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Putin's new secret weapon

Tom McGhie, Mail on Sunday
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President Vladimir Putin came to the conclusion three years ago that Russia was sitting on a secret weapon more powerful than all its military might.

Ownership of 30% of the world's gas supply and being the second-biggest oil producer has given him a new and powerful economic bargaining counter.

And the former KGB officer has shown that he intends to use these resources to restore pride in Russia, which suffered in the years after the downfall of communism.

The bad news for Britain is that two of our largest oil companies, [BP](#) and [Shell](#), which between them have invested more than £10 billion in Russia, are in the firing line as Putin attempts to get Russia a larger slice of the action. But the treatment meted out to Shell and BP pales into insignificance compared with the brutal way it treated Ukraine last year.

In the midst of negotiations on raising gas prices, the Russians suddenly cut supplies to Ukraine. This was devastating for Ukraine, but also for the rest of Europe, which relies on Russian gas coming through Ukraine's pipelines.

There has been similar pressure using gas as a political and economic weapon on other countries on its borders. What countries such as Lithuania and Georgia have in common is that they are mainly pro-West and have opted out of the Russian sphere of influence.

Earlier this month, Russia was accused by the Georgians of using its gas resources as a political weapon. The complaint came after Gazprom, Russia's state-owned gas company, announced that prices would double. This decision came in the middle of a political row between both countries sparking accusations that gas was a tool of Russian foreign policy.

Gela Bezhuashvili, Georgia's foreign minister, says: 'They present it as a commercial deal, but there is a portion of politics in it.'

Russia has a good argument for raising prices. Existing prices are heavily subsidised and half the market rate. And the Kremlin is reluctant to sell cheap gas to countries that have decided to shift their loyalties to the West.

But energy analysts have noted that there is a pattern to demands for price rises. Countries loyal to Russia get a better deal.

Strangely, Russia's crude use of gas has had a beneficial effect on UK energy policy. Suddenly, security of supply has become a key issue with the Prime Minister arguing that Britain must boost its own supplies of energy by restarting a nuclear rebuilding programme and developing our own renewable energy sources such as wind and wave power.

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Most Western political leaders recognise that Russia wants to dominate gas supplies to the West, but there is a growing suspicion in the UK that Gazprom wants to dominate the British market.

Gazprom has made no secret that it has been eyeing up [Centrica](#), owner of [British Gas](#), with its 16 million customers.

The advantages to Gazprom are obvious. It would have instant access to a huge new market and it would have an outlet for the gas coming through its pipelines. The UK would, in effect, be at the mercy of the Russians.

But because the British energy market is open and it already has a number of foreign big players, such as EDF of France and Germany's Eon, there are no good obvious reasons for refusing Gazprom entry.

Gordon Brown has made it clear he is not keen on such a move. While it is unlikely that the Government would halt a takeover, to be successful, Gazprom would have to satisfy regulators that it would stick to strict corporate governance-rules. At present, Gazprom is unlikely to pass that test because of the close connections to the Kremlin and its refusal to give up total control of its pipelines.

For Shell and TNK-BP - the joint Russian and British gas company --the dangers of the Kremlin's new aggressive pro-nationalisation policies are more obvious.

In late September, Russia turned up the pressure on massive foreign-led energy projects by ordering an environmental investigation of Shell's Sakhalin venture off the far east coast of Russia and warning TNK-BP over violations at its Kovykta gas field in Siberia.

Russian moves to put the brakes on Shell and [Exxon Mobil](#) developments on Sakhalin Island have raised suspicions that the Kremlin is seeking a bigger stake for Gazprom in the multi-billion pound projects, signed when oil prices were lower and power lay with foreign investors.

Russian officials say they are motivated by concerns over the environment - Sakhalin is close to feeding grounds for the endangered gray whale and there are problems with pipes laid on the ground near earthquake areas.

Russia is furious that the fields are running well over budget, cutting into Moscow's future earnings under production-sharing agreements that mean the oil companies will recoup their costs before having to pay any royalties.

Shell has warned that there will be further delays in the project, one of the largest in the world, because of a decision earlier in the month to revoke environmental permits.

The company has infuriated the Kremlin by doubling its estimate of the project's cost to £10.5bn. Exxon's nearby Sakhalin-1 project could cost £8.9bn, a Russian official said last week, a £2.2bn overshoot that Moscow says it will oppose. Natural Resources Minister Yuri Trutnev says there is no question of removing Shell's licence.

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Until recently, TNK-BP had escaped Moscow's attentions. But on September 28, prosecutors warned TNK-BP, which holds the licence to the huge Kovykta gas field in Russia's Far East, over violations of environmental law.

TNK-BP says there was no sign of any threat to its licence for Kovykta. Chief executive Robert Dudley says: 'We haven't received anything on this. We've got all the permits in place, we've had all the environmental reviews, so I'm not sure what to make of this.'

Kovykta has reserves of more than two trillion cubic metres of gas, which TNK-BP wants to export to China. But Gazprom has so far allowed it a licence to supply gas only to the local Irkutsk region.

In another blow for foreign operators and energy-hungry Asia refiners, Russia's technical standards watchdog last month said more checks were needed on Exxon's Pacific terminal, meaning regular shipments could not start before mid-November.

Energy industry observers see a pattern in Russia's sudden desire to make things more difficult for foreign firms.

Putin is determined to take control of what he regards as Russia's vital strategic assets. And he believes the agreements struck by Shell and BP were made at a time when the country was weak.

Shell and BP are well aware of the tough new Russian attitude, but are determined to stick it out. They know things are not easy, but they also know that Russia needs the West's skills if it is to exploit its energy reserves.

In the understatement of the year, Peter Henshawa, BP executive at TNK-BP's office in Moscow, says: 'Things are sometimes difficult in Russia.'

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