



russian analytical digest

www.res.ethz.ch
www.laender-analysen.de

RUSSIA'S ECONOMIC AND SECURITY RELATIONS WITH CENTRAL ASIA

■ ANALYSIS

- Russia and the Central Asian Economies:
From Colonial Subordination to Normal Trade 2
By Martin C. Spechler, Bloomington, Indiana

■ DIAGRAMS

- Central Asian Economies 5
Main Export and Import Partners (2008) 7

■ ANALYSIS

- Turkmenistan's Relations with Russia 10
By Richard Pomfret, Adelaide, Australia

■ DIAGRAMS

- Turkmenistan's Natural Gas Industry 14

■ MAP

- Major Natural Gas Pipelines in Central Asia and Around the Caspian Sea 15

Analysis

Russia and the Central Asian Economies: From Colonial Subordination to Normal Trade

By Martin C. Spechler, Bloomington, Indiana

Abstract

Russia is gradually losing its once-dominant role in Central Asia as the countries in the region build ties with other neighbors. “Staple globalism,” which involves a continued strong role for the state in providing commodity exports and selecting imports of capital equipment and luxury consumer goods, plays a strong role in defining Central Asian trade practices. Ultimately, Central Asia is not an important market for Russia.

Evolving Relations

Since the breakup of the Soviet Union in 1991, the five Central Asian republics have become increasingly independent, both politically and economically. Despite Moscow’s continuing claims of “privileged interest” in this vast area of nearly seventy million citizens, all five regimes have found ways to establish ties beyond the Soviet successor states, while retaining correct and mutually beneficial relations with their former colonizer. Kazakhstan and Turkmenistan have been able to sell their energy resources at world market prices, while importing capital equipment and select consumer goods. Consequently, these petro-states have seen their agricultural and manufacturing sectors stagnate or fail (see Table below). Uzbekistan has grown moderately by exploiting its abundant cotton, gold, and uranium, while keeping state expenditures up.

This foreign trade pattern has been called “staple globalism”. Distinct from true multilateralism, favored by the World Trade Organization (to which only Kyrgyzstan has yet acceded), “staple globalism” involves a continued strong role for the state in providing commodity exports and selecting imports of capital equipment and luxury consumer goods.

The region’s other two states, Kyrgyzstan and Tajikistan, are the smallest and weakest. They have had to depend on remittances, as well as outside aid and protection from international financial agencies and China, along with the Russian Federation, to the extent of the latter’s ability. Yet, in spite of this assistance, their estimated real GDP is still below the 1989–90 level, according to the EBRD. Therefore, since the collapse of the Soviet Union, all the Central Asian Republics have increased their commercial and investment connections with the West and China, at the expense of their former Soviet partners.

Background

From Tsarist times, Russia played the leading role in Central Asia, even before the region’s khanates were

formed into union-republics by the Communist authorities in the 1920s. Nineteenth century Russia controlled these (mostly) Sunni Muslim, patriarchal societies through military government and European troops. Russians and Ukrainians settled in the north Kazakhstanian steppe in particular. The colonizers developed and purchased Central Asian cotton fiber, its oil and natural gas, and its fruits, animal products, and vegetables. During World War II, Moscow built factories in Central Asia in order to produce airplanes and other war materials and sent skilled Europeans to run them, as well as refugees from Nazi invasions.

Besides sizable Slavic populations in the cities, the legacy of this involvement is the role of Russian as *lingua franca* in Central Asia, and access to Russian technical materials. Soviet Russia also promoted technical education and careers for women, secular Marxism, Western dress and material tastes, and hierarchical bureaucracies, all of which persist. Television programming, universities, and the internet continue to ensure Russian influence. Despite efforts to promote national cultures and languages, attitudes towards Russia and Russians remain fairly good, despite bitter memories of the impact of Moscow’s colonization of the region—collectivization of livestock, enforcing a monoculture, introducing alcoholism, and purges of cadres.

Various efforts by Moscow since 1991 to re-establish the former Soviet patterns of economic relations in Central Asia, thus enshrining Russia as the dominant external economic force, have largely failed. All of the newly independent republics remain members of the Commonwealth of Independent States (CIS), which does little but collect data and hold uneventful meetings. The CIS was supposed to retain free trade among the twelve post-Soviet members, but from the start Central Asian states have established border controls and customs tariffs, albeit at lower rates for one another. By 1993 the Russian ruble had lost its

place as the official currency; now each Central Asian state has its own currency, all convertible to some extent. Several efforts to establish Central Asian organizations for economic cooperation have failed to fulfill their grand designs. The Asian Development Bank (ADB) has invested some \$1.8 billion in road reconstruction and other projects, but ADB's prodding has not moved the Central Asian regimes to meaningful integration. The most recent such effort, the Eurasian Economic Community (EurAsEC), sponsored by Kazakhstan's President Nursultan Nazarbaev, has met resistance from Islam Karimov, the Uzbekistan president, and indeed Uzbekistan effectively withdrew from EurAsEC in November 2008. Uzbekistan has also limited its participation in the Shanghai Cooperation Organization, originated by China and joined by Russia and the other Central Asian states, with the exception of Turkmenistan. All of the Central Asian states negotiate commercial deals for energy and investments among themselves and with China or Russia on a bilateral basis, with settlement in dollars or euros. Petty trade in foodstuffs and clothing articles is carried on by shuttle traders and bazaars.

Directions of Trade

Both the size and direction of the Central Asian Republics' external trade are difficult to estimate, owing to their land-locked positions. All must export and import to the West through Russia or the Gulf. For example, Ukraine is listed as Turkmenistan's leading export market for its natural gas, but this is because of a pipeline route, which runs through Russia, via Ukraine, to Europe. Tajikistan sells more to Netherlands and Turkey than to Russia or China, according to the IMF *Directions of Trade* for 2006–08, because of the disembarkation of aluminum ore. Indeed, Kyrgyzstan's second biggest customer is Switzerland! As for imports, Turkmenistan buys most from the UAE, but few of these goods originated there. Kyrgyzstan reportedly imported \$9.3 billion in goods from China in 2008 (but only \$2.4 the previous year), but undoubtedly much of this was re-exported to its much larger neighbors. In spite of some of the counter-intuitive economic statistics emerging about the region, some of the latest figures are revealing.

Kazakhstan is Russia's biggest trade partner; it sends about 10% of its exports (metals, oil) to Russia and imports about one-third of its purchases (\$42.8 billion in 2008, up from \$27.1 in 2006) from the Russian Federation. Kazakhstan with its large ethnic Russian population shares a lengthy border with Russia, so this

is not surprising, though its purchases from Russia may also be exaggerated by re-exporting to the southern tier of Central Asia.

Central Asia has about half the population of the Russian Federation, but its average income per capita in 2007, adjusted for the cost of living, was barely a third of Russia's \$14 thousand (see the Table for purchasing power parity-adjusted figures). Converted at average exchange rates, Russia's national income per capita is about four times higher. So even given the proximity, Russian-Central Asian trade should be relatively small. Indeed, Russia takes only \$10 billion (including transshipment from Ukraine) of Central Asian merchandise out of the \$223 billion it imported in 2007 from all sources—about the same 4% as in the 1990s. Russia possesses many of the same energy and raw materials as their Central Asian neighbors. Of the \$57.6 billion Central Asian imports in 2007, Russia supplied (either directly or trans-shipped) \$18.6 billion in merchandise, or just under one-third. Most of transportation charges are probably included in this total, but other services are poorly registered. China, a relatively recent entry into the Central Asian market, supplied \$10.3 billion.

In sum, we can see that Russia retains a leading, but lately much reduced, role in supplying Central Asia. Why? Russia doesn't offer the best capital goods or the cheapest consumer goods. Russia has had its success mostly in selling arms (at concessionary prices) and atomic reactors. Overall, though, Central Asia is not an important market for Russia.

Under "staple globalism" the Central Asians are selling their cotton and metals elsewhere for hard currency. Until recently Uzbekistan-made GM automobiles that had found strong demand in Russia, but are now being sold elsewhere. At the huge Dordoi market outside Bishkek, goods from China, Turkey, and Europe are sold to Russians, Uzbeks, and Kazakhstanis. Even the natural gas still flowing through existing pipelines is declining in value. Turkmenistan, which has the largest reserves, used to sell almost all of its output to Russia for about \$1 billion a month. But pricing and other disputes interrupted gas exports, which led the Turkmen authorities to open a new pipeline to China via Uzbekistan and Kazakhstan that will eventually carry 40 billion cubic meters (bcm) of gas, a sizable share of Turkmenistan's production. Nonetheless, President Gurbanguly Berdimukhamedov has agreed to contribute gas to the Russian "South Stream" pipeline project, and sales of 30 bcm to Russia will resume in early 2010.

Investments in Central Asia

Because Russia gained massively from the oil boom of 2000–07, its energy giant Gazprom and other state-owned companies were able to announce some investments in Central Asian energy and telecommunication companies. However, construction is slow. For example, the modernization of the Aqtau-Samarqand oil pipeline is “not progressing very fast,” according to a Kremlin source. The long-planned Rogun Hydroelectric Power Plant in Tajikistan has been neglected so far by the Russians, in part because Uzbekistan opposes its use of water needed for summer irrigation. Building work on the Kambarata hydroelectric station in Kyrgyzstan is also on hold. Explorations of gas fields announced may well be delayed, owing to the decline of natural gas prices and Gazprom’s weak finances. In addition, Russian promises to provide loans of \$7.5 billion to the Central Asian states have yet to be fulfilled. Meanwhile, China has lent Kazakhstan several billion dollars and bought into its energy companies.

Effects of Worldwide Slump

The worldwide slump of 2008–09 severely affected the Russian economy and forced a significant depreciation of the *ruble*. Its GDP fell almost 9% in 2009. An immediate effect was on the estimated 2–2.8 million migrant workers from Kyrgyzstan, Tajikistan, and Uzbekistan, who have been employed in Russia or Kazakhstan in the informal economy or seasonal construction. Of these temporary migrants, 18–35% are women, according to Rafis Abazov. Such laborers are particularly vulnerable to illegal exploitation, fraud, and abuse. In addition, the Russian authorities have imposed new restrictions. The decline in oil and gas prices has also affected Kazakhstan, where the construction boom has been halted and two major banks forced into reorganization. Kazakhstan’s *tenge* devaluation in 2009 reduced the value of wages earned by the migrants who still have jobs. These developments have cut remittances to nearby Kyrgyzstan.

For Uzbekistan, the decline of migrant employment abroad is the most tangible result of the worldwide slump. At its peak in 2006–07 approximately 500,000–800,000 Uzbeks worked outside the country, according to the Conference on Labor Migration. Remittances through official channels from Russia were about \$3.3 billion in 2008. Dollar flows led to a boom in apartment prices in Tashkent and other cities, with prices more than doubling. The unexpected worsening of the global economy has suddenly altered this situation. Many Uzbek migrants have had to return to their villages with less cash than they counted on. Access to foreign exchange at Uzbekistan’s banks has been tightened for importers and travelers, actions which have led to a 25–30% premium for dollars on the black market.

While there is little Uzbekistan can do to boost employment of its workers abroad, it is trying to expand its exports. Russia is unlikely to want the additional gas Uzbekistan has offered, so Uzbekistan is trying to diversify its export routes and involve other countries, especially China, in developing its hydrocarbon resources. Its anti-crisis program has added more credit for exporters. Now Tashkent appears to be reaching out to the Europeans as well.

Turkmenistan is the Central Asian Republic that has been least affected by the world economic downturn, as it has also been able to draw on its accumulated reserves to support transportation and communication investments and public salaries.

Conclusion

Russia has lost much of its economic advantages in Central Asia, owing to competition from other countries, the desire for independence in the region, and the admitted inability of the Russians themselves to develop attractive non-energy industries. Russia should therefore expect rising Asian powers and energy-short Europe to gradually increase their economic relations with these countries.

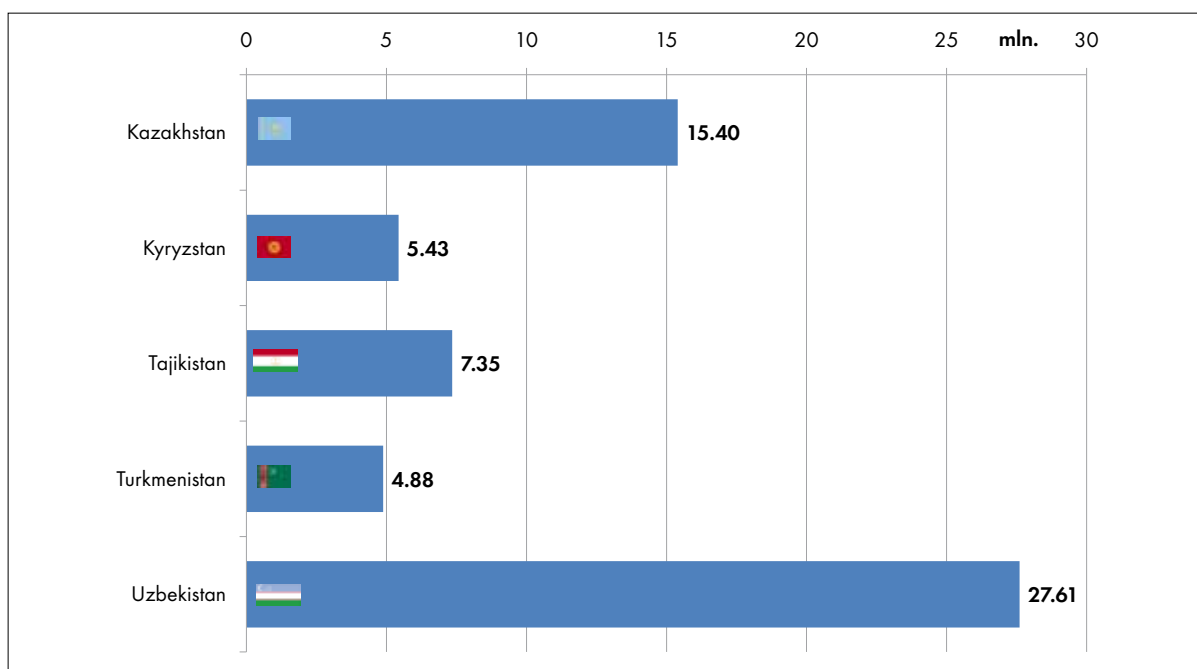
About the Author

Martin Spechler is a Professor of Economics at Indiana University. His most recent book is *The Political Economy of Reform in Central Asia: Uzbekistan under Authoritarianism* (Routledge, 2008).

Diagrams

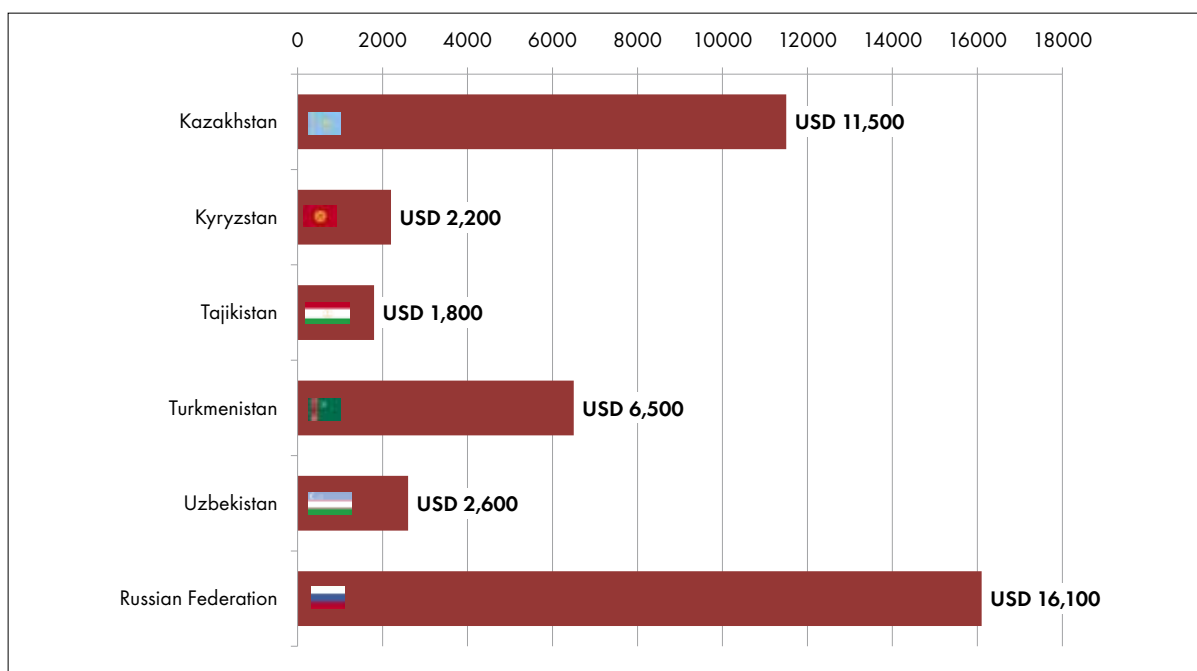
Central Asian Economies

Population (mln., July 2009 Estimate)



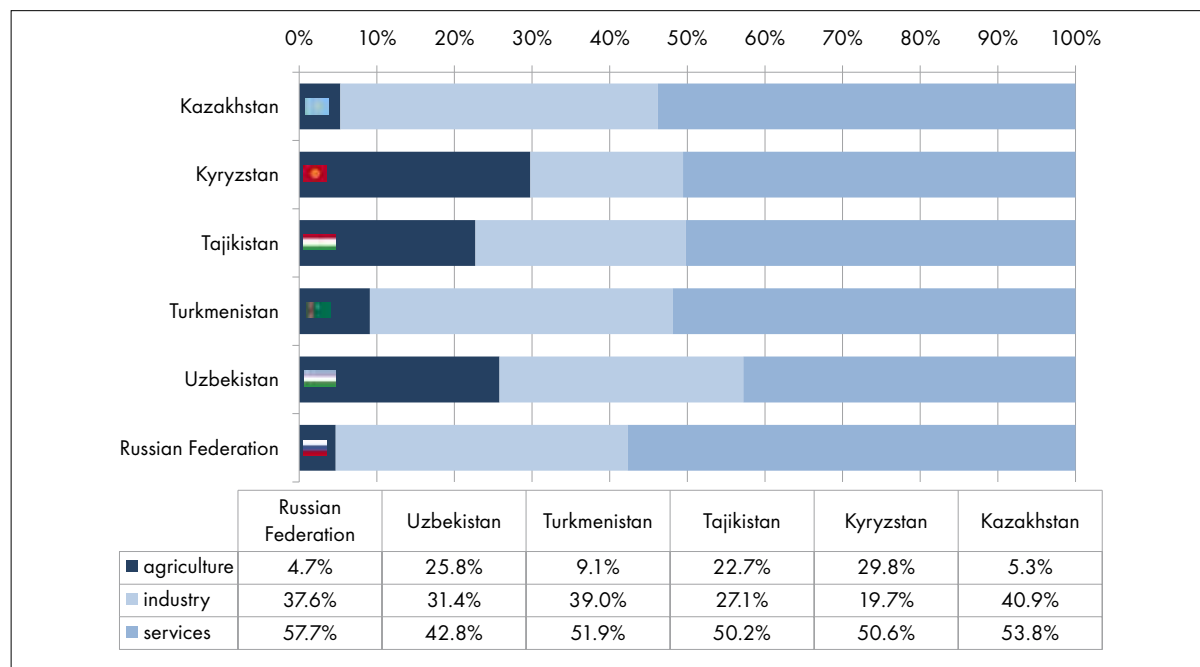
Source: CIA World Factbook, <https://www.cia.gov/library/publications/the-world-factbook/>

GDP Per Capita (PPP, USD, 2008 Estimate)



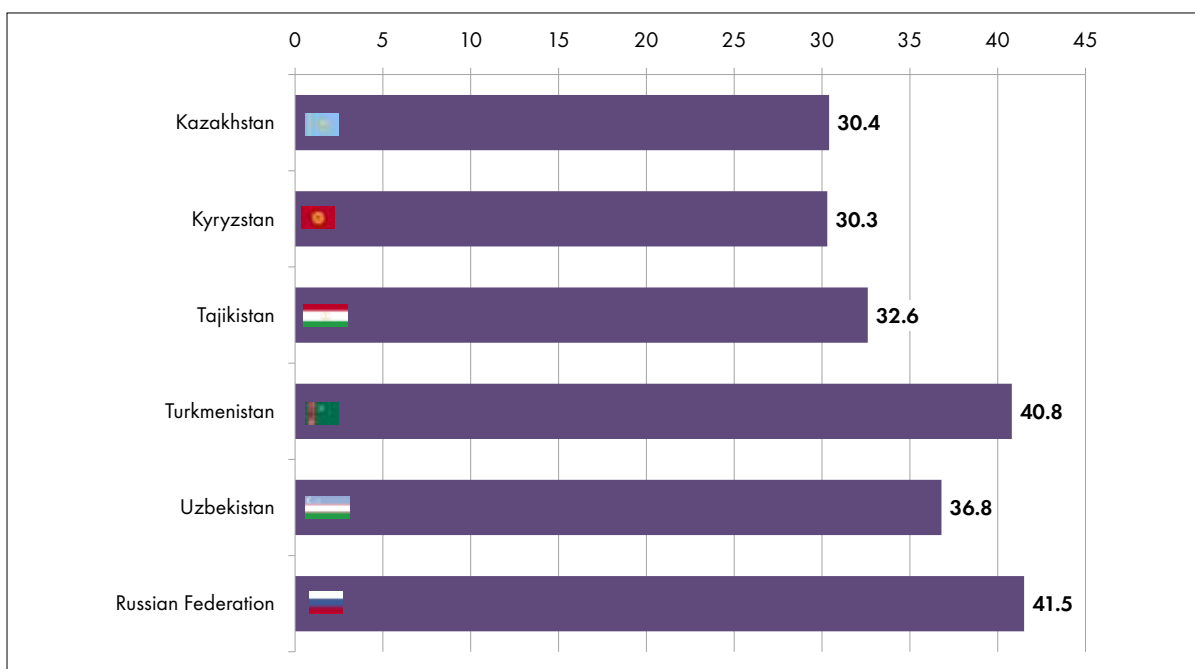
Source: CIA World Factbook, <https://www.cia.gov/library/publications/the-world-factbook/>

GDP Composition by Sector (2008 Estimate)



Source: CIA World Factbook, <https://www.cia.gov/library/publications/the-world-factbook/>

GINI Coefficient

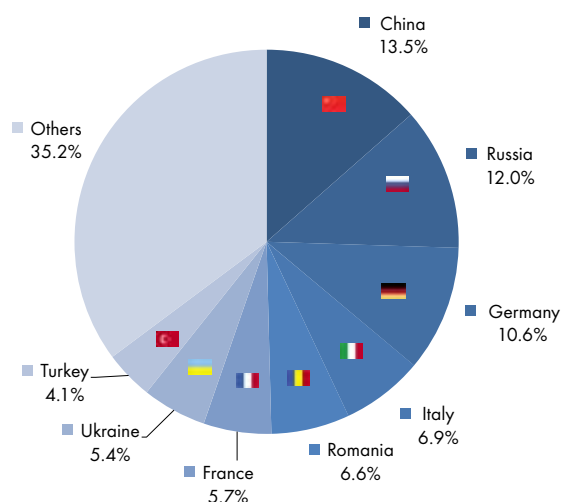


Kazakhstan: 2005, Kyrgyzstan: 2003, Tajikistan: 2006, Turkmenistan: 1998, Uzbekistan: 2003, Russian Federation: September 2008

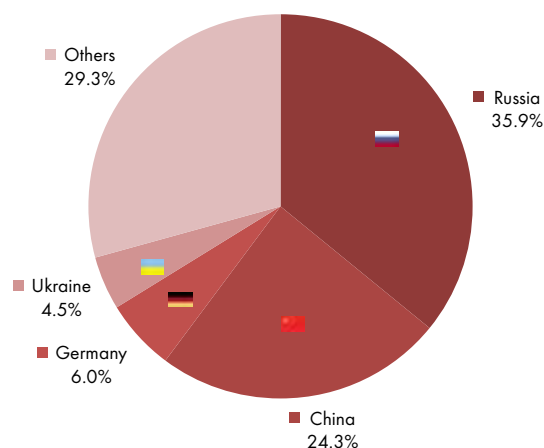
Source: CIA World Factbook, <https://www.cia.gov/library/publications/the-world-factbook/>

Main Export and Import Partners (2008)

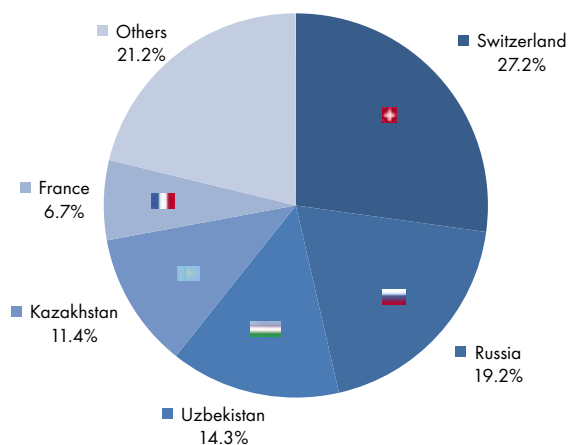
Kazakhstan – Export Partners



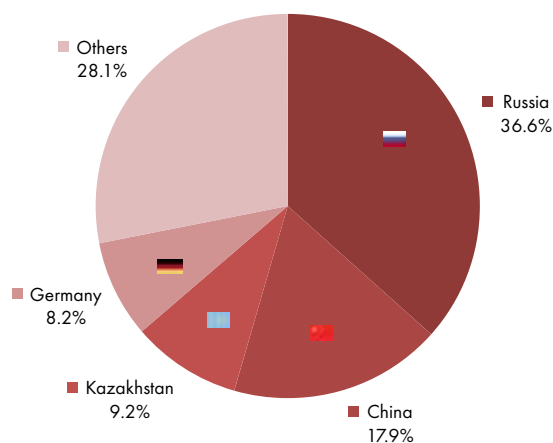
Kazakhstan – Import Partners



Kyrgyzstan – Export Partners

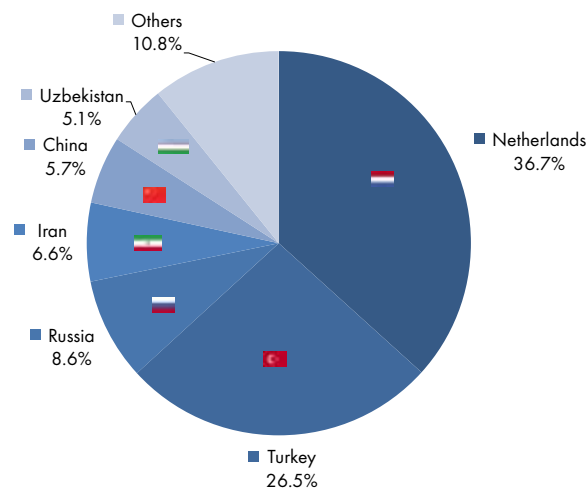


Kyrgyzstan – Import Partners

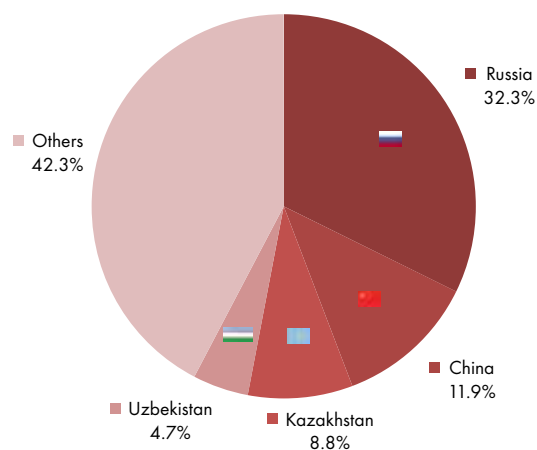


Source: CIA World Factbook, <https://www.cia.gov/library/publications/the-world-factbook/>

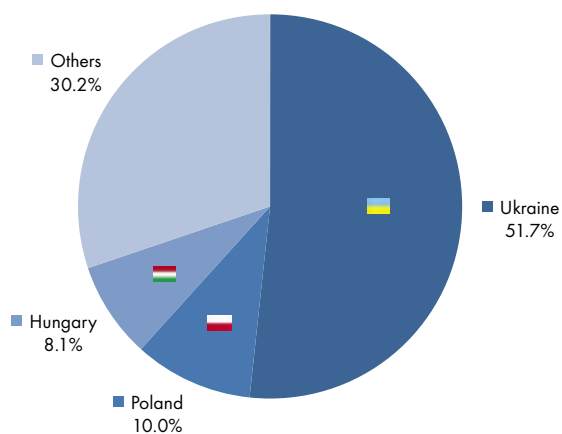
Tajikistan – Export Partners



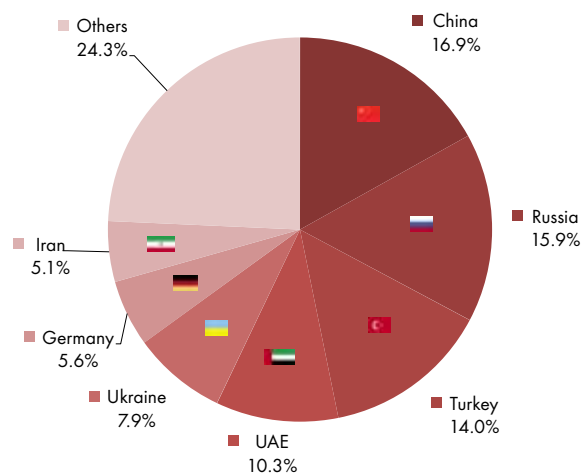
Tajikistan – Import Partners



Turkmenistan – Export Partners

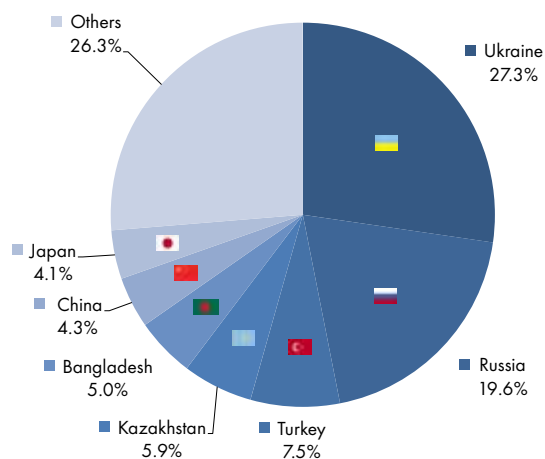


Turkmenistan – Import Partners

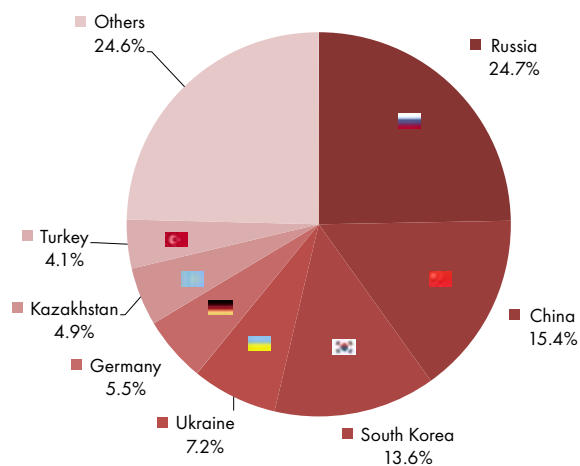


Source: CIA World Factbook, <https://www.cia.gov/library/publications/the-world-factbook/>

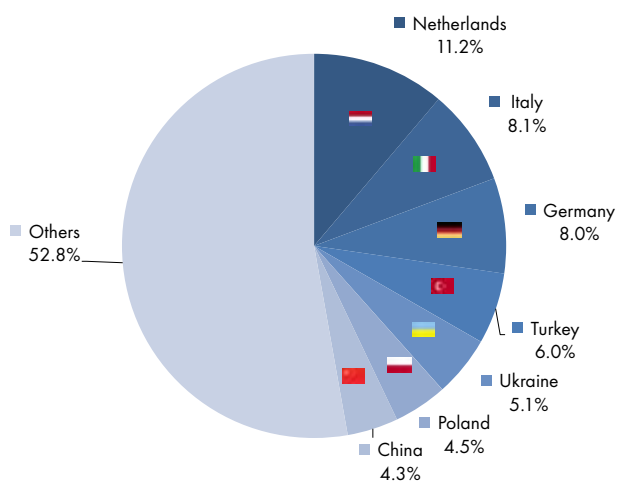
Uzbekistan – Export Partners



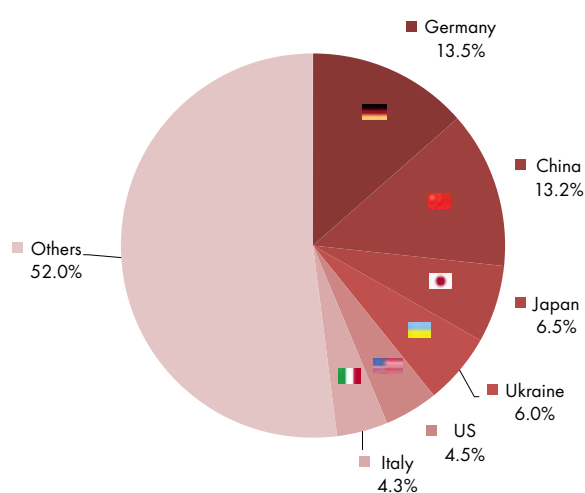
Uzbekistan – Import Partners



Russian Federation – Export Partners



Russian Federation – Import Partners



Source: CIA World Factbook, <https://www.cia.gov/library/publications/the-world-factbook/>

Analysis

Turkmenistan's Relations with Russia

By Richard Pomfret, Adelaide, Australia

Abstract

This article analyses the interaction of domestic and external considerations in determining Turkmenistan's choice of routes for its natural gas exports and the implications of this for Turkmen-Russia relations. Turkmenistan has abundant supplies of natural gas, possessing the largest reserves in the former Soviet Union with the exception of Russia. As a result, Turkmenistan plays an important role in CIS gas supplies and issues surrounding gas dominate Turkmen-Russian relations. Turkmen gas bought at below EU prices traditionally has enabled Gazprom to balance low domestic prices with lucrative exports to the EU. This situation has, however, been under challenge since 2006: intra-CIS gas trade is becoming more transparent, Central Asian suppliers have bargained for higher prices from Russia, and there is competition to build pipelines for exporting Turkmen gas to non-CIS markets. These developments promise to weaken Turkmen-Russian links, but their effects could be negated by technical developments which may undermine Turkmenistan's competitiveness as a gas supplier to non-CIS customers.

Turkmenistan under Turkmenbashi

Economic development of the Turkmen Soviet Republic centred on replacing its population's nomadic lifestyle with collective farms, primarily to grow cotton, and on investment in natural gas production during the 1980s. In the early 1990s, Turkmenistan's newly independent and nationalistic leadership blamed Soviet planners for the lack of diversification in its economy, whereby only about ten percent of the workforce were employed in manufacturing. Nonetheless, with readily exportable cotton and gas, the new, independent country was able to survive the dissolution of the USSR with minimal economic change.

Saparmurat Niyazov, or Turkmenbashi the Great as he preferred to be known, established a highly centralized regime. Major decisions at all levels of government had to be cleared by the President's office, and any opposition was ruthlessly suppressed. The economy continued to be highly regulated, and remains essentially unreformed. Apart from cotton and gas revenues, the economic goal was self-sufficiency reflected in increased output of wheat and promotion of import-substituting industrial projects. In conjunction with the aim of self-sufficiency, Turkmen foreign policy was defined by neutrality, formally recognized in a 1995 UN resolution.

Turkmenistan's national economy remained the simplest of all the Soviet successor states. Rents from cotton and gas exports accounted for between two and three-fifths of GDP in the 1990s. In 1990–2 Turkmenistan was the world's sixth largest cotton producer with an average harvest of around 1.4 million tons, but a mixture of policies to divert acreage from cotton to wheat, poor maintenance of the irrigation system, and lack of

incentives for cotton farmers, to whom the monopoly state marketing board paid well below the world price for their production, led to stagnation of cotton output. Annual gas production fell from around 60 billion cubic metres (bcm) in 1992–3 to 30–33 bcm in 1994–6 and to half of that in 1997 and 1998, when supplies were cut in response to non-payment by Ukraine.

Turkmenbashi created an aura of benevolent autocracy with free provision of gas, electricity, water and salt for residential use, plus low cost public housing, and other subsidized goods and services. However, a considerable amount of gas royalties and cotton revenues went to off-budget funds under the President's personal control; much was spent on monumental projects, mostly to honor the President and to reinforce a personality cult. The 1997–8 shocks of Ukraine's non-payments for gas and of Russia's financial crisis coincided with increasingly authoritarian rule in Turkmenistan. Despite the inefficiencies, the system which looked to be in trouble in the late 1990s was sustained by rising energy prices. After 1999 the state focussed exclusively on maintaining the flow of gas exports, which strengthened dependence on Russia because, apart from a small pipeline to Iran opened in 1997, all of Turkmenistan's gas exports went north through Russian-controlled pipelines. No reforms were envisaged before December 2006 when Niyazov died.

Turkmenistan's Natural Gas

Turkmenistan's Soviet era gas fields are in the east of the country, connecting it to other parts of the former USSR via the Central Asia – Centre pipeline network. Russia refuses to allow Turkmenistan's gas to

transit to the lucrative European markets, restricting Turkmenistan's gas exports to CIS markets. Increased exploitation of western gas fields highlighted the need for new pipelines, and in the 2000s rising energy prices brought Turkmenistan into greater international focus. The temptation to find new customers for Turkmen gas became overwhelming; the reclusive President Niyazov rarely travelled after 1997, but even he made an official visit to Beijing in April 2006 to discuss the construction of a new pipeline.

Imports from Turkmenistan are a key item in Russia's demand/supply equation, and the price paid for those imports impact on Gazprom's profitability. The delivery price of Russian gas to Western Europe varies according to a formula which includes (lagged) oil prices. Gas prices paid by the EU tripled after 2002, peaking at \$500 per 1,000 m³ in the last quarter of 2008, before falling to a 2009 range of \$250–300. Prices in Russia are much lower: in 2006 Gazprom's domestic industrial consumers paid an average \$44 per 1,000 m³ and residential consumers much less, while the price paid by the EU averaged \$240. Turkmenistan's sales to Russia free up Russian gas for export to Europe; the lower the price paid for Turkmen gas and the greater the amount of Turkmen gas that could be sold to Russian domestic consumers, the higher Gazprom's profitability.

Until 2005 Turkmenistan's gas exports were non-transparent, with payment by barter to shady intermediaries. In the 2003–5 contract with Russia, for example, half of the price of \$44 per 1,000 m³ was to be paid by barter, with potential for large-scale corruption through arbitrary valuation. Following the 2004 Orange Revolution, Ukraine announced that its July 2005 contract with Turkmenistan would not involve barter terms, and in April 2005 Russia and Turkmenistan agreed that Gazprom would make all payments in cash. The role of intermediaries in gas transactions involving Russia, Ukraine and Turkmenistan was terminated in an agreement in March 2008. Intra-CIS trade was largely insulated from the rapidly increasing EU gas prices until 2006. However, since then the price Turkmenistan charges for its gas has increased. Turkmenistan's price from Gazprom, \$44 per 1,000 m³ in 2003–5, was increased to \$65 in January 2006. In September 2006 Turkmenistan negotiated a further increase to \$100 per 1,000 m³ for 2007–9, and in November 2007 this was raised to \$130 for the first half of 2008 and \$150 for the second half of 2008.

Thus, Russia has been prepared to increase the price paid for Turkmen gas in order to secure gas supplies for the domestic market and to discourage Turkmenistan

from non-Russian pipeline projects. Russian production from its Siberian fields is past its peak; future output will be from Arctic gas fields, which will not come online before 2011, and the difficult conditions in this region could delay development. Meanwhile, Russia is looking to Central Asia for gas, which primarily means Turkmenistan. Uzbekistan will supply about 12bcm a year to Russia until 2012; Uzbekistan's production is not much lower than that of Turkmenistan, but with a much larger population most is consumed domestically. Kazakhstan's gas production is lower, but large new gas fields are coming into production, which are located close to the Russian border. In March 2008 Gazprom announced that it would pay 'European' prices for Central Asian gas in 2009, i.e. in the range of \$200–300 per 1,000 m³. The announcement was part of a strategy of encouraging Central Asian countries to retain Russia as their principal market and not to agree to new pipeline routes.

Pipeline construction is often politicized as, for gas even more than for oil, it is by far the most efficient means of transport; infrastructure determines the direction of trade flows. Non-Russian pipelines could run south to Iran, southeast to Pakistan and India, east to China or west across the Caspian Sea to Turkey and the EU, but pipelines are expensive. The high fixed cost of pipeline construction made investment in new routes unattractive in the 1990s, but as energy prices rose after 1998 the share of transport costs in the delivered price declined and non-Russian buyers and sellers began to investigate new pipelines. To some degree, choices are mutually exclusive; pipelines are large-scale projects with economies of scale, and the amount of gas available for shipment limits the number of viable pipelines.

Turkmenistan's first non-Russian gas pipeline was built to Iran in 1997 with an annual capacity of 8 bcm, but larger projects through Iran have been stymied by US threats of sanctions against companies doing business with Iran. Negotiations in 1997 with Unocal to construct a pipeline through Afghanistan to South Asia collapsed as the US government drew back from relations with the Taliban government; this route is still on Turkmenistan's agenda, but until Afghanistan's (and Pakistan's) government can provide reasonable security guarantees it remains a distant prospect. Following Turkmenbashi's April 2006 visit to Beijing, construction began on a 7,000 kilometre long pipeline to China via Uzbekistan and Kazakhstan, which was formally opened in December 2009; China has committed to buy 30 bcm a year, a target which should be reached in 2011.

In May 2007 Russia, Turkmenistan and Kazakhstan signed an agreement to build a 10 bcm a year pipeline along the eastern coast of the Caspian, the Prikaspiisky route, feeding into the Russian pipeline network. In December 2007 the proposed capacity of the Prikaspiisky pipeline was doubled, to carry 10 bcm from both Kazakhstan and Turkmenistan, and in 2008 it was increased further to accommodate larger deliveries from Turkmenistan. Construction has, however, not begun and critics question whether the pipeline will ever be built. The December 2007 agreement also called for modernization of the existing Central Asia – Centre pipeline from Turkmenistan through Kazakhstan to Russia, intended to increase its annual capacity from the current 50+ bcm a year.

Several proposals to construct a gas pipeline under the Caspian Sea and then to Turkey were aired during the 1990s and early 2000s, but the project was limited to the Baku-Erzurum pipeline from Azerbaijan to Turkey which opened in 2006. The TransCaspian portion was resurrected when relations between Turkmenistan and Azerbaijan warmed after Turkmenbashi's death, and in August 2007 the USA granted \$1.7 million to Azerbaijan for a feasibility study. The TransCaspian would link up to the Baku-Erzurum pipeline and the proposed Nabucco pipeline from Turkey to Hungary. The feasibility of the TransCaspian and Nabucco projects is linked, because Turkmen supplies are needed to justify Nabucco's capacity.

Turkmenistan's leadership knows that pipelines through a greater variety of countries will increase its bargaining power, but the Prikaspiisky project offers an advantage when it comes to timing. Rather than waiting until 2012 (or later) for Nabucco and an unknown gas contract with European buyers, the Prikaspiisky project offers an earlier inflow of cash from Russia. With two major pipeline routes running north, however, Turkmenistan would remain dependent on Russia as the main purchaser of its gas.

Turkmenistan after Turkmenbashi

After the death of President Niyazov in December 2006, Gurbanguly Berdymukhamedov became President, and in 2007 consolidated his power. The change of leader created the prospect of policy change, although to date reforms have been minimal. Heavy-handed regulation continues to characterize almost all of economic life.

In foreign relations the new president made a clean break. In 2007 President Berdymukhamedov visited New York, Brussels, Moscow and Tehran, welcomed Recep Tayyip Erdogan, Vladimir Putin and Hu Jintao

to Ashgabat, and sent observers to meetings of regional organizations. Despite the greater engagement with the wider world, the substance of Turkmen energy policy has not yet changed much. Turkmenistan's gas pipelines still pass overwhelmingly through Russia, with the proposed Prikaspiisky and upgraded Centre pipelines promising to increase annual capacity to over 80bcm. The 30 kilometer pipeline to the Iranian border opened in December 2009 will increase export capacity to Iran to perhaps 20 bcm. China is the new variable in the equation since its pipeline from Turkmenistan opened in December 2009, but the projected flow of 30 bcm in 2011 will be well below the capacity of Turkmenistan's pipelines to Russia.

Western plans to construct a TransCaspian pipeline to access Turkmen gas without transiting Russia are threatened by the prospect that Turkmenistan will have insufficient natural gas to supply a TransCaspian pipeline, as well as meeting other existing commitments. Turkmenistan has agreed to supply 80 bcm a year through Russia and 30 bcm to China by the 2020s, as well as up to 14 bcm to Iran which could increase to 20bcm, and perhaps to the EU and South Asia. If gas production (82 bcm in 2008) can be doubled over the next decade and a half, then these commitments and dreams might be satisfied. Otherwise, Russia is in the pole position due to its control over the established pipeline, with China well-placed, having completed the construction of a pipeline, and other potential buyers nowhere as they will not build pipelines without gas to fill them.

Russia will resist a TransCaspian pipeline, and it has more leverage in the Caucasus than China. However, two forces favor western pipelines. First, Western influence in Turkmenistan may be strengthened by the technical edge of its energy sector firms, as the technically difficult exploitation of offshore fields highlights the need for cooperation with foreigners with the necessary expertise. Second, in 2008 President Berdymukhamedov hired a British firm to conduct an independent audit of Turkmenistan's gas reserves; the firm's initial reports suggest that previous estimates of reserves totalling 3–5 trillion cubic meters are far below the mark, and that there is plenty of gas to fulfil Turkmenistan's existing obligations and to fill new pipelines to the West – as long as it can be exploited. The first contracts to exploit the South Yolotan field, projected to produce 30 bcm per year, were allocated in December 2009 to firms from China, South Korea and the United Arab Emirates. US and EU firms were disappointed to be excluded, but the Turkmenistan gov-

ernment has stated that it would prefer western firms to exploit the abundant, but more technically challenging, offshore fields.

Conclusions

Turkmenistan has been poorly run since independence. The inherited natural resource wealth has been dissipated by mismanagement and by misuse of the rents from cotton and natural gas. Turkmenbashi's prized neutrality left the country dependent on Russia, which controlled the pipeline outlets. Whether his successor, President Berdymukhamedov, is serious about reform is of great importance, because without reform the economy will remain dependent on revenues from gas exports and without reform Turkmenistan will be less able to increase gas production and hence improve its pipeline options.

The external situation is in a state of flux. In CIS gas markets, greater transparency since 2006 has been accompanied by price increases, as the gap between prices paid by the EU and prices on intra-CIS sales have narrowed. Gas deals have often had a geopolitical component, with Russia more willing to put pressure on Georgia or Ukraine after the Rose and Orange revolutions of November 2003 and November 2004, and to keep Central Asia within its sphere of influence. So far Russia has remained Turkmenistan's major market, even though it has had to accept the opening of pipelines from Turkmenistan to China and Iran.

The increase in prices offered by Russia for Central Asian gas was poorly timed as world energy prices and EU demand both dropped substantially in 2008–9. In the short-term, Russia reacted by reducing its gas purchases from Turkmenistan; supply was first reduced by

an April 2009 explosion in the pipeline which Turkmen sources believed to be a deliberate disruption and then cut as part of a pricing dispute which lasted for most of the remainder of the year. These episodes confirmed Russia's willingness to play hardball and sidestep contractual commitments when it saw an economic advantage in doing so. Under current market conditions and in light of Gazprom's dubious technical capacity, several observers question whether the Prikaspiysky pipeline will be built as planned. Nevertheless, in the longer term Russia will aim to keep Turkmenistan in its sphere of interest and oppose pipelines that threaten its monopoly power.

Finally, Turkmenistan's future prospects as a gas exporter could be affected by new technical developments in transporting liquefied natural gas (LNG). Advances in liquefying gas, in specialized LNG ships and in degasification terminals are eroding the position of pipelines as the least-cost delivery method for gas, and this will benefit suppliers with ocean port access, such as Qatar or Australia, at the cost of landlocked suppliers, such as Turkmenistan. Russia itself is embracing LNG as the delivery mode from its newest gas fields in the Far East and the Arctic. In the EU, large new regasification facilities in Spain, the UK, Italy and elsewhere allowed gas importers to buy LNG on the world spot market in 2009. Even if Turkmenistan can increase its gas production substantially, the development of an LNG spot market will undermine the rationale for investing in expensive pipelines such as the TransCaspian-Nabucco route. In this scenario, Turkmenistan, as a high-cost supplier to the world market, would most likely return to being a poor isolated economy under Russian hegemony.

About the Author

Richard Pomfret is Professor of Economics at the University of Adelaide in Australia. His most recent book is *The Central Asian Economies since Independence* (Princeton University Press, 2006).

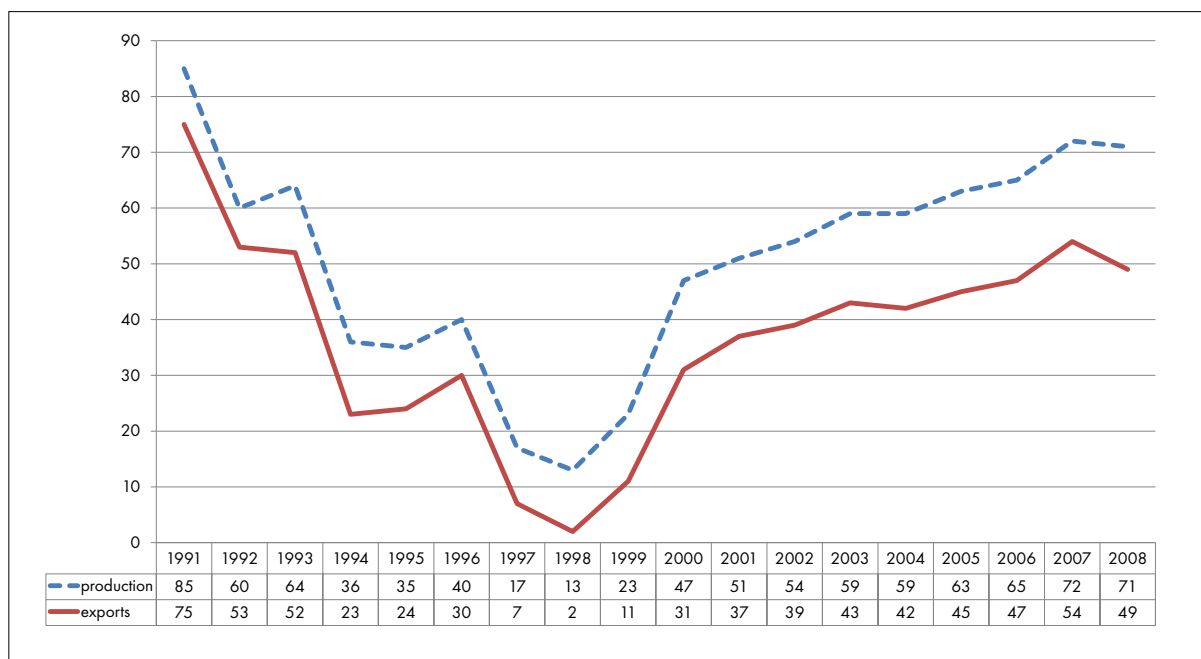
Further Reading

- Luca Anceschi, *Turkmenistan's Foreign Policy: Positive Neutrality and the Consolidation of the Turkmen Regime* (Routledge, 2009).
- Gregory Gleason, Turkmenistan under Niyazov and Berdymukhamedov, in Robert Rotberg (ed.) *Worst of the Worst: Dealing with repressive and rogue nations* (Brookings Institution, Washington DC, 2007), pp. 115–34.
- Indra Overland, Natural Gas and Russia-Turkmenistan Relations, *Russian Analytical Digest* 56/09, 3 March 2009.
- Richard Pomfret, Turkmenistan's Foreign Policy, *The China and Eurasian Forum Quarterly* 6(4), November 2008, pp. 9–34 – available at <http://www.isdp.eu/cefq>
- Richard Pomfret, "Turkmenistan and EU Gas Supplies," in Pascaline Winand (ed.) *Securing Sustainable Energy Supplies in Europe and Australia* (Peter Lang, Bern, forthcoming)

Diagrams

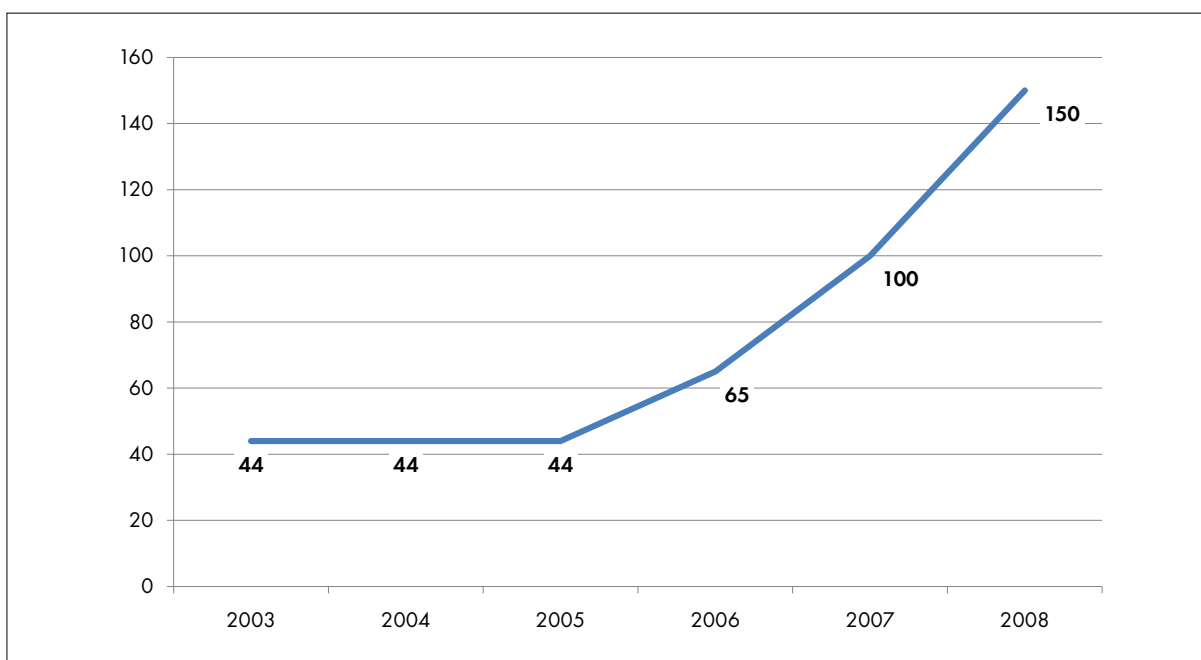
Turkmenistan's Natural Gas Industry

Gas Production and Exports (bln. cubic metres, 1991–2008)



Source: Economist Intelligence Unit

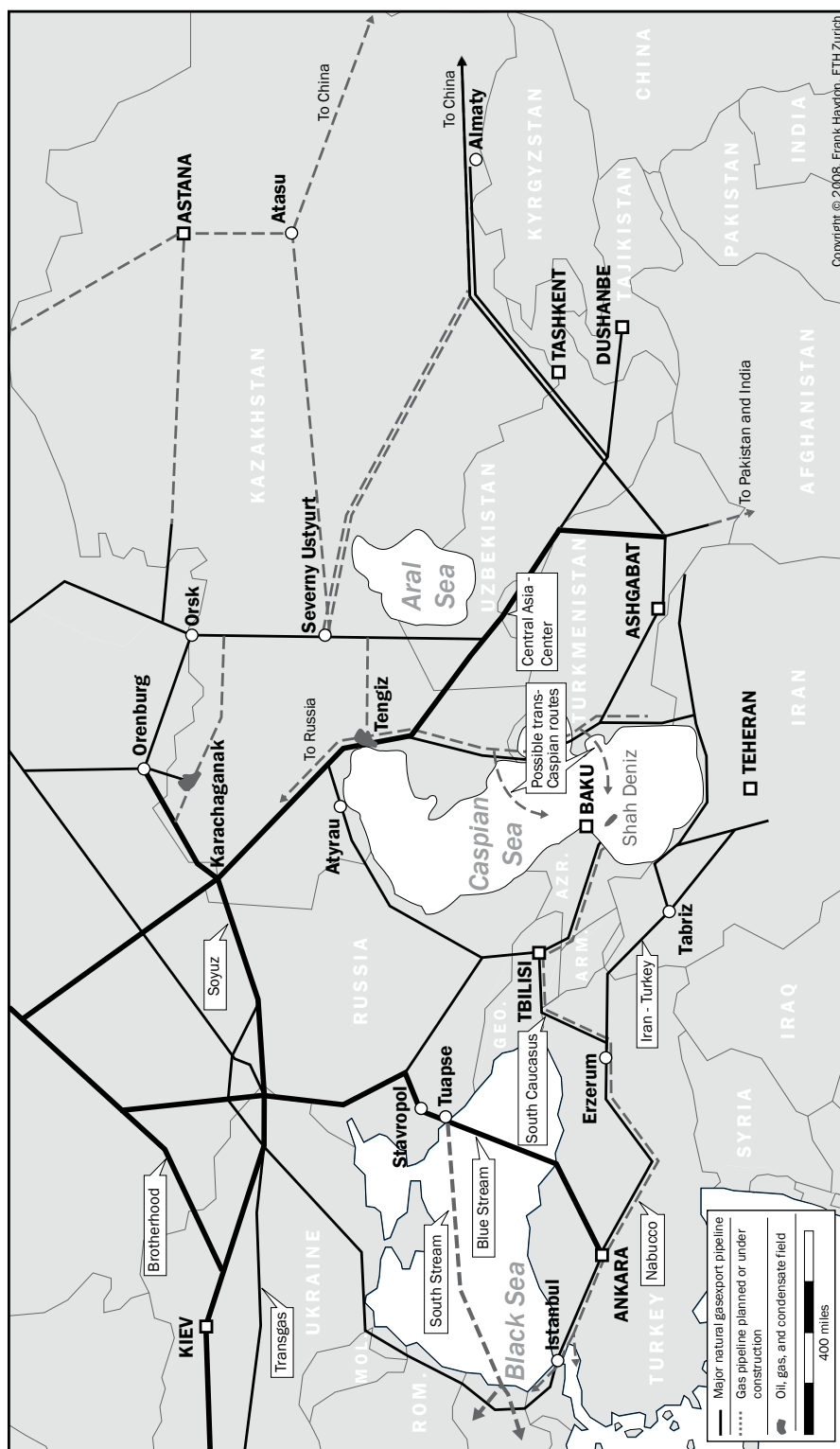
Gas Export Prices Paid by Russia's Gazprom (USD per tcm)



Note: Since 2009 the gas export price is based on a formula linked to the oil price (European price formula). Turkmenistan's export to Russia were terminated in April 2009 by a pipeline blast.

Map

Major Natural Gas Pipelines in Central Asia and Around the Caspian Sea



About the Russian Analytical Digest

Editors: Stephen Aris, Matthias Neumann, Robert Orttung, Jeronim Perović, Heiko Pleines, Hans-Henning Schröder

The Russian Analytical Digest is a bi-weekly internet publication jointly produced by the Research Centre for East European Studies [Forschungsstelle Osteuropa] at the University of Bremen (www.forschungsstelle.uni-bremen.de), the Center for Security Studies (CSS) at the Swiss Federal Institute of Technology Zurich (ETH Zurich), and the Institute of History at the University of Basel (<http://histsem.unibas.ch/seminar/>). It is supported by the German Association for East European Studies (DGO). The Digest draws on contributions to the German-language Russland-Analysen (www.laender-analysen.de/russland), the CSS analytical network on Russia and Eurasia (www.res.ethz.ch), and the Russian Regional Report. The Russian Analytical Digest covers political, economic, and social developments in Russia and its regions, and looks at Russia's role in international relations.

To subscribe or unsubscribe to the Russian Analytical Digest, please visit our web page at www.res.ethz.ch/analysis/rad

Research Centre for East European Studies at the University of Bremen

Founded in 1982, the Research Centre for East European Studies (Forschungsstelle Osteuropa) at the University of Bremen is dedicated to socialist and post-socialist cultural and societal developments in the countries of Central and Eastern Europe.

The Research Centre possesses a unique collection of alternative culture and independent writings from the former socialist countries in its archive. In addition to extensive individual research on dissidence and society in socialist countries, since January 2007 a group of international research institutes is participating in a collaborative project on the theme "The other Eastern Europe – the 1960s to the 1980s, dissidence in politics and society, alternatives in culture. Contributions to comparative contemporary history", which is funded by the Volkswagen Foundation.

In the area of post-socialist societies, extensive research projects have been conducted in recent years with emphasis on political decision-making processes, economic culture and the integration of post-socialist countries into EU governance. One of the core missions of the institute is the dissemination of academic knowledge to the interested public. This includes regular email services with nearly 20,000 subscribers in politics, economics and the media.

With a collection of publications on Eastern Europe unique in Germany, the Research Centre is also a contact point for researchers as well as the interested public. The Research Centre has approximately 300 periodicals from Russia alone, which are available in the institute's library. News reports as well as academic literature is systematically processed and analyzed in data bases.

The Center for Security Studies (CSS) at ETH Zurich

The Center for Security Studies (CSS) at ETH Zurich is a Swiss academic center of competence that specializes in research, teaching, and information services in the fields of international and Swiss security studies. The CSS also acts as a consultant to various political bodies and the general public. The CSS is engaged in research projects with a number of Swiss and international partners. The Center's research focus is on new risks, European and transatlantic security, strategy and doctrine, area studies, state failure and state building, and Swiss foreign and security policy.

In its teaching capacity, the CSS contributes to the ETH Zurich-based Bachelor of Arts (BA) in public policy degree course for prospective professional military officers in the Swiss army and the ETH and University of Zurich-based MA program in Comparative and International Studies (MACIS); offers and develops specialized courses and study programs to all ETH Zurich and University of Zurich students; and has the lead in the Executive Masters degree program in Security Policy and Crisis Management (MAS ETH SPCM), which is offered by ETH Zurich. The program is tailored to the needs of experienced senior executives and managers from the private and public sectors, the policy community, and the armed forces.

The CSS runs the International Relations and Security Network (ISN), and in cooperation with partner institutes manages the Crisis and Risk Network (CRN), the Parallel History Project on Cooperative Security (PHP), the Swiss Foreign and Security Policy Network (SSN), and the Russian and Eurasian Security (RES) Network.

The Institute of History at the University of Basel

The Institute of History at the University of Basel was founded in 1887. It now consists of ten professors and employs some 80 researchers, teaching assistants and administrative staff. Research and teaching relate to the period from late antiquity to contemporary history. The Institute offers its 800 students a Bachelor's and Master's Degree in general history and various specialized subjects, including a comprehensive Master's Program in Eastern European History (<http://histsem.unibas.ch/bereiche/osteuro-paeische-geschichte/>).

Any opinions expressed in Russian Analytical Digest are exclusively those of the authors.

Reprint possible with permission by the editors.

Editors: Stephen Aris, Matthias Neumann, Robert Orttung, Jeronim Perović, Heiko Pleines, Hans-Henning Schröder

Layout: Cengiz Kibaroglu, Matthias Neumann

ISSN 1863-0421 © 2010 by Forschungsstelle Osteuropa, Bremen and Center for Security Studies, Zürich

Research Centre for East European Studies • Publications Department • Klagenfurter Str. 3 • 28359 Bremen • Germany

Phone: +49 421-218-69600 • Telefax: +49 421-218-69607 • e-mail: fsopr@uni-bremen.de • Internet: www.res.ethz.ch/analysis/rad