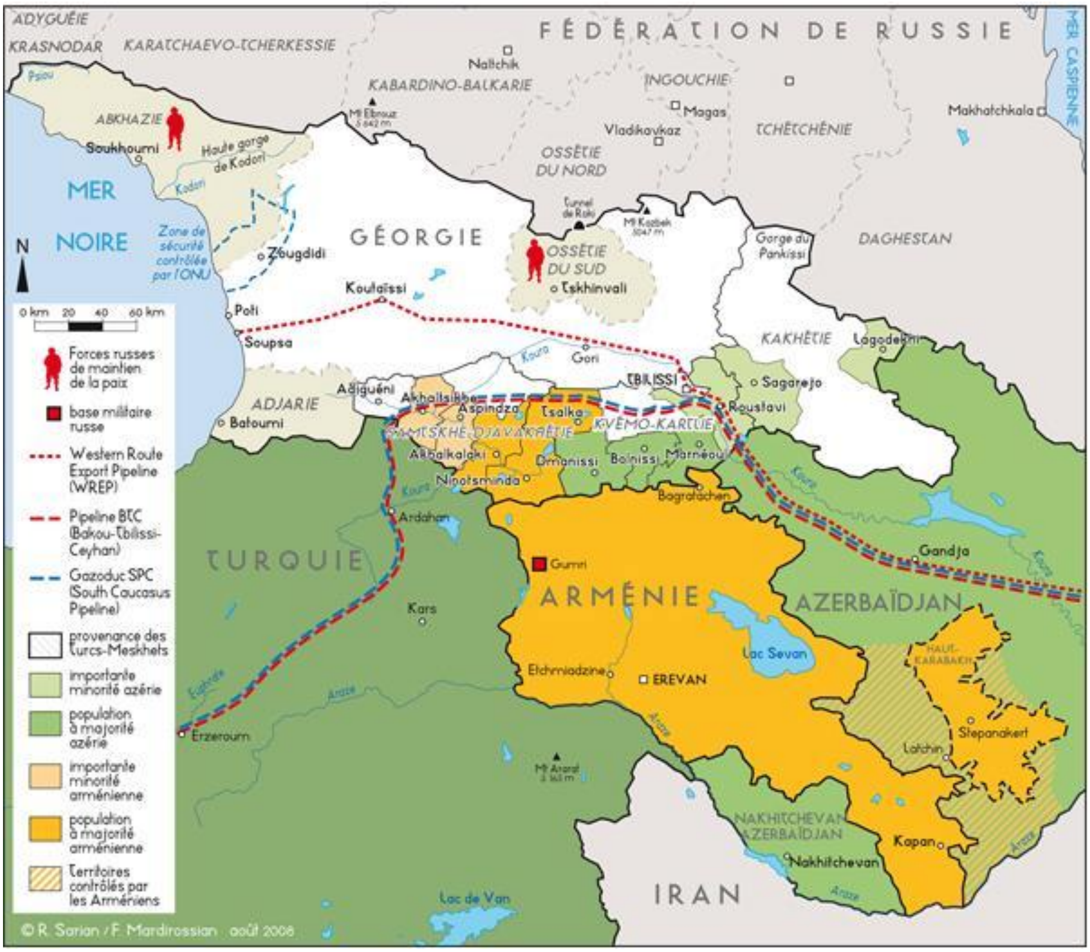
[11] As former U.S. Energy Secretary Bill Richardson noted in 2005, "I have seen energy advance U.S. geopolitical interests, as the nation did in pressing successfully for the construction of east-west oil and gas pipelines in Central Asia, securing political autonomy for the newly independent states of the former Soviet Union". Bill Richardson, "Foreword", in Jan Kalicki & David Goldwyn (eds.), *Energy & Security: Toward a New Foreign Policy Strategy,* Woodrow Wilson Center Press, (Washington D.C.: 2005), p.xvii. Jan Kalicki who served during the 1990s as the U.S. Ombudsman for Energy & Commercial Cooperation with the Newly Independent States notes that "Moscow recognized that alternative oil route would give the Caspian states a measure of independence never before enjoyed since at least the Bolshevik Revolution. The U.S. government played a critical role in countering this opposition –recognizing the stakes involved for the future independence of the Caspian States", in Kalicki & Goldwyn, ibid, p.162.

[12] For the strategic rationale behind U.S. Caspian policy see, Strobe Talbot, *The Russia Hand: A Memoir of Presidential Diplomacy,* (Random House: 2002), pp.91-94, Zbigniew Brzezinski, *The Grand Chessboard: American Primacy and Its Geostrategic Imperatives,* (Harper Collins: 1997), pp.128-130 & Barnes Joe, "U.S. National Interests: Getting Beyond the Hype", in Yelena Kalyuzhnova, Amy Myers Jaffe & Dov Lynch (eds.), *Energy in the Caspian Region: Present and Future*, London, (Palgrave: 2002), pp.215-216.

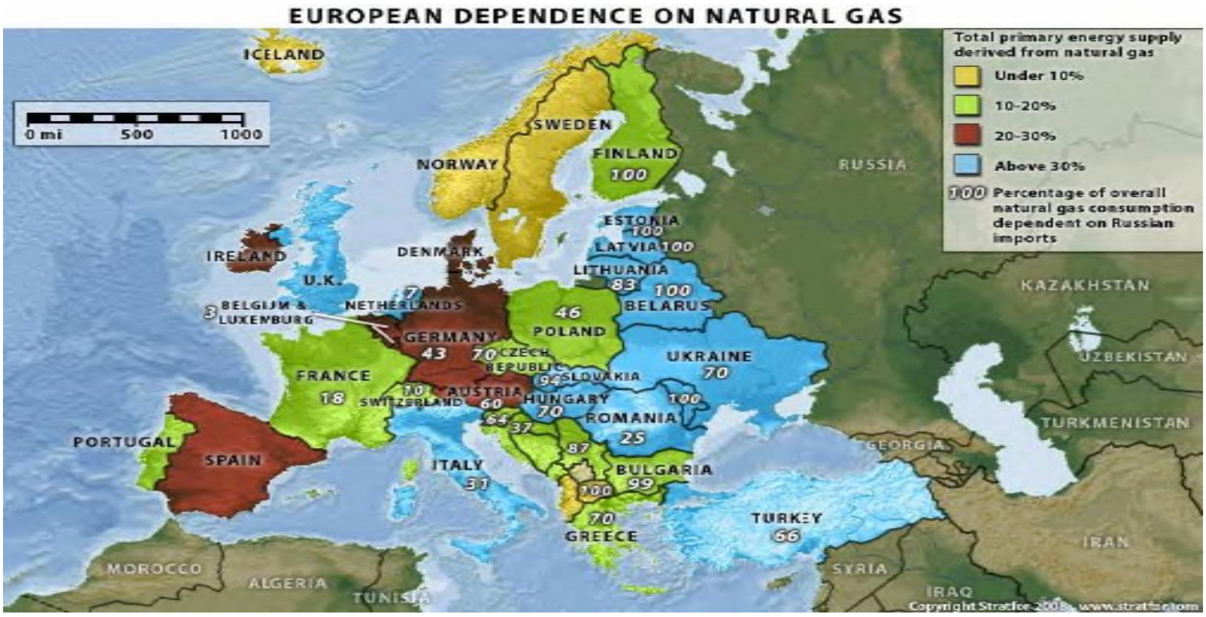


Source: Le Monde Diplomatique, August 2008

Therefore he, who bought and simultaneously controlled the routes of these exports, would be able to exercise a predominant influence over their foreign and security policy. *Nabucco was supposed to do for the U.S. in the 2010s what the Baku-Tbilisi-Ceyhan (TBC) did in the 1990s: drive a hole in Russia's ability to dominate the post-soviet economies of its hydrocarbon-rich "comrade" colonies. Yet Nabucco was and remains even more dangerous from a Russian point of view*. Compared to BTC, Nabucco would deliver an even harder blow on Russia's geostrategic ambitions, since, thanks to its size, it would not only "open up" Turkmenistan to Western influence, but also allow Ukraine to limit its dependence on Russian gas imports thereby facilitating a more pro-western orientation of Kiev's foreign and defence policy that could even allow its eventual inclusion into NATO. This is not a far-fetched scenario. This nearly happened in April 2008 and constituted the main underlying cause for the Russian-Ukrainian gas crisis of January 2009. Russia did not hesitate to remind to the non-Atlanticist Europeans and to pro-western Ukrainians that it could "gladly freeze" Europe and lose billions of dollars in revenue in order to keep Ukraine out of NATO. At the same time Russia's ambassador to NATO indirectly threatened Ukraine with the possibility of Crimea's separation.[13]

[13] More analytically See Theodoros Tsakiris, *The Blue Gold: Russo-Ukrainian Relations and Europe's Natural Gas Strategy*, Hellenic Center for European Studies, (Papazisis Publications: 2011), (in Greek), pp.108-112.

No one should ignore that one of the fundamental motivations behind the Kremlin's determination to scuttle Nabucco, is to pre-empt any possibility for the diversification of Ukrainian gas imports from Azerbaijan and more importantly Turkmenistan. Such an eventuality would allow Kiev to resist Russian demands on the security of its European-oriented gas exports, while resisting Moscow's continued long-term military presence in the Crimea. This presence is a propos one of the stronger guarantees that Ukraine will stay out of NATO.[14]



Source: *Tanguy Moulin-Fournier, Head of Strategy for GDFSuez South East Europe, "Southeast Europe as the Gateway to European Gas Security of Supply", Paper presented at IENE's 3d South East Europe Energy Dialogue, Thessaloniki, 18-19 June 2009, p.8.*

For Atlanticist Europe the diminishment of Russia's control over its former "Near Abroad" was a welcoming development especially if it was accompanied by the means of limiting their overwhelming dependence on Russian gas imports. The announcement in March 2011 that Nabucco was planning to extend its reach by another 60km to the Czech hub of Lanzhot so as to be able to penetrate the Slovakian, Czech and Polish markets,[15] may make little sense for a project that has no gas contract whatsoever, but it attests to the geostrategic rationale which has been driving Nabucco for the better part of decade. This is not to say that other EU member-states like Greece, Italy, Germany and France would not want to diversify –to various degrees- from Russian gas imports. Their main difference with "Atlanticist" Europe is that:

(a) they are more worried that a lessening of Russian predominance in the post-Soviet space will make Russian gas exports to Europe *less, not more, secure* and that is part of the reason why they support the *bypassing of Ukraine, Belarus and Poland via the construction of the Nord & South Stream projects without refraining from participating in the smaller Caspian-originated pipelines that would inflict minimal damage on Russia's regional power position such as ITGI and Trans Adriatic Pipeline (TAP).*[16]

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[14] Ukraine wanted to join Nabucco as early as 2006 and was among the first to welcome the pipeline's relative progress during 2009 especially after the signing (13 July 2009) of the pipeline's Intergovernmental Agreement (IGA) in Ankara. See Simon Pirani, Jonathan Stern, & Katja Yafimava, *The Russo-Ukrainian Gas Dispute,* ibid, pp.52-53, "Ukraine Welcomes Nabucco Gas Pipe, Ready to Join", *DowJones,* 14/7/2009 & "Ukraine Interested in Joining Nabucco Consortium, Considering LNG Imports", *Middle East Economic Survey,* 27/07/2009.

[15] "Deadline Set for Competing Gas Corridor Projects, Nabucco Plans Extension", *Middle East Economic Survey,* 28/03/2011, pp.8-10.

[16] Greek policy never accepted the premise that Nabucco and South Stream are mutually exclusive opting instead for a far more balanced approach that simultaneously promoted both the ITGI and South Stream projects, a policy that was more close to the general opinion of the European Council rather than the European Commission bureaucracy. See, Elisabeth Loverdos & Theodore Tsakiris, "Greece's Role in Europe's Energy Security Policy for Natural Gas", *Evropeon Politeia,* 03/2009, p.625. Jozias Van Aartsen, the former Dutch Foreign Minister and the first European Council appointed Southern Gas Corridor Coordinator specifically notes in

(b) they believe that any form of diversification away from Russian gas imports does not have to come primarily from the Caspian Sea, as opposed to greater Arab LNG imports (from Qatar) and the development of Eastern Mediterranean (Israel / Cyprus) and North African (Libya, Egypt, Algeria) gas resources;

(c) they also believe that any form of Caspian gas that bypasses Russia should inflict –for the time being- a minimal (Azerbaijan) not a maximal (Turkmenistan) geostrategic damage on Moscow's relative power position vis-à-vis the U.S. in the post-Soviet space, even though this position seems to be under review after the expansion of Turkmen gas deposits in South Yolotan and

(d) Incidentally, these four states are neither part of the Nabucco project nor of the Nabucco lobby, even though France initially attempted to join the Nabucco consortium in 2008 via GdF only to be vetoed by Turkey due to France's recognition of the Armenian genocide, as well as French scepticism regarding the pace, quality and desirability of Ankara's integration into the E.U.[17]

Disagreeing on the Tactics: Analysing Nabucco's Deadlock

Even though Nabucco's European patrons and Washington agreed from the start on what would be the geopolitical benefits served by the implementation of Nabucco they differed greatly on what geopolitical tactics should be followed in order to pursue the realization of the project. In reality U.S. diplomacy not only blocked Nabucco's efforts to get Iran involved in the project but also impeded any practical chance Nabucco had to get any KRG (Kurdish Regional Government) gas in time to meet SOCAR's deadline for the tendering of SD2 gas even if this deadline is moved to mid-2013, as OMV's CEO, Gerhard Roiss recently noted following Shah Deniz's decision to eliminate the ITGI project from further consideration on 20 February 2012.[18] This double geopolitical jeopardy coupled with the growing financial inability of the Nabucco downstream partners to continue to foot an ever increasing bill have magnified Nabucco's quagmire, while illustrating the strategic significance of Turkmenistan as a potential "life saver" for the 31 bcm/y project.

Iran

When Nabucco initially appeared on the Caspian Gas arena in 2002-2003, it targeted both Azeri and *Iranian* gas resources. According to its original rationale Shah Deniz 2 gas, which was initially expected in 2014-2015 would be complemented by *existing* Iranian gas resources that already reached Turkey since 1997. In reality Iran was swapping its own Turkmen imports with exports to the Turkish market and could thus increase the volume according to Nabucco's needs.

The political climate before the unexpected emergence in 2005 of Mr. Mahmoud Ahmadinejad as the President of Iran guaranteed the supply of at least 5 bcm/y to Nabucco and that is exactly what the project needed to convince the Azeris, the SD2 consortium and the IFIs (International Finance Institutions) that it was truly bankable. As the U.S. government escalated its economic warfare campaign against Tehran throughout 2005-2010 it succeeded in not only coercing the exit of every major European company from Iran's own onshore sector –including inter alia OMV- but *also forced Nabucco's partners –over the vociferous opposition of Turkey- to drop any idea regarding not only the supply of Iranian gas to Nabucco but also the supply of Turkmen gas to Nabucco via Iran*.[19]

The Nabucco consortium and its political lobby was very well aware that this could mean the economic sinking of the project, especially from the moment that the U.S. forbade even the transit of Turkmen gas via

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his first report that "projects such as Nabucco and South Stream are compatible", Jozias Van Aartsen, *Activity Report: September 2007-February 2009 / Project of European Interest n° NG3*, Brussels, (4 February 20009), p.3.

[17] "Franco-Turkish Dispute Overshadows Nabucco Project", *Euractiv*, 20/02/2008, http://www.euractiv.com/en/energy/franco-turkish-dispute-overshadows-nabucco-project/ article-170424

[18] "OMV: Shah Deniz Pipeline Decision To Come Middle 2013", *DowJones*, 22/02/2012

[19] On the division inside Nabucco regarding the necessity of securing Iranian supplies, which was led by OMV and Botas and opposed by RWE, see Igor Tomberg, *Iran in the European Gas Market: A Russian Point of View*, IFRI, Institut Français des Relations Internationales, (October 2009), pp.15-18 & Theodoros Tsakiris & Costis Stambolis, *The Energy Security Policy of the Islamic Republic of Iran: Domestic and International Parameters with an Emphasis on Natural Gas Exports to Europe*, Institute of Energy for Southeast Europe, (Athens: December 2009), pp. 32-40

Iran. As Turkey's Prime Minister Reccep Tayip Erdogan noted repeatedly in 2009 even after the signing of the Nabucco Intergovernmental Agreement in July 2009, "Nabucco cannot work without the participation of Iran".[20] The fact that Nabucco managed to "hide" this major strategic failure from its own "risk calculus" for over two years is another testament to the political influence the Nabucco lobby enjoys in both Washington and Brussels.

Since Nabucco's initial feasibility study estimated a capital expenses cost of around EUR 8 billion for a 3.300 km pipeline, the obligatory rerouting of the project that expands its length by an additional 500km, would unavoidably increase its final cost and make it even more difficult for SOCAR and the other SD2 partners to accept. It took Nabucco until May 2011 to publicly recognize that the re-routing of its original pipeline network from Iran to Iraq would increase its cost by several billion EUR, even though it has yet to clarify the extend of the estimated increase.[21] It was none other than the EU Energy Commissioner Guenther Oettinger who acknowledged on 8 May 2011 that "Nabucco will cost between EUR12 billion and EUR15 billion".[22] ***If Iran was not excluded from any form of participation in the Nabucco project the pipeline would have already been built***. The damage done to Nabucco by U.S. diplomacy is truly revealed by the fact that Iran has managed to expand its ability to import Turkmen gas from 8 bcm/y to around 20-22 bcm/y by commissioning since January 2010 a second pipeline linking its gas processing plant in the north-eastern city of Kharingan with Turkmenistan's Dauletabad field.[23] *If the U.S. had allowed even for the transit of Turkmen gas to Turkey via Iran, as Ankara repeatedly pleaded with Washington, there would have been no need for Nabucco or its Brussels-based lobby to put all of their eggs in the Trans-Caspian pipeline basket*.

Iraq

Iraq's prospective involvement in the Nabucco project, which will justify for most of the drastic increase in Nabucco's capital expenses, dates back to the signing of the project's Intergovernmental Agreement in July 2009, when Iraq's Prime Minister Nuri al-Maliki pledged to supply the project with "at least" 15 bcm/year of gas.[24] Of course the Iraqi PM did not specify from where the gas would come, even though the only readily available potential is the Khor Mor and Chemchemal gas fields where UAE's Dana Gas in cooperation with Nabucco partners OMV and MOL have finally started to produce significant gas quantities since January 2011.

In September 2010, Kurdistan's natural resources minister, Ashti Hawrami, told *Platts* that by mid-2011 the Arab-European JVC would have linked the fields with the Dohuk power station and have a surplus production capacity of around 5 bcm/y that could be channelled to Nabucco via the Turkish Natural Gas network after a 50km interconnector is build between Dohuk in Northern Iraq and the Turkish regional gas network.[25] Yet, apart from the fact that Nabucco would still have to construct its own 500km link to the Turkish-Iraqi network and upgrade the system along the way, one should also note that the Khor Mor/Chemchemal fields have yet to reach the aforementioned 5bcm/y overcapacity, even though this has little to do with the consortium's technical or financial ability. Increased production on the fields as well as any plans for their potential exports to Turkey will have to wait for a comprehensive resolution of a major intra-Iraqi feud over the division of hydrocarbon revenues between the central Iraqi government and KRG.

This process which has developed into a *cul de sac* between Baghdad and Erbil was unlikely to be essentially resolved in time for Nabucco to meet either the October 1st 2011 deadline for the final submission of

[20] "Erdogan Warns of Nabucco Failure Without Iranian Participation", *Middle East Economic Survey / M.E.E.S.*, 05/10/2009, pp.11-12. It is also notable that Former German Chancellor Gerhard Schroeder, now a board member of the Nord Stream pipeline company, told reporters that day that, to improve its prospects, "Nabucco should be filled with gas from Iran, because it offers another alternative for gas shipments to Europe. However, the European Union will have to overcome political resistance, and it will need strength to settle political disagreements over sanctions targeting Iran and energy sources originating from this country", *ibid*.

[21] As late as June 8 2011, Mr. Stefan Judisch the head of RWE's Gas Supply & Trading division, who is spearheading Nabucco's efforts to secure the necessary gas supplies, noted that ""What we can already say is that the costs will increase to reflect the fact that the pipeline is now planned to be longer because of the [new] feeder to Iraq…But on a like-for-like basis --excluding the Iraqi feeder-- the final construction costs will be marginally higher than our present estimate". *M.E.E.S.*, 13/06/2011.

[22] "EU Energy Commissioner: Nabucco to cost between EUR 12b to EUR 15b", *The Wall Street Journal*, 09/05/2011

[23] "New Turkmenistan-Iran Gas Pipeline Inaugurated", *M.E.E.S.*, 11/01/2010, p.15.

[24] *M.E.E.S.*, 20/07/2009

[25] "From the Wellhead", *Platts Oilgram*, 31/01/2011, p.9.

tenders regarding the transportation of SD2 gas to Europe and it is equally unlikely that is will influence the SD2 final decision which may come within 2012 or by mid-2013 at the latest. Under the current legal framework the Khor Mor / Chemchemal PSA (Production Sharing Agreements) signed by the KRG with Dana, OMV and MOL are null and void according to authorities in Baghdad who are wary of seeing the KRG emerging as a de facto energy exporter outside the national policy framework. Such a development would create additional friction between OPEC and Iraq over the latter's function outside the OPEC system. No Arab Iraqi can accept Irbil's energy independence outside the context of a Federal Petroleum Law which would include a proportionate distribution of export revenues between Iraq's three communities. The export contracts KRG could sign with Nabucco would effectively be null and void without Baghdad's consent.

This deadlock has plagued the essence of Iraqi politics since 2008 and even though a draft Petroleum Law was agreed at the Parliamentary Committee Level on 17 January 2012[26] it is not certain that it would get the Parliament's final approval. There are several good reasons for the continuation of this deadlock since the Kurds have linked their acceptance of an internal quota mechanism that could leave most of their oil & gas export earnings at the hands of the Iraqi Federal Government on the incorporation of Kirkuk into the KRG. It is not clear if the Kurds have won a commitment on Kirkuk but any last minute back-state dealing may prevent the implementation of the agreement even if the Law is finally approved by the Parliament. The complete withdrawal of U.S. combat troops from Iraq in December 2011 has further complicated the labyrinth of post-Saddam Iraqi politics thereby leaving the Kurds little incentive for making any substantial concessions to their Arab partners. More importantly Sunni and Shi'a Iraqis would not even agree to the export of KRG gas, especially if Baghdad wins the upper hand vis-à-vis Irbil on future gas exports.

Washington had clearly sided with Baghdad against Irbil on this matter, thereby unintentionally undermining Nabucco for a second time. There was a very good reason for that and it related to the U.S. failure to revamp Iraq's post Saddam electricity system that has managed to provide Arab Iraqis with a mere 4-6 hours of power per day. Contrary to the KRG where electricity supply is constant for 20-22 hours per day, the rest of the country is dramatically undersupplied. *Moreover what Iraq is forced to do to make up for this undersupply is even more worrisome from the U.S. perspective*. Baghdad is not only importing around 1.000 MW of Iranian electricity amounting to approximately 1/7 of its final demand and 50% of its overall imports, but has also signed on 30 June 2011 a $365 million agreement with Tehran for the construction of a gas pipeline that will provide three major Iraqi Thermal Power Plants with some 25 million cubic feet of Iranian gas a day. The three power plants surround the Iraqi capital and are located in the Sadr City as well as the northern and southern outskirts of Baghdad and would be able to produce up to 2.500 MW of electricity. The pipeline which will be build primarily on Iranian expenses with an Iraqi participation equal to 25% of capital expenses is estimated to be 130km long and 48 inches in diameter.[27]

Washington is unlikely to pressure Iraq to meet Nabucco's timetable while sitting idly by as Iran expands its economic influence over the Iraqi federal government. The instability in the country is more than endemic as the volatility of its ethnic and clan-based political structure has again started to rise following the U.S. military withdrawal. In January 2012 alone dozens of Iraqis died in renewed Shia-Sunni clashes and terrorist attacks around Baghdad and the so-called Sunni triangle. The following day the Parliamentary Committee voted in favor of the Petroleum Law the major Sunni-party, *Iraqiya,* left the al-Maliki government in protest over the Prime Minister's order to arrest on December 2011 a leading member of *Iraqiya* and Iraq's very his own Vice President, Tariq al-Hashimi, on the grounds of "terrorist activities".[28]

At the end of the day if Iraq agrees to seriously promote a gas production policy, such a policy will be almost entirely domestically oriented in order to maximize oil exports and limit its growing dependence on Iranian electricity and fuel oil imports. There could be as much as 5-10 bcm/y of Iraqi surplus production available for exports by 2013-2015 but no one in Iraq would loose its sleep over how quickly they could be exported or if they would be exported in time to "save Nabucco". As Iraq's Deputy Prime Minister for Energy Al-

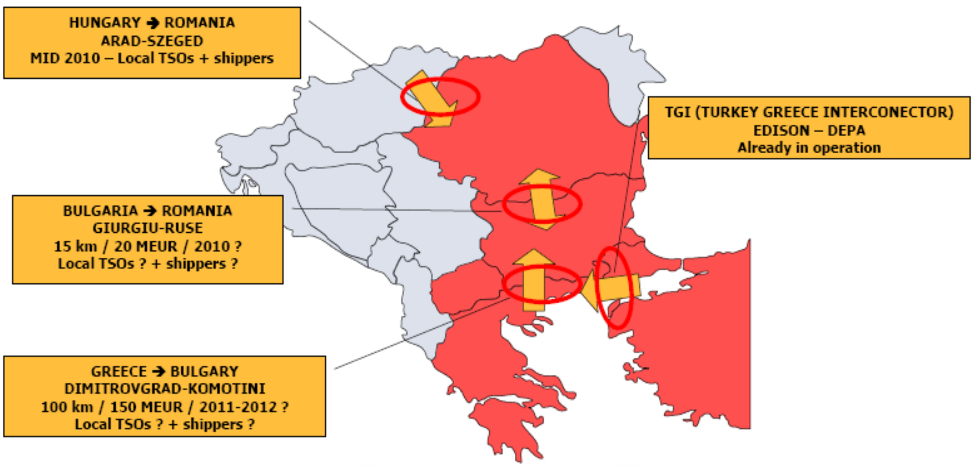
[26] "Iraqi Leaders Agree Draft Oil Law", *Reuters,* 17/01/2012
[27] "Iran, Iraq Finalize Gas Pipeline Agreement for Thermal Power Plants", *Shana,* 30/06/2011
[28] "Iraq Finishes First Oil Export Expansion Phase", *Platts Oilgram News,* 19/01/2012

Shahristani clearly stated on 7 April 2011: "We have an agreement to supply the EU with some gas, not necessarily from Nabucco. Iraq is not committed to that project".[29]

Nabucco Downstream

One additional factor that magnifies Nabucco's problems is the fact that it can no longer trust the ability of its weakest links, namely the fragile economies of Bulgaria, Romania, and Hungary, to be able to foot an ever increasing bill so as to basically transport around 20 bcm/y to Austria's main transit hub located close to Vienna in Baumgarten. Each of these EU newcomers may not need more than 2-3 bcm/y of additional gas supply in order to cover its prospective demand by the end of the current decade. For those 2-3 bcm/y that amount to around 1/4 to 1/3 of Nabucco's transportation capacity these states were asked to *carry the same burden of cost (EUR 1,31 billion) carried by major European companies who actually led the project such as OMV and RWE*.

That was already a hard act to follow even *before* these three states introduced strict austerity programmes supervised by the IMF. Now that the aforementioned equal burden of cost may increase to EUR 2-2.5 billion –if Nabucco's budget reaches EUR 12-15 billion- it would be next to impossible for these states to finance their own contribution to Nabucco without *prior* IMF approval or EIB (European Investment Bank) assistance, especially since (a) Bulgaria and Hungary have already joined South Stream, (b) Romania is negotiating its own inclusion into the Russian-led project and most importantly (c) Bulgaria, Romania and Hungary along with Greece and Serbia will be interconnected by 2014 with five 3-5 bcm/y capacity pipelines which are 1/3 funded by the European Commission, with a total cost of EUR 370 million,[30] and are much more tailored to their *actual* needs and their *actual capacities* compared to what Nabucco would have to offer them.



Source: Tanguy Moulin-Fournier, ibid, p.19.

The emergence of these smaller capacity pipelines has had a profound impact on Azeri strategy and the relative competitiveness of the Nabucco, TAP and ITGI projects in the following ways:

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[29] "Iraq looks beyond Nabucco for gas exports to Europe", *New Europe*, 10/04/2011

[30] The total cost of the IGB, IBR and IRH gas pipelines that were all included in the European Energy Programme for Recovery in March 2009 approximated EUR 250 million. The feasibility study on the Interconnector Bulgaria-Serbia (IBS) approved by the European Commission in April 2011 referred to a cost estimate of EUR 100-120 million for a 150km pipeline, of which EUR 60 million have been earmarked by the Regional Development Fund of the E.C. "Bulgaria Seeks Consultant for Gas Interconnection with Serbia", *Sofia Echo*, 12/07/2011, http://sofiaecho.com/2011/07/12/1122339_bulgaria-seeks-consultant-for-gas-interconnection-with-serbia

(a) It has undercut the willingness of the weaker Nabucco partners to support an ever expanding project that is growing more and more inimical to their own needs. This is a fact which is not lost to the Azeris and the SD2 partners as it was clearly noted by Senior SOCAR Vice-President Elshad Nassirov on 15 November 2010 who underlined that "Important to us is that whatever pipeline we choose, we want the right to sell our gas to the nearest markets. We do not consider the idea of Nabucco merely transporting our gas from Baku to Baumgarten...With a small upgrade, more Balkan countries can be linked to Nabucco. These countries have expressed their interest in getting small volumes of our gas. From Nabucco, we want to supply Greece as well. If we go ahead with the smaller pipelines like ITGI, we will also not limit ourselves to the supply zones of Greece and Italy only. From Greece we can supply Bulgaria, F.Y.R.O.M., Albania and Serbia too".[31]

Apart from the fact that Greece does not need to link to Nabucco to get more gas from Azerbaijan, since it already does so via the ITG (Interconnector Turkey-Greece), Nabucco has been unable to offer additional market outlets to SOCAR in the Western Balkans as the Trans Adriatic Pipeline plans to do through the I.A.P. (Ionian Adriatic Pipeline) or DEPA/Edison plan to do via the IGB for Bulgaria, Romania and Hungary. It should be noted though that Nabucco did propose the extension by 60km of its westernmost extreme from Baumgarten to the Czech hub of Lanzhot so as to be able to penetrate the Slovakian, Czech and Polish markets while Poland's *PiNG* has expressed its interest to join the OMV/RWE-led project since early 2009.[32]

Such a western extension may satisfy SOCAR's demand for greater downstream penetration but makes little economic sense unless the Balkan components of Nabucco are persuaded to foot the bill. *Nabucco could of course restructure its shareholders structure so as to ease the financial burden on its Balkan components by attracting Poland's PiNG and CEZ or another major German company, but this is unlikely to happen over 2012 when Shah Deniz is expected to take its decision on which of the two Baumgarten-bound projects (Nabucco or SEEP) will be selected to compete with TAP.*[33]

(b) The emergence of this interconnected market system, of which the first component, the Interconnector Romania-Hungary became operational in October 2010,[34] has opened up a prospective gas market of 10 bcm/y to SOCAR that can be tapped *three-to-four years before* Shah Deniz 2 (SD2) begins to produce any gas in 2017. This system offers *readily available European markets to the Azeris and is currently being duplicated by BP's SEEP planners who have yet to clarify which components of this interconnected system will be utilized for its own anti-Nabucco pipeline alternative.*

(c) The fact that the two crucial components of this interconnected chain, the ITG (Interconnector Turkey-Greece) and the IGB (Interconnector Greece-Bulgaria) are controlled by Greece's DEPA and its national TSO (DESFA), underline a significant advantage for the ITGI/IGI Poseidon project vis-à-vis Nabucco. Once ITG's capacity is upgraded by DESFA and once IGB is completed hopefully by late 2013, Greece can help SOCAR to tap an *existing market three-to-four years before SD2 or alternatively fill the Balkans' demand via Arab or Israeli LNG*. All these factors have forced Nabucco to concentrate its efforts on Turkmenistan as the most probable additional gas source to SD2.

Despite the fact that the U.S. has been trying to forge a strategic rapprochement between the two states, ever since their first ever joint oil & gas conference took place in Baku in September 2008, there has been very little progress on any prospective Trans-Caspian Pipeline that could prove a "life saver" for Nabucco for more than two years, despite a recent mandate given (September 2011) by the European Council to the European Commission that allows it to negotiate with Turkmenistan and Azerbaijan the prospect of constructing

[31] Elshad Nassirov interview with Rudolf ten Hoedt, "We Don't Want to Depend on only One Pipeline", *European Energy Review*, 15/11/2010.

[32] Over 2011 TAP has signed MoU with Montenegro, Croatia, BiH, and Slovenia in order to examine the possibility of exporting Azeri gas through the construction of the Ionian Adriatic Pipeline (I.A.P.). Such a prospect would depend on the availability of Azeri exports beyond Shah Deniz 2. "RWE Outlines Nabucco Extension Plans", *M.E.E.S.*, 25/04/2011. On TAP's Western Balkan agreements, http://www.trans-adriatic-pipeline.com/

[33] As late as December 2011, Rovnag Abdullayev, SOCAR's President, stated that the final decision on the SD2 Main Export Pipeline will be taken by April 2012. "Shah Deniz Gas Export Decision Now Due by April", *News Azerbaijan*, 12/12/2011, http://news.az/articles/economy/50687. This is no longer the case, as it is more likely that the consortium will decide on the final selection within 2013.

[34] Theodoros Tsakiris, *"Balkan Gas Interconnectors Progress as Borisov Grows Wary of Nabucco", Euractiv*, 10/12/2010.

a TCP line. Then two developments occurred: (a) the further upgrading of Turkmen gas resources which may hold as many as 24,6 trillion cubic meters (TCM) from an existing confirmed resource base of 8,1 TCM[35] and (b) the unexpected declaration of the Turkmen head of state Gurbanguly Berdymukhamedov in November 2010 that it would de-link the construction of a Trans Caspian Pipeline or TCP from its long-standing dispute with Azerbaijan over the sovereignty of the Kyapaz/Serdar fields.

3.2. Leading the Way: BP Tilts Shah Deniz Partners Against Nabucco

Yet unfortunately for Nabucco, as it became clear–by late January early February 2011- that the Turkmenistan "rescue" option has lost its erstwhile momentum, BP, which controls 25.5% of the Shah Deniz consortium, seized the initiative and slowly –although steadily- begun shifting the pendulum against Nabucco and in favor of its own *SEEP* project which was nevertheless disclosed as late as September 27, 2011. BP's "attack" on the credibility of the Nabucco project was carried out through the following initiatives/developments some of which were supported indirectly by SOCAR and the Azeri government, even though Baku did not target *per se* the credibility of the Nabucco project.

It should nevertheless be underlined that Nabucco's own handling of this "attack" only magnified its effectiveness in ways that consolidated the belief of both Baku and Shah Deniz that ITGI or TAP are much more competitive alternatives compared to the 31 bcm/y project: (i) On 20 February 2011 senior BP executives with intimate knowledge of the Shah Deniz and South Caucasus Pipeline extension[36] projects told *The Guardian* that the real price of the Nabucco project was far greater than the one hitherto quoted by the consortium, due to the obsolete nature of its initial feasibility study that was completed in 2005 and more importantly its inability to secure any gas from Iran, as it was originally planned in 2003-2005. BP noted that the real cost would be as high as EUR 14 billion, almost double the initially required sum of EUR 7.9 billion.

Two days earlier Nabucco's CEO Mr. Reinhart Mitschek told in an interview with *DowJones* on 18 February 2011 that he remained confident on the prospective construction of the project as he reconfirmed the pivotal importance of securing Shah Deniz 2 volumes as a prerequisite for the realization of the Nabucco pipeline. "I'm convinced we will get the needed gas," Mitschek noted, underlining that "without supply contracts with Azerbaijan there will be no Nabucco pipeline." Mitschek also declined to evaluate the possibility of a potential merging between Nabucco and the two other Southern Corridor projects, ITGI and TAP, noting that "We are open to so-called dock on projects, that ITGI and TAP for example hook up to Nabucco in Turkey. But for that a merger won't be necessary".

ITGI leaders Edison and DEPA have also declined the prospective conglomeration of the two projects insisting that ITGI can and should be built first, even though Harry Sachinis, the CEO of DEPA has been keen to present ITGI since at least June 2010 as the first step of a larger Nabucco project, which could follow ITGI's construction.[37] Mr. Mitschek's optimism is nevertheless checked by the fact that the consortium has been obliged to push, for the forth consecutive time, the deadline for the Final Investment Decision (FID) to early 2012 while admitting a significant increase of the cost, as it is rerouting the project's final plan to connect with

[35] "Turkmen Energy Minister Announces Expected Rise in Gas Reserves", *M.E.E.S.*, 14/03/2011.

[36] Rashid Javanshir, the President of BP Azerbaijan announced on 30 November 2011 that the BP-led Shah Deniz consortium will invest up to $3 billion in the upgrading of the main gas trunk pipeline that connects Baku via Tbilisi to the north-eastern Turkish city of Erzurum. The gas pipeline, which extends for over 700km from the Sangachal Terminal to the Erzurum dispatching centre of the Turkish NGTS (National Gas Transmission System), has a maximum throughput capacity of 8 bcm/y. This capacity would have to triple to 24 bcm/y in order to accommodate the 16-17 bcm/y of Shah Deniz Phase 2 that would be exported to Turkey (up to 7 bcm/y) and via Turkey to Europe (10 bcm/y). Javanshir said that the $3 billion is part of the overall investment budget for the development of Shah Deniz Phase 2, which is estimated to reach around $20 billion. The expansion of the existing gas infrastructure will also include the construction of around 400km of new parallel and feed-in lines to the main Trunkline, including as Javanshir noted, "the extension of the Sangachal Terminal and [the] construction of two new compressor stations of in Georgian part of pipeline". *Trend News Agency*, 30/11/2011. The plan also includes around 500km of underwater pipeline linking the fields with the expanded Sangachal terminal.

[37] "DEPA Forges Strategic Partnership With Turkey And Azerbaijan", Interview of Harry Sachinis with Theodore Tsakiris, *Middle East Economic Survey*, 28/06/2010.

the prospective Iraqi gas resources. This rerouting, which was made in order to avoid taking Iranian gas, is expected to increase the length of the project by 550-600km, even though neither Mitschek nor Dolezal, Nabucco's senior spokesman, were able to give an estimate of the expected cost increase. Mr. Dolezal told *Trend News* on 21 February 2011 that "The investment costs of 7.9 billion euro are based on the feasibility study. Any other figures released in the meantime are speculations and not accurate".

(ii) On 1 March 2011, BP Azerbaijan announced that the Shah Deniz development partners and SOCAR, have concluded an agreement that extends the life of the 1996-concession by five years from 2031 to 2036. This extension was necessary to guarantee that the consortium members, which include operators BP (25,5%) and Statoil (25,5%), will be able to mobilize the needed capital to develop Shah Deniz Phase 2, which is estimated to increase production by 16-17 bcm/y by 2020. In 2010 Shah Deniz produced 6.9 bcm/y even though it has a peak production capacity of 8.9-9 bcm/y for Phase 1.

The extension of the concession became unavoidable after Turkey and Azerbaijan squabbled for almost two years before they reached an agreement regarding the volumes, prices and transit terms of Shah Deniz 2 production, an agreement that was finalized as late as October 2011. As early as 2008, Shah Deniz 2 was expected to start production by 2013-2014, a date that has been pushed back considerably to 2017-2018. The extension of the contract is also another indication that the Azeris are approaching their decision time on the winner of the ongoing tender for the 10 bcm/y from Shah Deniz 2 which will transit via Turkey to Europe. ***The extension of the PSA contract signalled to Nabucco that the consortium would not welcome any additional deadline extensions on the project's implementation timetable like the one Mitscheck announced on 18 February 2011***.

(iii) On 17 March 2011, Shah Deniz Stage 2 operator BP informed the consortia competing for Southern Gas Corridor supplies that they should submit by 1 October 2011 their final transit tariff cost estimates for the delivery of the 10 bcm/year available for export to Europe via Turkey. BP's deadline –which was confirmed by SOCAR in early May- pushed back by 90 days the final deadline initially set by the Azeri government for June 2011,[38] ***but it was still ahead of the December 2011 deadline extension originally requested by the Nabucco partners so as to coincide with their recently updated timetable***. BP Azerbaijan Vice-President and the consortium's senior officer in charge of Shah Deniz Phase 2 Development, Alasdair Cook, told a conference in Ankara in mid-March 2011 that an October deadline would allow the Shah Deniz consortium to take its final investment decision in 2013 so as to be able to ship the early gas volumes to Europe by mid to late 2017. The BP move coincided with an announcement by SOCAR's President Rovnag Abdullayev that the final purchase and transit agreement between Azerbaijan's SOCAR and Turkey's Botas on Shah Deniz supplies and transit tariffs would be signed by late 2011, as indeed were in October 2011.

Instead of trying to meet the SD deadline and attempt to modify its own cost estimate, Nabucco strategists moved in the exact opposite direction by introducing plans that would increase the project's cost way beyond BP's February 2011 estimate of EUR 14 billion. What is even more surprising for Nabucco is that its strategists decided to do so in a manner that directly antagonized the very existence of the South Caucasus Pipeline and the SD2 plans regarding its expansion to approximately 20-22 bcm/y.

A few hours after the announcement of the October 1st deadline by Alasdair Cook, Jeremy Ellis, Head of Business development for RWE Supply and Trading, said to the delegates of an international energy conference held in Ankara, that the consortium was considering expanding the pipeline from the Turkish-Georgian border all the way to the Azeri capital, thereby making it unnecessary for the Shah Deniz consortium to upgrade the capacity of the South Caucasus Pipeline (SCP), which connects Baku to Turkey's Erzurum. The Shah Deniz consortium has plans to expand SCP's capacity from its existing 8.8 bcm/y to 20-22 bcm/y, while also constructing a new smaller gas pipeline that could accommodate future Azeri exports. SCP's current capacity is almost 100% utilized and would have to be expanded significantly if it is able to transfer the additional 17 bcm/y that will be produced from Shah Deniz Phase 2.

[38] The June 2011 deadline was originally set by Nassirov. See Nassirov's interview in *European Energy Review,* op.cit.

Mr Ellis said that Nabucco would emerge as a "one stop pipeline," connecting Baku with Baumgartern, thereby offering suppliers less complexity and secure transit, especially Turkmenistan, while together with the existing SCP the extension would create multiple export pipeline routes from Azerbaijan. Mr Ellis also noted that "We [Nabucco] have been thinking about this and designing it for some time, but we needed to get some momentum going first…If SCP is expanded only for the sake of Shah Deniz 2 gas, [then] what happens?" he asked, referring to the fact that the SCP, now capable of shipping around 9 bcm/y, will have a capacity of 20 bcm/y – enough only to accommodate Shah Deniz Stage 2 gas – after SD2 related upgrdes are completed.[39]

The Nabucco extension – identified as 'NaBaku' in Mr Ellis's presentation – and the SCP will give Azerbaijan "strategic optionality," he said. "Given now that the gas picture is where it is, the Azeris must be concerned that their next generation of projects may not have room in Nabucco," Mr Ellis said. "By taking the pipeline to the wellhead, it allows for a much safer alignment and security of transit for all of us." He added that the Nabucco extension to Baku helps the strategic interests of both Azerbaijan and Turkmenistan. "There appears to be a concern from the Turkmens about capacity to transit through Azerbaijan and Georgia," he said. "By extending Nabucco we can eliminate those concerns."[40]

The announcement that Nabucco will become NaBaku –***without of course proposing any cost estimate for this huge extension- essentially attempts to dictate to Azerbaijan its final decision not only on the desirability but –more importantly- on the programming of a major Turkmen transit via Baku***. As Nassirov had clearly noted since 15 November 2010, Azerbaijan does not need to wait for the Turkmens to make up their minds or resolve the Serdar/Kyapaz dispute in order to take its own decision on the 10 bcm/y of Shah Deniz 2.

(iv) On 26 March 2011 BP gave its strongest indication that it had decided to "drop" Nabucco. Iain Conn, BP's chief executive for refining and marketing told an international oil & gas conference held in Brussels on 26 March that the SD consortium, would prefer a scalable pipeline project that would best serve the needs of Azerbaijan's medium-term export potential vis-à-vis Europe. "We are going to build a 10 bcm line into Europe that's expandable. We've got to stop being preoccupied by the word Nabucco". ***Instead of considering the repercussions of such a statement Nabucco's strategists decided to further undermine their comparative position vis-à-vis both TAP and ITGI by announcing yet another delay in their implementation timetable***.

On 6 May 2011 Reinhard Mitschek announced that the consortium has decided to delay its investment decision, which was expected in the 3Q or 4Q of 2011 for at least one year noting that the construction of the pipeline could start in 2013 with the aim of transporting its first gas volumes in 2017. Yet this may not be the last postponement for the project since Mitschek underlined that "The Open Season process will start as soon as there are firm indications that gas supply commitments are in place". Nabucco's CEO refused to give a specific timetable on the availability of such supply commitments even though it is unlikely for Nabucco to secure any gas supply contracts from either Turkmenistan or for that matter Iraq within 2012. Mitschek also said that Nabucco is open to linking up with competing projects, but that Nabucco remains "the backbone" of the gas line that would connect the European Union to the Caspian Sea Region. Nabucco planners have been extremely lukewarm to announce the new cost of the project despite estimates calculated by senior BP officials over the last two months which indicated a sharp increase in the EUR 7.9 billion cost projection that dates back to 2005.

Yet on 9 May 2011 none other than EU's Energy Commissioner, Günter Oettinger who was perceived to be among Nabucco's most fervent supporters, publicly noted during a conference held in Stuttgart that the actual cost of the project is likely to range between EUR 12-15 billion. Christian Dolezal, Nabucco's Press Secretary, told *Trend News Agency* on 7 May 2011 that "the cost of the Nabucco project is under consideration, and the results will be based on facts. At the same time, the publication of any other data is speculative and inaccurate". ***The fact that Nabucco indirectly branded Commissioner***

[39] "Deadline Set For Competing Gas Corridor Projects, Nabucco Plans Extension", *Middle East Economic Survey*, 28/03/2011.
[40] *Ibid*.

Oettinger as making speculative and inaccurate statements is highly indicative of the project's difficulties.[41]

Two months after the expiry of the deadline (1 October 2011) set by the Shah Deniz 2 joint venture to evaluate the proposals of the four joint ventures vying for the transit of 10 billion cubic meters of natural gas per annum with which the Southern Gas Corridor of the E.U. will be inaugurated, a series of important developments clearly signify that we have entered the final phase of this over-celebrated "war of the natural gas pipelines". ***None of them seem to augur well for Nabucco's future, at least not in its present form as an independent Asia-Europe gas transportation system***. These developments may be summarized by the following points:

(a) The finalisation of intergovernmental agreements between Turkey and Azerbaijan regarding the transport of 10 billion cubic meters/ year (bcm/y) through Turkish territory on 25 October 2011. These agreements guarantee the terms of transit for all three competing pipeline consortia while simultaneously securing an additional 6 bcm/y for the medium-term needs of the Turkish economy thereby allowing Ankara to significantly diminish its imports dependency on Russia's Gazprom by not renewing its 25-years gas supply contract through the soviet-era western Balkan pipeline.

(b) The announcement on 02 November 2011 by the vice president of SOCAR Mr. Elshad Nassirov and its confirmation by the minister of Energy of Azerbaijan Mr. Natik Aliyev himself on 18 November 2011, of the decision by Turkey and Azerbaijan to proceed with the construction of a new pipeline called TANAP (Trans Anatolian Pipeline) *with a minimum export capacity of* 16 bcm/y that basically duplicates the planned Nabucco route. (*Middle East Economic Survey,* 28 November 2011). This Nabucco replacement that will link with Shah Deniz's own export infrastructure in Erzurum, the point where the existing SCP (South Caucasus Pipeline) connects with the Turkish NGTS (Natural Gas Transportation System), will be constructed in case -which is the most probable- that Turkey's NGTS will not be able to secure enough spare transportation capacity for servicing the aforementioned 10 bcm/y (or for that matter their expansion to 20 bcm/y as Shah Deniz and SOCAR desire via their scalability criterion).

There is of course the option of upgrading the transit capacity of the Turkish NGTS without resorting to the construction of an entirely new pipeline, but on any case this does not spell good news for Nabucco, since Nabucco's construction was not dependent on the upgrading of the Turkish NGTS. One of its major advantages vis-à-vis ITGI and TAP was that it was not dependent on the upgrading of the Turkish NGTS to transport the Shah Deniz exports to Europe. *Now that Turkey and Azerbaijan guarantee the upgrading of the Turkish NGTS through the addition of new compressors or even the construction of an entirely new pipeline, Nabucco's last advantage vis-à-vis TAP and ITGI has been effectively eviscerated*.

(c) The disclosure at an international conference that took place in Istanbul on 18 November 2011 of the intense doubts entertained by the Azeri Energy Minister Mr. Aliyev regarding the realization of the Nabucco project. The high-ranking Azeri official and former president of SOCAR made it clear that Nabucco will be built "once all of Azerbaijan's gas production projects, including Shah Deniz II and Absheron, are fully launched, as well as gas from third countries such as Turkmenistan comes on stream". Then, Mr. Aliyev emphasised, "Nabucco could be the best option".

The problem for the Nabucco's planners, as Aliyev underlined is that Nabucco has too big a capacity and is too expensive to be realized without the supply of at least another 10 bcm/y from an additional source *beyond* Azerbaijan. As Aliyev himself stated "We believe that apart from Nabucco, which has certain elements of uncertainty about the timeline of its development, there are other projects that can be seen as attractive. First of all these are the Trans Adriatic Pipeline and the Interconnector Turkey Greece Italy pipeline and other projects of more local character [e.g. the South East Europe Pipeline (SEEP) of BP]." (*MEES,* ibid)

The real question now is no longer whether Nabucco remains –**in its original plan-** as the strongest candidate for Shah Deniz 2, but which among the two smaller –more pragmatic- projects are more in synch with

[41] "Nabucco Announces Further One-Year Delay, Construction Now To Start In 2013", *Middle East Economic Survey,* 16/05/2011. Oettinger repeated his EUR 12-15 billion cost estimate during a speech in Berlin on 29 August. "EU's Oettinger Backs Nabucco Gas Pipeline, Sees Improved Prospects", *DowJones,* 29/08/2011.

the strategic priorities of Azeri strategies and the commercial necessities of the Shah Deniz consortium. ***The most probable answer is that a functional merger between TAP and ITGI –even if Albania is included- would be able to give Nabucco the final coup de grâce while making sure that Greece will emerge as the irreplaceable transit state for the implementation of Phase I in Europe's Southern Gas Corridor Strategy. Even a completely new Nabucco project running from European Turkey to Baumgarten would still be significantly more expensive than TAP's EUR 1.5 billion. The emergence of the SEEP project –which has nevertheless remained rather nebulous- does not appear to be radically challenging this conclusion.***

3.3. The South East Europe Gas Pipeline Project: BP's Fourth Export Alternative

Less than a week before the October 1 deadline expired for the submission of the comprehensive bidding proposals regarding the export of 10 bcm/y to Europe from Shah Deniz 2, BP, which is also the project's operator, revealed the existence of a fourth export option beyond the vying Nabucco, ITGI and TAP pipelines. BP's South East Europe Pipeline or SEEP project, which is 1,300-km long and aspires to copy Nabucco's route from European Turkey to Baumgarten will be tailored to a net export capacity of 10 bcm/y that will probably be scalable to 20 bcm/y in order to allow for the increase of future export capacities once additional Azeri gas becomes available by the early 2020s from the development of new fields in offshore Azerbaijan. A Spokeswoman for Azerbaijan BP Tamam Bayatly told *Dow Jones Newswires* on 27 September 2011 that "While this is not an advanced project, this is a possible export solution. The three pipeline projects will submit their proposals by October 1, and in parallel there is a fourth possible option that will be looked at" she added. BP's belated entry in the Pipelines Game surrounding the Shah Deniz 2 Gas and the much celebrated Southern Gas Corridor Strategy of the European Union has created a stir among its competitors. Even though few of them might have actually been surprised almost all of then, have a series of questions regarding the project's viability. Al Cook, BP's vice-president for Shah Deniz development, described the 10 bcm/y project as "another possible solution" while noting that "it doesn't follow from this that we necessarily find flaws in the three offers.

But it is wise to have another option on the table".[42] Indeed, BP's last-minute proposal raises some serious questions regarding its credibility. What would be the cost of the project? Will it be an independent pipeline system the likes of Nabucco or will it use existing gas export infrastructure that connect or are in the process of connecting the markets of South Eastern Europe with the main Central European hub in Baumgarten. How will these 10 bcm/y be divided between the transit states in Bulgaria, Romania and Hungary and if BP intends to get only 5 bcm/y to Baumgarten will this make any economic sense for the transit states to bear an equal share of cost in order to get the same gas volumes they could get via Nabucco *even* if they were to get it at a reduced investment cost of 66%?

[42] David Blair, "BP Plans Gas Pipeline to Europe from Azerbaijan", *Financial Times,* 26/09/2011

Source: *Financial Times,* 27/10/2011

If BP opts to build an independent gas system then it would have to go through a strenuous regulatory approval process within the EU states in order to secure all the necessary permits. These permits are extremely difficult to get in time even if the bureaucracies of the involved states *want* to support the materialization of the project. BP should provide the transiting states with the necessary incentives in order to get through the permitting process unscathed and that means giving them an equal share of the project's benefits both in gas and in rates of return. *The problem with these incentives is that these IMF-supervised states, save Turkey, will have already spent by 2014 several tens of million EUR in order to integrate their gas markets and pipeline systems through the construction of several 3-5 bcm/y interconnectors, despite the fact that they are all 1/3 financed by the European Energy Programme for Recovery. The 3-5 bcm/y Interconnector between Romania and Hungary was commissioned in October 2010.*

If BP wants to bring around 5 bcm/y to Baumgarten then it would probably have to sell 1-2 bcm/y to Bulgaria, 1 bcm to Romania and another 1-2 bcm/y to Hungary. One major problem for BP is that the infrastructure for the satisfaction of the national gas needs for Bulgaria, Romania, and Hungary would be already in place 3-4 years *before* the beginning of production in Shah Deniz Phase 2. ***Why should these four states spend a single cent to construct a pipeline they would already have by late 2013? Why should they also have to wait until 2017 to get Shah Deniz Gas when they can cover their long-term gas needs by securing Arab or Israeli LNG imports once the IGB is completed thereby eliminating BP's market altogether?*** In addition to that, BP would have to build an entirely new 10 bcm/y pipeline between Turkey and Bulgaria, a prospect that would cost at least EUR 600-700 million since the TGI (Turkey Greece Interconnector), which is a shorter 3 bcm/y capacity pipeline, cost around EUR 300 million to construct in 2007. *That is primarily why a SEEP option that reaches Baumgarten with an export load of merely 5 bcm/y, may be as economically unattractive as building Nabucco at a 50% throughput capacity*.

The Fifth Option: Balkan Entente?

There is of course another solution for Shah Deniz and one BP is more likely to choose if it were to actually follow its so-called "minimum built" criterion. This solution excludes the transfer of SD2 gas to both Southern Italy and Baumgarten and reserves it for the requirements of the regional market that mostly needs it: that is South East Europe itself. Instead of overlapping with the aforementioned interconnectors and construct an entirely new system from Eastern Thrace to Baumgarten, BP could try to utilize them. In that case it would also need to think of the Greek market which is (since 2007) already connected with Turkey and will be (by late

2013 or early 2014) connected with the Bulgarian market via the IGB pipeline. Greece is also the only EU client of Azerbaijan, while SOCAR is among the front-runners for the privatization of Greece's Public Gas Company or DEPA which controls 1/3 of the IGB and 50% of the IGI/Poseidon project.

Moreover, despite the doom and gloom perception on the Greek economy, natural gas demand will almost double by the end of the decade due to the completion by 2014-2015 of several new CCGT power plants currently under construction by private developers and the implementation of a long-term programme on behalf of the Greek State-owned Public Power Company (PPC or DEH) that aspires to replace by 2020 all of Greece's old lignite-fired power plants with new gas-fired units. That means that the Greek market will expand far faster and far deeper than i.e. Bulgaria and could reach, according to DESFA, a consumption level of up to 7 bcm in 2020.[43]

If BP chooses not to ignore Greece and reserves for Greek importers the right to import at least 1-2 bcm/y of SD gas via the ITG, then BP cannot possible expect to get 5 bcm/y to Baumgarten. ***A much more logical option for BP would be to keep the 10 bcm/y within the Balkan markets and completely forsake the Baumgarten hub but that is not necessarily Statoil's or for that matter SOCAR's preference.*** The most logical option if BP wants to construct *SEEP* with the minimum cost would be to utilize both the ITG and IGB, sell 1-2 bcm to Greece, Bulgaria, Romania and Hungary and then get around 2 bcm/y to Hungary which could be subsequently sold to either Austria or Croatia *via the existing interconnections*. It can also use the future Serbian-Bulgarian interconnector (IBS) which will also be 30% financed by the European Commission to send another 1-2 bcm/y to Serbia thereby ending Russia's monopoly control over its gas imports. The IBS will be completed by 2015, while the IHC (Interconnector Hungary-Croatia) has already been operating since December 2010.

That is indeed a different plan that transports no gas to Baumgarten, but utilizes with a minimal investment cost existing interconnectors between Turkey-Greece-Bulgaria-(Serbia)-Romania-Hungary and (Croatia) in order to almost evenly spread the 10 bcm/y of SD2 gas within Southeastern Europe without having to reach the bigger central European consumers. Moreover the net long-term price of gas in the far less liquid and liberalized Balkan Gas market may be higher than the end price in Baumgarten or for that matter Italy, and this is something always important from an exporter's point of view. However it is questionable if either BP's SEEP or this "Balkan Entente" version can adequately meet the Shah Deniz 2 consortium's scalability criterion and –more importantly- the timetable of SD2 own development. If Umid Babek, BP-operated Shafag-Ashiman and Total-operated Absheron were to start producing a cumulative 10 bcm/y by the early 2020s then would the abovementioned South East European markets be able to absorb these increased volumes? The answer is probably not.

How could then one fulfil Azerbaijan' scalability criterion for post Shah Deniz 2 exports since it would need to build-up (beyond Turkey) a second Eastern Balkan-10 bcm/y capacity system (for post SD2 volumes), given the fact that the maximum capacity of the existing/planned Balkan interconnectors does not exceed 5 bcm/y? *If SOCAR, is keen, especially for political reasons, to establish a strong and more importantly an expandable foothold in the European gas market, it would be able to better achieve that goal if it reached either Baumgarten or Italy, as soon as possible.*

Finally, and most importantly, the infrastructure necessary for the diversification of gas imports for those Southeast European states currently most dependent on a single source, namely the Greece-Bulgaria-Romania-Hungary Interconnectors, will be ready by early 2014 at the latest, regardless of SD2 developments. ***Why would any of these states wait another three years for Shah Deniz 2 gas when they can sign up for Arab or for that matter Israeli (from Tamar field) LNG imports in 2012 and get them delivered via IGB once it is commissioned in early 2014 at the latest? Hasn't Bulgaria signed a MoU with Egypt (April 2009) & Qatar (May 2009) for the import of LNG and another MoU with DESFA (July 2009) in order to reserve***

[43] Dr. George Paparsenos, CEO DESFA S.A, *Greek Natural Gas System: Developments and Prospects,* presentation to the 5th IENE South East Europe Energy Dialogue, Thessaloniki, (June 2011), p.5

specific regasification capacity in the Revythousa import terminal so as to cover its immediate gas needs?[44]

4. Greece's Geopolitical Gains & Losses

As it has already been mentioned, in the European or Balkan sub-region of the Greater Black Sea Area a diminishment in the relative energy security position of a state actor is unlikely to translate to an immediate national security risk and thereby increase the probability for the use of force both between and within states.

But how is energy security perceived by the states of South Eastern Europe that has emerged as the unavoidable transit area for all three competing pipeline projects vying to secure the 10 bcm/y of Shah Deniz gas, which will flow to Europe via Turkey at around 2017? For Southeast European states energy security is no longer perceived as a zero-sum game because of the region's increased political stability and deepening economic cooperation that spearheaded -throughout the 2000s- its strategic reorientation towards integration with the European Union and NATO.

Even the prospect of EU membership, no matter how long-term, has offered a critical layer of political stability, which was further enhanced by the presence of European police and security forces in Bosnia and Kosovo respectively that has helped to keep the incomplete peace of the Dayton Accords while sustaining a cocoon of *de facto* independence for Kosovo. This does not mean that the region's political volatility has been eradicated.

It does mean though that the European presence –and equally importantly- the prospect of EU integration have played a critical role in neutralizing that volatility. Consequently any serious step backwards that would challenge this fundamental reorientation of the region's policies and politics towards a Euro-Atlantic future would have not merely economic but also political repercussions, which could easily spill-over into the EU in the form of yet another post-Yugoslav crisis thereby destabilizing the entire region, a prospect that Greece has actively tried to deter by championing the enlargement of the EU into S.E.E. throughout the last fifteen years.

One of the means in Greece's efforts was to spearhead the establishment of the Energy Community Treaty Organization (ECTO) in 2005 which facilitated the eventual integration of Bulgaria and Romania into the EU two years later. The Treaty establishing the Energy Community was utilized by the European Commission as a tool of establishing energy interdependence as a basis of economic and political integration.[45] Energy as a backbone of economic development and political integration plays a major role in consolidating the region's European vocation while it is also emblematic of the way the EU's involvement in the region has transformed the strategic parameters of regional energy geopolitics from a zero sum-game to a more cooperative mentality.

As a result, *energy security in the region does not necessarily create an atmosphere of renewed antagonism that would equate to a continuation of the Yugoslav wars by other means, in this case oil & gas pipelines*. This does not mean that there are no relative-gain and loss concerns between former and even current geopolitical adversaries. Indeed there are. *What is important to note is that institutional footprint of the EU and what it holds for the region's future has transformed energy geopolitics to a contributing factor of political stabilization and economic integration.* Thanks to this reality, energy security for the states of Southeast Europe is basically composed of two principal considerations: (a) the security of energy supply that is primarily achieved via oil & gas import diversification strategies as well as the heretofore lukewarm development of indigenous hydrocarbon resources and (b) the geopolitical utilization of any country's participation in major oil & gas infrastructure projects connecting several regional players as a means of promoting it European vocation, namely its usefulness in EU "eyes".

[44] Dr. Theodore Tsakiris, *Blue Gold: Russian-Ukrainian Relations and the European Natural Gas Strategy,* (in Greek), (Papazisis: 2011), p.281 & "I.G.B. Pipeline Company Established by Edison, DEPA and BEH", *Middle East Economic Survey,* 15/03/2010, p.12.

[45] ECTO also includes four states as observers, Turkey, Georgia, Moldova, Ukraine and Norway. On September 2009 ECTO started accession talks with Turkey and on October 2009 completed accession talks with Moldova and Ukraine that are expected to be formally admitted in the ECTO by December 2009. On the historical development of the ECTO via the Athens Process Memoranda of 2002 and 2003, http://www.energy-community.org/portal/page/portal/ ENC_HOME/ ENERGY_COMMUNITY/ Process. (accessed 09/11/2009).

These projects, such as the ITGI, Nabucco, South Stream, SEEP and Trans Adriatic gas pipelines, regional LNG (Liquefied Natural Gas) projects in Croatia, Albania and Greece could offer to the involved states not only the promise of import diversification, which is of paramount importance for their own energy security needs, but also the benefit of acquiring political capital vis-à-vis its neighbours and vis-à-vis their ultimate goal of being incorporated into the Euro-Atlantic institutions and in particular the European Union. What is important to note though it that this capital is not spent within an antagonistic but in a synergetic framework.

These mega-infrastructure projects also operate as a catalyst for political reconciliation and rapprochement between the Eastern and Western parts of the Balkans by forging powerful bonds of mutual interest. These projects create relationships of economic and political co-dependencies that accelerate the regional integration and liberalization of energy markets- a principal EU objective- not only between the regional states themselves but also between the regional states and the European Union itself.

What is important to emphasize is that despite the fact that SEE as a whole could operate as a major transit hub for the transport of Russian, Caspian and in the medium-term, Middle Eastern, hydrocarbons to Central Europe, the pipeline projects do not contribute to the political destabilization of the region and do not hinder its potential integration into the European Union.

The expansion of ITG's capacity within the framework of materializing the ITGI or TAP projects will only add to the geopolitical gains for *both* Greece and Turkey and expand the economic dynamic of the overall rapprochement between the two states. Greece currently imports via Turkey 0.75 bcm/y. Even if these imports increase to over 2-2.5 bcm/y by the end of the decade, accounting for more than 1/3 of Greek demand (6-7 bcm/y) in 2020, Greece, as it has clearly manifested by its management of the Russian-Ukrainian crisis of January 2009, can replace its entire gas consumption via extended LNG imports.[46]

This flexibility makes it extremely difficult for any Turkish government to disrupt the flow of gas to Greece on political grounds for the added reason that it would also incur the wrath of the exporting state, and in this particular instance Azerbaijan, whose revenues would decline as a result of a theoretic Turkish pipeline embargo against Greece. Moreover, the expansion of Greece's existing storage capacity to 220,000 metric tons in its sole LNG liquefaction plant that is located on the island of Revythousa, near the port city of Megara, would significantly increase Greece's security of supply margin and would be available before 2015.[47] In any case the construction of TAP is not likely to increase the country's dependence on Turkish transit.

The original agreement on the construction of the ITGI project called for the consumption of up to 1-2 bcm/y of Azeri gas in Greece and the transfer of the remaining 8 bcm/y to Italy, even though Bulgaria's participation in the IGB project will most likely guarantee that at least 1 bcm/y of the 7 bcm/y initially earmarked for the Italian market would go to Bulgaria. It is unlikely that the TAP project would not make similar arrangements for Greece and to a secondary degree for Bulgaria if TAP wins the Shah Deniz 2 tender. In any case, if TAP wins the SD2 tender it should seriously consider the inclusion of a Greek private or state gas company/entity as a partner.

It should also be noted here that the construction and operation of the IGB pipeline through which Bulgaria desperately wants to decrease its complete import dependence on Russia is not necessarily related to the Shah Deniz 2 tender, in the sense that the pipeline can run on a commercial basis several years *before* Shah Deniz gas flows through Turkey to Europe. The IGB network to Hungary can also be utilized as a means of accelerating the transfer of Arab, Cypriot or Israeli LNG to these states. These LNG sources, especially the Arab/Qatari one, would be available once IGB is commissioned and thereby eliminate the commercial underpinning of the SEEP project that in its current form appears to be completely disregarding Greek interests.

Azerbaijan's Energy Minister Natiq Aliyev has made it perfectly clear as early as June 2010 that SOCAR would want to use the existing ITG infrastructure and the prospective network of East Balkan Interconnectors, namely the IGB, IBR and IRH gas pipelines, in order to reach additional markets in South East Europe *regardless* of which pipeline project wins the Shah Deniz 2 tender.[48] It is not in TAP's interest to disregard Bulgarian needs

[46] For the Greek management of the January 2009 crisis, see Theodoros Tsakiris, *Blue Gold,* ibid, pp. 120-121. For the projection of Greek demand in 2020, Paparsenos, *ibid,* p. 13.

[47] Revythousa currently has a storage capacity of 130,000 metric tons. Its expansion is expected to be completed by 2015 at a cost of EUR 159 million. It would allow for Revythousa to correspond to Greek demands for a total of 28 days compared to its present capacity of 18 days. Paparsenos, ibid, p.18.

[48] "Aliyev Shifts Azerbaijan's Gas Focus to Smaller Projects", *Middle East Economic Survey,* 07/06/2010

and forsake the utilisation of the IGB infrastructure in case its capacity is still available by 2017-2018 when SD2 gas will start flowing towards Europe.

Concluding remarks

Greek foreign policy makers will function, at least for the near future, under the Damocles sword of the country's economic crisis. This imposes a number of constraints and limitations. In addition, as key organizations such as the EU and NATO are changing in an effort to adapt to new global and regional trends, Greece needs to find its own niche in the distribution of regional roles and convince its partners and allies of its own added value in common endeavours. A difficult task, indeed, for a country with limited resources but the alternative is strategic irrelevance in the wider region. The best option would probably be Greece's active participation to the shaping of the EU's new regional policies, without, however, ignoring the need for national initiatives or the further multilateralization of Greece's foreign policy.

While maintaining and even further emphasizing its European orientation, there is no reason why Greece cannot develop its relations with other major powers, including the US and Russia. Past tensions between Washington and Moscow made it difficult –and politically costly- for countries like Greece to cooperate with Russia on areas of common interest (like energy). The 'reset' in U.S.-Russian relations would probably allow Greece more leeway for energy cooperation with Russia.

As mentioned in various parts of the study, ***energy-related projects can be instrumental in Greece's effort to repair its image, re-acquire a leading regional role, increase its influence and accumulate 'diplomatic capital'. In this context, the Southern Gas Corridor can play an important role. Unfortunately for Athens the decision for the pipeline route was not taken by Greece. Despite Greece's initial preference for ITGI, once Shah-Deniz decided in favour of TAP the Greek government must immediately embrace the project and facilitate its completion at the earliest possible time [and, of course, under the best possible conditions for Greek interests]. Otherwise, the final decision of Shah-Deniz will be in favour of either Nabucco or SEEP. To prevent such a development, an active diplomatic effort, on the basis of close coordination and cooperation between the Ministries of Foreign Affairs and Energy & Environment should be undertaken by Greece.***

It should be mentioned that TAP will be crossing Albania before reaching its final destination (Italy), which raises some questions because of various outstanding issues between Greece and Albania which need to be resolved. Although it would be a mistake to underestimate bilateral problems, it would also be wrong to underestimate the common interests and the potential for bilateral cooperation as Albania is, for a number of reasons, an important neighbour and partner for Greece. The potential benefits of cooperation should also be understood and appreciated in Albania, as well.

If TAP wins the SD2 tender, it should seriously consider the inclusion of a Greek private or state gas company/entity as a partner. Greece should also use the IGB network to Hungary as a means of accelerating the transfer of Arab, Cypriot or Israeli LNG to these states regardless of the competition between TAP, SEEP and Nabucco. These LNG sources, especially the Arab/Qatari one, would be available once IGB is commissioned, circa 2013, and thereby eliminate the commercial underpinning of the SEEP project that in its current form appears to be completely disregarding Greek interests.

In addition to the Southern Gas Corridor, ***Greece should try to enlarge its footprint in the energy map through other projects, including South Stream, Burgas-Alexandroupolis[49], as well as the exploitation of potential oil and gas deposits in various parts of the country, notably in Western Greece and the maritime areas to the south of Crete.*** While Greece should continue and intensify its diplomatic efforts for the delimitation of its exclusive economic zone (EEZ) and other maritime zones with neighboring countries, this should not unduly delay efforts to exploit natural resources in the aforementioned areas.

Finally, if technological and financial conditions allow, Greece could also benefit through the construction of a pipeline to transport natural gas from the Israeli and Cypriot deposits in the Eastern

49 *As a result of the recent [December 2011] decision by the Bulgarian government, the proposed Burgas-Alexandroupolis oil pipeline may not be constructed, although Russian sources claim that the project is only temporarily "frozen", a position Greece would obviously welcome.*

Mediterranean through Greece to Western European markets. Such a pipeline project, as well as a Liquid Natural Gas (LNG) alternative, would make an even larger contribution to European Energy security, especially if combined with prospective Greek hydrocarbons production. ***In a very difficult period for Greece, such energy projects provide an excellent opportunity for diplomatic and economic benefits***.

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ELIAMEP can trace its origins to informal meetings in the mid-1980s among academics, diplomats, military officials and journalists. That group's goal was to introduce an independent and scholarly approach to policy options regarding European integration, transatlantic relations as well as the Mediterranean, South-eastern Europe, the Black Sea and other regions of particular interest to Greece. In April 1988 these meetings were institutionalized and became the Hellenic Foundation for Defence and Foreign Policy (Greek acronym, ELIAMEP).

Since its official establishment, ELIAMEP has experienced significant growth and has attracted the attention of scholars, government officials and corporate entities in Greece and abroad. As developments in the wider region moved rapidly, the focus of the institute was enlarged to include more policy-relevant research projects assisting post-communist democracies in the creation of a civil society, providing training and networking services and acting as a contact point to public and private sector bodies on politico-economic and security matters, as well as on European affairs. This was reflected in the 1993 amendment of ELIAMEP's statutes to include a change of name (without abandoning its original acronym), which would illustrate the Foundation's wider scope of concerns and activities: Hellenic Foundation for European and Foreign Policy. The message is clear: in the context of the EU and shared sovereignties, a distinction needs to be drawn between European policy and traditional foreign policy.

Over the years, ELIAMEP expanded its activities to include topics such as migration, human rights, civic participation and social inclusion, climate change and its impact on human security; good governance and security sector reform, and energy security, with a view to having a greater impact on the public through the dissemination of information and of policy proposals, the organisation of training and conflict management seminars and international conferences, the publication of books, journals and monographs. ELIAMEP is frequently visited by journalists from various parts of the world requesting the Foundation's help for information, analysis and interviews. It is now generally recognised as one of the leading think-tanks in the region.

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