



TURKEY PLAYED ITS HAND WELL IN THE ENERGY GAME

The agreements signed between Turkey and Russia following negotiations held on December 27-28 brought about two significant outcomes. First was Turkey's nod to the construction of the South Stream Pipeline through its territorial waters. Given the agreement signed with Azerbaijan for the Trans-Anatolian Pipeline just a few days before that, it can be concluded that the pipeline race, in the middle of which Turkey seeks to assume a position, has gained entirely new dynamics. This, however, is the subject of another note.

The second component of the deal with Russia consisted of natural gas deliveries via the Western Line. The 6 billion cubic meters (bcm) of gas that has been delivered for the past 25 years as per the agreement signed in 1986 was to be cut on January 1, 2012 upon the termination of the contract by BOTAŞ. The reasons for the termination of the contract, as stated by the Turkish side, included a price dispute, the accumulation of take-or-pay liabilities, and more pronouncedly, the goal to liberalize the energy market. Nevertheless, when Gazprom dragged its feet about concluding agreements with the private sector, natural gas deliveries destined for western Turkey faced peril.

It appears that Turkey, in the light of a series of parallel developments, chose to eliminate the potential risks for 2012 with a last-minute maneuver, involving once again state agency. At the first phase, as the Trans-Anatolian Pipeline de facto slayed the Nabucco Pipeline project, alternative factors that kept Turkey from making up its mind as to whether or not to support the South Stream project have vanished. As a matter of fact, an ambitious project with a volume of 63 bcm, the South Stream is especially dear to Russia as it will enable the country to outdistance its rivals in the race for dominance in the European natural gas market. On the other hand, it appears that Turkey was wise enough to give a green light the South Stream project only with a favour in return. Although many components of the agreement are yet to be unveiled, it is understood that Turkey was awarded certain concessions about natural gas delivery in exchange for the steps it has taken to facilitate the South Stream project. As Energy Minister Taner Yıldız stated during the press meeting after the signing of the agreements with Russia, Turkey is planning to avoid a possible natural gas shortage during 2012 by consuming the gas accumulated within the scope of take-or-pay obligations. Accordingly, Turkey will consume 3 bcm natural gas out of the take-or-pay account in 2012.

Pricing, another critical issue for Turkey, also appears to be addressed during negotiations. Gazprom Chairman Alexey Miller's remarks that changes were foreseen on the terms of contract had raised expectations about a price cut, which was later confirmed by Minister Yıldız during the press meeting. He stated that Turkey's retrospective demands about pricing, which elevates costs for BOTAŞ, produced "a couple of arrangements." Here, the emphasis on retrospective demands is of importance. "The easing of retrospective liabilities of BOTAŞ" can imply that the natural gas purchase price applicable for BOTAŞ will converge with the private sector price¹ or that some of BOTAŞ's debt to Gazprom will be wiped off. Though it is impossible to learn the true nature of the change in pricing as such information is confidential, it is now known that a cut was introduced. In any case, this is good news for BOTAŞ, which has been facing severe problems about costs and criticism for trying to overcome this challenge via cross-subsidization.

It is stressed both by the Turkish and the Russian side that this last agreement does not imply a new contract or the renewal of the agreement dated 1986. Instead, the parties are mentioning an addendum to the Blue Stream and Western Line agreements signed in 1997 and 1998, respectively. It appears that for 2012, Turkey will purchase the 6 bcm foreseen by the expired 1986 agreement, in addition to the amounts foreseen by the other two agreements, partially or entirely via the take-or-pay scheme. Judging by the insufficient technical capacity of the Blue Stream, it can be concluded that almost all of the additional amount will be provided via the Western Line and therefore the actual difference between the amount delivered via the two pipelines in 2011 and that to be delivered during 2012 will not be significant. The signals we receive so far give the

¹ It is known that contract price for companies importing natural gas via the Western Line is considerably lower than the price BOTAŞ is charged for.

impression that the search for a long-term solution has been deferred. During the press meeting, Minister Yıldız stressed that any deviation from the commitment to liberalization and privatization was out of question. With this perspective, he added that the negotiations between private sector and Gazprom would continue during the first months of 2012 and if the parties can reach an agreement, contracts would be handed over the private sector, as targeted.

In the light of these, the current picture can be interpreted as follows: Playing its hand successfully, Turkey gave the green light to the South Stream, which it had been inclining towards anyway, and obtained concessions about prices and take-or-pay responsibilities in return. At the same time, Turkey managed to appease its counterpart and remove the barriers before private sector activity. It is a happy development that the tension between Turkey and Russia ongoing for more than a year hence eased to some extent and that the 2011 ended with mutual good will and an exchange of praises. Though energy geopolitics is a game of power, it may just as well end up in win-win situations.