

THE ROLE OF ENERGY IN TURKEY'S RELATIONS WITH RUSSIA AND IRAN

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This paper was commissioned as part of a CSIS research project called “The Turkey, Russia, Iran Nexus: Regional Perspectives.” This project, which CSIS is pursuing in cooperation with the Economic Policy Research Institute of Turkey (TEPAV) and Institute of Oriental Studies (IVRAN) Moscow, is exploring evolving relations between these three pivotal countries and their implications for regional developments in the Caucasus, Central Asia, and the Eastern Mediterranean, and for their relations with the United States and other countries. It seeks to promote dialogue and a deeper understanding of these relations among experts and officials in all four countries. CSIS will develop a comprehensive assessment of the forces driving these relations and their long-term implications, and offer various policy recommendations. For more information on the project, please visit our website at <http://csis.org/program/turkey-russia-iran-nexus>.

I. Turkey's Global Energy Strategy

This paper briefly outlines Turkey's overall energy strategy to set the context for an assessment of how Russia and Iran figure in that strategy, particularly with respect to Turkey's ambition to become a vital east-west and north-south energy bridge.

Energy is one of the tools of Turkey's re-emergence as a regional geopolitical player. Turkey's main goal in formulating its energy strategy is first and foremost to strengthen its energy security. To this end, its energy strategy can be summarized under three main principles:

- 1) To decrease Turkey's heavy reliance on imported energy resources by increasing the use of domestic energy resources (coal, hydrocarbon and renewables, including hydropower) and by liberalizing its energy market. This also includes raising energy efficiency within Turkey.
- 2) In terms of imported resources, to ensure diversification of both sources and suppliers, as well as transportation routes to become a more effective key transit country and energy hub between the energy-producing countries to its east and the energy-consuming countries to its west.
- 3) To introduce and gradually increase the share of nuclear energy in its energy mix.

The limits of Turkey's domestic energy resources in the face of its growing energy demand have resulted in a dependency on energy imports, primarily of oil and gas. Currently, around 26 percent of the total energy demand is met by domestic resources, while the rest is supplied from a diversified portfolio of imports. Turkey imports around 91 percent and 98 percent respectively of the oil and natural gas it consumes. Consequently, the primary objective of Turkey's energy strategy is to ensure its own energy security while contributing to that of Europe. As a result, Turkey's energy picture is as follows:

- ✓ Dependency on foreign resources: 74 percent
- ✓ Turkey's annual demand increase: 4-5 percent (EU's annual demand increase: 1.6 percent). Over the last decade, Turkey has been second only to China in terms of natural gas and electricity demand increases.
- ✓ Turkey's principal energy demand is expected to increase by 4 percent annually until 2020.
- ✓ More than \$100 billion investment required in the next 15 years (Annually \$6-8 billion).

Within this context, both the Russian Federation (RF) and Iran are important partners for Turkey in the energy field (see the tables below). Energy issues play a prominent role in Turkey's relations with both of these countries, with whom Turkey sees cooperation as complementary to its goal of becoming a natural energy bridge between East and West, North and South.

CRUDE OIL IMPORTS – 2009/2011

	2009 (M tons)	Percentage	2011* (tons)	Percentage
Russia	5.7	40	2,116,500	12
Iran	3.2	26	9,287,092	51
Iraq	1.7	12	3,071,477	17
S. Arabia	2	14	1,965,299	11
Italy			116,405	1
Kazakhstan			1,185,556	7
Azerbaijan			80,719	0
Syria			254,655	1
other		0.8		
TOTAL	14,000,000		18,077,703	100

*In 2011, 18.077.654 tons crude oil imported. 2.433.408 tons was domestic production. Total refined amount was 20.744.705 tons.

NATURAL GAS IMPORTS : 2010/2011 (BOTAŞ numbers)

2010 Percentage (billion cubic meters)	2011 Percentage (billion cubic meters)
Russia 45.5 (14.5)	Russia 55.3(21.8)
Iran 25.5 (7.7)	Iran 21(8.3)
Azerbaijan 14.5 (4.5 ¹)	Algeria 10.7 (4.2)
Algeria 12 (3.9)	Azerbaijan 9.9 (3.9 ¹)
Nigeria 3.5 (1.1)	Nigeria 3.1 (1.2)
TOTAL: 32.4 bcm	39.5 bcm

II. Russia and Iran in Turkey's Global Energy Strategy

Energy Relations with Russia

In 2011, the RF was Turkey's second largest trading partner (\$30 billion; \$6 billion exports, \$24 billion imports) and the principle item in bilateral trade was energy (70 percent of imports; \$21 billion). Naturally, cooperation and trade in the energy field with the RF constitutes one of the main factors of Turkey's multidimensional bilateral relations.

As economic cooperation is one of the factors that drive political relations, the close cooperation Turkey has established with the RF is not only reflected in the trade numbers, but has also contributed to the further deepening of relations in the political sphere by creating a mutual economic interdependence (more on energy supply dependency to Turkey).

Russian Natural Gas Diplomacy Toward Turkey: Linkages Between Energy and Non-energy Issues

Both Turkey and the RF attach importance to the principle of "mutual benefit" in energy relations—any project or area of cooperation must serve the interests of both countries. Natural gas is only one aspect of their comprehensive relations. During the Russian and Ukrainian gas crisis of 2008 and 2009, as well as when Iran cut gas supplies to Turkey in 2007 and 2008 winters, Russia was extremely graceful and careful in supplying extra gas to the Turkish market to remedy the possible negative impacts of shortages. This example and similar practices later on display Russia's loyalty to its commitment as a "reliable supplier."

The mutual benefit or "win-win" principle, often referred to by Prime Minister Erdoğan, aims to establish a balanced interdependence between the two countries, which makes it possible for Turkey and the RF to cooperate on such large projects as the Blue Stream pipeline and more recently the Akkuyu nuclear power plant project. However, some energy experts in Turkey are very nervous and warn the government not to adopt a one-sided approach to energy relations with the RF.

Another issue in which Turkey seeks extensive cooperation is the prevention of any tanker accidents in the Turkish Straits. The large volume of tanker traffic in the Turkish Straits constitutes a serious and imminent threat to human life, the vast cultural heritage of İstanbul, and the marine environment of the Straits. An accident would also disrupt oil transportation through the Straits. Accidents can only be prevented if the Straits cease to be used as a tanker highway.

Therefore, by-passing the Straits in oil transportation, be it through the realization of the Samsun-Ceyhan pipeline or another project, is of utmost strategic and economic importance for Turkey. Turkey regularly raises its concerns in the ongoing, but still inconclusive, talks with the RF on Samsun-Ceyhan. The Russian side approached the Samsun-Ceyhan project as an opportunity to bring a "basket deal" to bilateral energy negotiations which included demarcation of the South Stream route through Turkey's Exclusive Economic Zone (EEZ), the nuclear power plant deal, and gas distribution rights in Turkey. When Turkey secured a deal with Azerbaijan on the Shah Deniz II gas field and the standalone Trans-Anatolia Pipeline (TANAP), which would jointly be built from the eastern border of Turkey to the western most part of Turkey to carry gas to supply Nabucco and/or TAP, Turkey unilaterally gave Russia the much awaited permission to use its EEZ for feasibility studies of South Stream. At that point, the basket deal was moot. Turkey's concession on demarcation did not prevent the Russian side from reacting harshly to Turkey's decision to host NATO radar installations in its eastern city of Malatya. Russia sought

to retaliate by creating a linkage between its support for allied collective self-defense efforts and the energy sector, announcing that it would suspend talks on the Samsun-Ceyhan project.

Energy Flows from the Black Sea and Caspian Basin Regions: Convergence or Divergence?

For almost a decade now, Turkey has not considered its interests diverging from those of the RF in the field of energy. Quite to the contrary, in the face of lost interest, strategy coordination, and political will on the side of the U.S. and the EU, the RF is one of Turkey's main partners in this field and Turkey attaches great importance to maintaining a dialogue and working with Russian partners to further their mutual interests and gain more ground in the Black Sea and Caspian basin regions.

Since the beginning of official discussions, Turkey stated that it does not regard South Stream to be a rival project to the Southern Gas Corridor. Each Southern Gas Corridor project, be it TANAP, Nabucco, ITGI, or TAP, is well underway to transport natural gas originating from or transiting Azerbaijan through Turkish territory.

In accordance with its understanding of the complementary nature of bilateral relations, Turkey has responded favorably to the Russian demand for the construction permit of the South Stream project in its EEZ in the Black Sea, on the condition that the environmental rules and regulations in Turkey are followed by the companies involved.

Prospects for Development of Nabucco and the Southern Corridor

Realization of the Southern Gas Corridor and the transportation of Azeri and Turkmen gas to Europe through the Southern Corridor has long been one of the main priorities of Turkey's energy policy. Turkey is working with Azeri and Turkmen partners as well as the EU to reach the "optimum way" in which this objective can be realized.

Although Turkey, in principle, supports all Southern Gas Corridor projects passing through its territory—Nabucco, ITGI, TAP and TANAP—it is the Shah Deniz Consortium that ultimately decides which route will be used to transport natural gas to Europe. After the deal with Azerbaijan on the Shah Deniz II gas field and TANAP standalone pipeline, Nabucco is likely to start cost-effectively from the western end of it and "in slices" with bilateral cooperation projects en-route.

The Turkish government does not give credit to arguments or any efforts by the RF or Russian companies to prevent these projects. There are deep relations, however, between Russian interlocutors and some construction and energy companies—some with media connections—in Turkey and from time to time they become vocal in favor of further cooperation between the two countries. However, this is only natural, given that economics always came before politics as a driver for the further strengthening of bilateral relations.

Most Turkish energy experts also believe that their Russian counterparts accept that the Southern Gas Corridor will be realized and will not undermine vital Russian regional interests. Russian officials and business leaders are trying to make use these projects for their advantage. Both countries appear to have come to the conclusion that the various Southern Corridor projects complement other energy projects promoted by Russia.

Challenges in Expanding Turkey's Gas Transit Options

Turkey is a natural geographic bridge between Azerbaijan, Iran, Iraq, Turkmenistan and Europe. Turkey is also renowned as a reliable partner in the transportation of energy resources in the international arena. The successful completion of projects such as the Kirkuk-Ceyhan oil pipeline, Baku-Tbilisi-Ceyhan oil pipeline, the Baku-Tbilisi-Erzurum natural gas pipeline, and Turkey-Greece-(Italy) Gas Interconnector projects attest to Turkey's reputation as a responsible and dependable partner. As a result, it is natural that Turkey is still regarded as the most feasible and viable route both politically and economically, in transporting natural gas from not only Azerbaijan, but also Iran, Iraq and Turkmenistan.

There are many factors that will have to be taken into consideration when projects are drawn up to transport gas from these countries to Europe. All of these countries and their energy sectors have their own unique and specific conditions. These conditions, as well as the international geo-political situation, including developments in of Iran, Iraq, and now Syria, have to be taken into account. Clearly, the greatest challenge is geopolitical, not economic. The Iranian nuclear issue, the future of Iraq and relations with the Kurdish Regional Government, the future of the Syrian regime, relations with Armenia, and Nagorno-Karabakh, will all be fundamentally important issues.

Cooperation on Nuclear Power

Turkey envisions reducing its dependency on imported fossil fuels, especially natural gas, through the sequential commissioning of nuclear power into the Turkish electricity grid. In this respect, Turkey intends to construct around 10,000 MW of nuclear capacity by 2030.

With that vision, and the uniquely favourable conditions provided by Russia, Turkey signed an intergovernmental agreement with the RF stipulating the construction and operation of a nuclear power plant at the Akkuyu site. This agreement projects a nuclear power plant composed of 4 reactors, each with 1200 MW installed capacity.

Construction is expected and likely to start in 2013. However, after the Fukushima incident, Turkish public opinion has heightened concerns on nuclear safety issues. Additional measures will be taken in the design and construction of the Akkuyu nuclear power plant to meet the most rigorous international safety standards, which in return may result in the postponement of the actual construction phase.

It is not yet clear whether Akkuyu will be the first project in a deepening cooperation with Russia on development of Turkey's nuclear power sector. However, the terms of the deal, which include educating Turkey's first nuclear scientists for the operation of the plant in Russia, and the possible success of the devised model may trigger further cooperation between the two countries.

Energy Relations with Iran: Shaped by Political or Market Forces?

Turkey's total demand for natural gas more than doubled from 18 bcm in 2002 to 39.5 bcm in 2011. So too did its electricity and oil demand. In the face of such requirements, energy constitutes one of the most important dimensions of Turkey's bilateral economic and trade relations with Iran. Turkey's cooperation with Iran should be seen from the perspective of Turkey's need to diversify its energy sources. Being the largest source country for oil imports (51 percent in 2011) and second largest source of gas imports makes Iran an indispensable partner in energy for Turkey

The prospect of expanded energy trade is a major mutual incentive in efforts to advance cooperative political ties with Iran. However, this element of relations is far from living up to its potential for a variety

of economic and technical reasons. Developments in Syria and Iraq will also be decisive in the fate of this cooperation. Growing tensions with Iran over Syria and Iraq and political change in the region seem to have diminished interest in the energy trade with Iran.

Between Failed Commitments and Bright Prospects

In comparison to Russia, Iran has been considered less a reliable partner for Turkey. While Iran is Turkey's largest oil supplier and second largest gas supplier after Russia, Ankara's energy and business dealings with Tehran have never been easy. Iran often demands comparatively higher prices while gas quality and quantity often fall below the agreed terms. After more than a decade of operation of the Turkey-Iran gas pipeline, Iran still cannot supply Turkey's contracted 10 bcm of natural gas a year (only in the last two years has Iran increased its supply to the Turkish market; 6.16 bcm in 2007, 5.8 bcm in 2008, 7.7 bcm in 2010, 8.3 bcm in 2011). In both January 2007 and January 2008, Tehran slashed gas exports to Turkey because of high Iranian domestic demand. In addition, there have been problems with the quality of the Iranian gas. Following a recent row on "take or pay" contractual obligations regarding price and amount between the two countries, Turkey took the issue to international arbitration. Despite these past problems and lingering concerns, Turkey needs Iranian gas to meet its domestic demand.

Ankara and Tehran have also come to loggerheads over Iran's failure to respect commercial contracts in the past. In May 2004, the Islamic Revolutionary Guard Corps forced the expulsion of the Turkish construction consortium TAV from Tehran's airport, despite a 15-year service contract. The same year, the Iranian government also cancelled Turkcell's successful bid to enter the Iranian cell phone market. Last but not least, there are political and financial impediments to Turkey's large-scale investments into Iran, given Iran's current tensions with the international community over its nuclear activities. Indeed, Iran could become a conflict zone if diplomacy and sanctions fail in the near future. Still, since 2007, there has been a renewed drive for an energy partnership with Iran. In July 2007, both countries signed a memorandum of understanding (MoU) in which the two sides agreed to build an ambitious 2,200 miles of gas pipelines (one from the South Pars field, the other from Turkmenistan to Turkey, forming a land connection from Turkmenistan's eastern and richest gas fields). These are costly, decades-long endeavors, which require a long-term engagement. Financing all these projects is going to be a major challenge. If completed, these projects could transport up to 40 bcm of gas annually to Europe via Turkey.

Iran and Turkey have also agreed to increase cooperation in electricity generation. In this context, they plan to construct natural gas power stations in Eastern Anatolia, where power shortages take a heavy toll on the local economy, especially during the long winter months. The latter investment is supposed to be spearheaded by the two countries' private sectors in order to avoid any possible sanctions on Iran.

Despite these prospects, Turkey's talks with Iran, particularly regarding development in the South Pars gas field, have been far from conclusive. For example, according to a November 17, 2008 MoU (a continuation of the first MoU of July 14, 2007), the Iranian side agreed to give the development rights of the 22nd, 23rd, and 24th phases of the South Pars field in the Persian Gulf to the Turkish Petroleum Corporation (TPAO) under a service contract. But four years later, the details of this agreement are still being worked out by the relevant institutions. The Working Group that was established for this purpose has convened on several occasions; however, no agreement has been reached regarding the details included in the MoUs.

Since Turkey's energy policy aims, among other things, to contribute to Europe's energy supply security, Ankara believes that these efforts will provide an impetus to the later phases of Nabucco and other East-West energy pipeline projects, albeit in the longer term due to current political constraints. Despite current frustrations, Iranian gas is certainly one of the options that might feed these alternative supply

sources. Recent progress on Azeri gas supplies will not by itself be sufficient to supply the later stages of the so-called Fourth Corridor. Shah Deniz gas, along with Iraqi gas and trans-Caspian connections, will continue to be vital, and Turkey's interest in acquiring Iranian gas is by no means seen as an alternative to the above sources. On the contrary, Turkey's hope is that possible progress in its Iranian negotiations will help to accelerate development of these other important supply sources.

Nuclear energy might emerge as an area of cooperation between Turkey and Iran if and when Iran gets its IAEA approved civilian-only nuclear program. The same Russian company (Rosatom, the Russian State Atomic Energy Corporation) that provides fuel to Iran is also slated to construct Turkey's first nuclear power station in Akkuyu. Turkey stands with the United States, the European Union, and the UN in support of diplomatic efforts to stop the Iranian government from developing nuclear weapons capabilities. It seems clear that Turkey will be a continuing interlocutor in nuclear negotiations with Iran in the near future.

Energy development projects can take years to put into operation; hence, engagement with Iran today is important for Turkey and other nations in order to secure their long-term energy needs. None of the countries dealing with Iran on energy matters can afford to wait until the Iranian sanctions have run their course.

Turkey hopes and believes that one day the international political situation with regard to Iran will change. When that happens, Turkey wants its companies operating in the energy sector to be prepared to accelerate their activities in Iran.

Effect of Oil-related Sanctions on Turkey–Iran Energy Trade

Turkey believes that every country has the right, under the provisions of international law, to benefit from the use of nuclear energy for peaceful purposes. In addition, without a dialogue, there will be no chance to convince Iran to cooperate with the international community, especially with the P5+1, based on the international commitments required by the Nuclear Proliferation Treaty (NPT) regime and the International Atomic Energy Agency (IAEA). However, Turkey would oppose the existence of nuclear weapons in its region. Ankara believes that the dilemma surrounding Iran's nuclear program should be solved through dialogue and negotiations. Accordingly, as a responsible member of the international community, Turkey has from the beginning actively contributed to the solution of this issue. It has also acted in compliance with legally-binding UN Security Council resolutions on sanctions.

On bilateral energy relations, given Turkey's own demand dilemma, the picture is more complicated. Last year Turkey imported 51 percent of its oil from Iran. This is up from 26 percent in 2010, a huge increase. The financial sector and the oil exports of Iran are specifically targeted in the recent sanctions against Iran. The country's energy bureaucracy is anxious, as it will be a major and costly challenge to find alternative supply sources for such a sizable volume of oil. The Kurdish Regional Government and/or Iraq are often mentioned as alternative sources, but neither is immune to political complications and both suffer from infrastructural hurdles. Energy Minister Yildiz announced in late March 2012 that Turkey would reduce imports from Iran by 20 percent in the interest of diversification of supply, and that BOTAŞ plans to purchase oil from Libya and Saudi Arabia on the spot market, but this may not completely offset the reduction in Iranian imports. Therefore, Turkey needs exemptions, such as those that Japan has secured, if not for the total amount of oil imports from Iran, certainly for sizeable amounts.

To make the picture more complicated, TÜPRAŞ, a privately held refinery, has a contractual obligation to purchase Iranian oil until September of 2012. It is not possible for the Turkish government to oblige a private company to terminate such a contract, especially in the absence of an internationally-accepted UN

resolution. Such an act would raise the question of who would bear the legal and contractual consequences of such a termination. Therefore it will be up to TÜPRAŞ to decide whether to proceed, regarding its current contract with Iran.

Turkey has similar concerns regarding possible future sanctions on Iranian natural gas exports. Turkey believes that the new wave of sanctions will not directly target Iranian gas exports because Turkey is under long-term contractual obligation to purchase a certain amount of gas from Iran on a yearly basis. The purchase and sale contract between the two countries includes strict “take or pay” provisions. Aborting natural gas purchases on Turkey’s part would not free it from payment obligation. Again, it does not seem possible for Turkey to disregard its contractual obligations in the absence of an internationally-binding UN resolution.

International developments and Iran’s response to them will determine Iran’s role in this equation; Iran could eventually play an important supplier role if its politics somehow shifted.

Caspian Sea Demarcation and Development of Central Asian Energy Resources

It is known that a common understanding has been reached on demarcation of the northern portion of the Caspian Sea between Russia, Azerbaijan, and Kazakhstan. Turkey hopes to see that common ground can also be found in the southern portion by Azerbaijan, Iran, and Turkmenistan. Turkey believes that the status of the Caspian Sea needs to be finalized only by the states bordering the Caspian Sea, namely Azerbaijan, the RF, Kazakhstan, Turkmenistan and Iran.

Turkey can substantially and most efficiently contribute to the global energy supply security by strengthening its role as a transit country and an energy hub in the region through multilateral projects. Connection of the Turkmen and Azeri gas networks and offshore oil/gas fields in the Caspian Sea would support this goal. Provided that the Turkmen and Azeris agree on the delimitation of their sectors in the Caspian, third parties have no right to intervene, since both sectors are adjacent to each other.

The Trans-Caspian Natural Gas Project, through which Turkmen and/or Kazakh natural gas will reach Europe via Azerbaijan and Turkey, is also an urgent matter as it will contribute to the diversification of routes and supply sources of Europe. Turkey places utmost importance on the realization of this project, without which the East-West Energy Corridor will not be complete.

From an energy security perspective, Turkmenistan and Kazakhstan should not become dependent on one country and one route for exporting their natural gas. They do not favor, so far, substantial energy relations with Iran. As a result, it is high time that they consider taking new initiatives.

III. Conclusion

The Turkish foreign policy elite considers engaging its immediate neighbors as complementary, rather than contradictory, to Turkey’s more traditional Western strategic alignments. Russia and Iran are cases in point.

There is no doubt that Turkish-Iranian, and to a lesser extent Turkish-Russian, energy cooperation has angered previous U.S. administrations because they undercut American efforts to check resurgent Russian energy policy in Eurasia, and more importantly, to isolate the Islamic Republic over its defiance of previous UN Security Council sanctions aiming to suspend its uranium enrichment program. Nonetheless, Prime Minister Erdoğan has repeatedly stressed that Turkey’s cooperation with Russia and Iran is intended only to diversify Turkish energy supplies. It would be “out of the question to stop imports from

either country [Russia or Iran],” Erdoğan said following the Russo-Georgian war of 2008, especially as Turkey’s energy needs grow by almost 5 percent per year. This statement alone concisely summarizes Turkey’s energy relations with those two countries.