



THE TURKEY, RUSSIA, IRAN NEXUS: ECONOMIC AND ENERGY DIMENSIONS

Proceedings of an International Workshop
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Highlights

- Economic relations between Turkey, Russia, and Iran reflect limited connectivity, dominated by energy and low-end commerce. There is potential for a European level of regional economic integration based on industrial relations, but this would require development of a regional planning process and expanded private sector dialogues and will be contingent on developments in political relations.
- Turkey and Russia have pledged to build a broad strategic partnership, but the relationship is more tactical than strategic. A strategic relationship implies greater alignment of interests and foreign policies in pursuit of common goals. With the exception of the Black Sea, the two countries have no common agenda and more divergent than convergent interests.
- Turkey–Russia economic relations remain mutually beneficial; however, the two countries would be hard pressed to achieve the goal of \$100 billion in total trade volume. Turkey is the third largest market for Russian gas and also imports substantial oil, coal, and petroleum products. They are pursuing cooperation in development of nuclear power and may link electrical grids around the Black Sea. While there are significant economic opportunities in Russia and Central Asia, Turkey is disinclined and unable to change its economic and foreign policy orientation away from the European Union and the United States.
- Iran has pursued a pragmatic policy to build closer economic and energy ties with its immediate neighbors to encourage regional cooperation, enhance its security, and reduce the impact of sanctions. While sectarian suspicions remain, Turkey has special appeal across the Iranian political spectrum as a neighboring Islamic state that has shown Iran respect and offers access to needed technological and financial assistance. These factors converge with Turkey’s strategy of developing cooperative relations with neighbors in order to foster continued economic growth and regional stability and enhance its regional stature.
- Turkey and Iran could realize their goal of doubling total annual trade volume to \$30-35 billion. Energy will remain the major component, but there is potential for diversification. Iran imports \$60 billion dollars of goods annually, most of which could be produced in or imported from Turkey. Iran is actively moving financial transactions and some of its \$16 billion re-export channel from UAE to Turkey.
- The Russia–Iran relationship is the most difficult of the three bilateral ties. Iranians across the board have a genuine distrust of Russia. The economic interests of the two countries are not convergent, yet there are elements of strategic partnership. Russian leaders find Tehran’s anti-Americanism useful as a way to balance U.S. political influence. Iran has developed its cooperation with Russia to advance this common strategic goal. Russia–Iran relations reflect expediency—when Iran is unable to secure technology or weaponry elsewhere, Russia has proven a useful partner.

Background on the Workshop

The Center for Strategic and International Studies (CSIS) in Washington, in cooperation with The Economic Policy Research Foundation of Turkey (TEPAV), Ankara, and The Institute of Oriental Studies (IVRAN) of the Russian Academy of Sciences, Moscow, held an international workshop at TEPAV on March 29, 2012 that explored economic and energy issues in relations between Turkey, Russia, and Iran. This was the first of two workshops designed to deepen and give a more multinational character to initial CSIS analysis of the nexus of relations between Turkey, Russia, and Iran and to promote international dialogue among experts and officials. CSIS commissioned four short papers by Turkish, Russian, and Iranian analysts to solicit their perspectives on how economic and energy among these three countries are evolving and shaping regional dynamics. During the workshop CSIS scholars presented the results of their preliminary research, the authors of the commissioned papers presented their findings, and the ensuing dialogue among the scholars and other participants (including other analysts and current and former officials) is captured in this workshop report. The workshop was conducted on a non-attribution basis to encourage candid dialogue. Final versions of the commissioned papers are posted on the web sites of all three institutions.

I. Turkey, Russia, Iran Economic Relations

Overarching Trends

The first workshop panel explored the scope and direction of overall economic and commercial relations between Turkey, Russia, and Iran. An American presenter noted that bilateral economic, energy, political, and security relations between the three countries are major factors shaping regional developments in the Caucasus, Central Asia, and the Eastern Mediterranean. The nexus of the three sets of relations are influencing each country's dealings with the other two and with a number of other countries, including the United States. These dynamics have important regional and global implications that the CSIS project seeks to assess. Cooperation and competition in economic and energy affairs are major drivers of all three bilateral relationships. Each country appears to be pursuing a strategy of deepening economic and energy cooperation with the other two even as they are engaged in competition of varying intensities for markets and political influence.

The volume and diversity of Turkey's economic relations with Russia and Iran have been expanding over the past several years. Oil and gas remain leading components, but construction, tourism, and transportation have also been important growth sectors. A Turkish speaker offered some macroeconomic data to set the context for the workshop, illustrating that economic relations between the three countries reflect a modest degree of connectivity, dominated by energy and low-end commerce. In his view, an abundance of energy supplies makes governments too powerful and stifles private sector development and economic diversification. He argued that there is the potential for a more organic economic relationship and a European level of regional economic integration rooted in industrial relations. Achieving this potential would require governments to foster a political and business climate where private economic actors can flourish along with a regional planning process and expanded private sector dialogues.

Eighty percent of Turkey's overall exports are in manufacturing. Private Turkish companies that are interacting with Europe are growing faster than others. Demand from Europe is very sophisticated, which contributed to urban development in Western Turkey. Turkey and Russia each export approximately 25 percent of the region's manufactured goods. Turkey's interaction with its southeastern neighbors, however, is on the low end—there is little demand for sophisticated products. There is considerable potential to change this consumption pattern.

The nature of Russian and Iranian political systems and regimes, as well as political and economic risks, will continue to impact expansion of their trade with Turkey. The growth of commercial relations will be affected by how well the three governments manage crises to Turkey's south, particularly in Syria. The global financial crisis led to a dip in commercial activities between Turkey and Russia in 2010. Pragmatism and mutual economic benefits have allowed Turkish-Iranian economic relations to develop over the past three decades despite enduring political differences. International efforts to isolate and sanction Iran over its nuclear program have made it increasingly difficult for Turkey and Iran to follow this course.

A Turkish participant cautioned against painting an overly optimistic picture of Turkey's relations with Iran and Russia, noting that neither neighbor wants to see Turkey achieve its ambitious objectives and expand its sphere of influence. Iran is waging an intense competition for influence with Turkey in the Middle East. Russia, while more relaxed about Turkey's activism, is concerned about Turkish soft power activities in Russia and neighboring states.

Turkey-Russia Economic Ties: Robust but Imbalanced

Economic relations with Turkey began to deepen during the late Soviet period. Turkey built industrial plants in the USSR with the loans provided by the Soviet government and it paid them back with food items. Early gas trade also functioned through barter mechanisms. In 1992, Turkey and the Russian Federation signed a treaty that set the context for normalization of relations and development of new transportation links.

Turkey and Russia have pledged to build a strategic partnership including political, economic, cultural, and security dimensions. Wide ranging cooperation was affirmed in the 30 articles of the January 2012 declaration of the second Turkish-Russian Joint Strategic Planning Group. Energy is Russia's strong card. Turkey's heavy dependence on Russian energy imports limits Ankara's freedom of maneuver and makes Russia an indispensable partner. A Turkish presenter argued that while Russia can make unilateral decisions on development of bilateral economic relations, Turkey has to weigh the concerns of EU countries and the United States concerning any deals with Moscow to safeguard its ties to the West. Turkey and Russia have some convergent interests, including economic and security cooperation in the Black Sea region and have taken common positions on certain political issues. Until Turkey regularly supports Russian positions on political and security issues, however, it cannot be characterized as a truly strategic partnership. Trade relations between Turkey and Russia remain very unbalanced and subject to political disruption. Russia imposed restrictions on Turkish imports in July 2008, citing concerns of illegal Turkish trading practices. This action, coupled with Turkish criticism of the Russian invasion of Georgia the following month, led to a year-long disruption of trade.

A Russian participant commented that many Russians perceive a change in Turkey's priorities and believe their southern neighbor is distancing itself from Western positions. This participant believes that Turkey aims to become a global actor that is not too closely aligned with any country. In the past, Turkish-Russian relations were a derivative of relations with the West. Past antagonisms have given way to pragmatic dealings. Turkey-Russia relations include a complicated mix of interests, which are more divergent than convergent. The relationship remains more tactical than strategic. There is economic interdependence, and the two governments have reached mutually-beneficial compromises on energy and trade relations. However, Turkey and Russia lack the common interests and foreign policy agenda that would constitute the basis for a truly strategic partnership.

While Turkey-Russian economic relations remain mutually beneficial, several participants expressed the assessment that the two countries would be hard pressed to achieve the goal of \$100 billion in total trade volume and that the current volume is not enough to pull Turkey away from its Western alignment. While there are important opportunities in Russia and Central Asia, a Turkish presenter concluded that Turkey is disinclined and unable to change its general foreign policy orientation toward the EU and the United States.

Iran's Strategy: Pragmatic Regionalism

An Iranian participant noted that since the end of the Iran–Iraq War in 1988, Iran has given highest priority to a policy of regional cooperation as a means to build trust and peaceful relations with neighboring states and diminish the risks of isolation. The collapse of the Soviet Union and the emergence of new states on its northern border, to which Iran has historical and cultural ties, gave further impetus to regionalism. Developing a positive relationship with Russia was seen as a way to counterbalance tensions with the West. Iran is also working to deepen economic relations with other Islamic neighbors—Iraq, Kazakhstan, and Pakistan. The strategy has been shaped by three main strains in Iranian politics. First, is the revolutionary ideology—initially rejectionist—that views Iran as neither West nor East, but an Islamic Republic open to good relations with other Islamic countries. The second strain is pragmatism, which has been reflected in regional policies. The third strain is expediency, which is the course followed when ideology and interests clash—as they often do vis a vis relations with Russia.

Iran's economic situation is shaped by two realities: an abundance of energy and fifteen neighboring countries, which facilitates its engagement in different regions. Iran has sought to use its enormous resource base to promote regional energy trade and cooperation and to build connectivity and interdependence that will reduce the impact of sanctions. Half of Iran's non-petroleum exports go to its neighbors.

Turkey-Iran Economic Relations: Moving Beyond Energy

An Iranian participant explained that Turkey holds a special place in the Iranian world view. Turkey, along with Malaysia and Indonesia, appeals to all four of the principal mindsets in Iran: the Islamic, merchant/bazaari, nationalistic, and technocratic. Among these three countries, Turkey is the only neighbor, and it has been governed since 2002 by an Islamist party which has treated Iran with great respect in its official dealings. Turkey's level of development offers Iran technological and financial assistance that it needs for its development. Ethnic Azeris, who comprise 25 percent of the Iranian population and favor improved relations with Turkey and Turkic countries, have also been a factor in expanding ties.

A Turkish participant noted that Iran–Turkey bilateral economic relations have gone through three periods: 1) During the Iran–Iraq War, when Iran's need for alternative land routes led to the expansion of transit trade; 2) After the collapse of the Soviet Union, when they agreed to construct a gas pipeline from Tabriz to Ankara; and, 3) the last decade, which has seen considerable expansion of energy and transit trade and tourism, despite significant political differences. Energy remains the dominant sector. Turkey imported over 50 percent of its oil from Iran in 2011 as well as 21 percent of natural gas. Over 160,000 large trucks crossed the Turkish–Iranian border in 2011, a route that is important for Turkish exports to Central Asia. Tourism has increased immensely, with 1.9 million Iranian tourists visiting Turkey last year, which has led to an expansion of shuttle trade. Many commercial interests in Turkey fear the loss of these economic ties if tensions over the Iranian nuclear program lead to deeper sanctions or a conflict. The presenter argued that Iran will try to leverage these interests to build political pressure on the Turkish government to rally to its side.

An Iranian participant argued that Turkey and Iran have the potential to realize the goal of doubling total trade volume (to \$30–35 billion) by 2015 set by the two governments in 2011 and reaffirmed during Prime Minister Erdoğan's March 2012 meetings with Iranian leaders. Energy will remain the major component, but there is potential for diversification. Iran imports \$60 billion of goods annually, including high end luxury goods, from Europe. Almost all of these goods could be produced in or imported from Turkey at lower cost if Turkish business leaders change their approach to the Iranian market and move away from their focus on low-end products and Iran took steps to improve its business climate. Bilateral trade could also expand considerably if Turkey became a base for joint ventures with European and other international companies to reach the Iranian market. Iran requires a sense of engagement from foreign companies and needs jobs. Companies can be successful in the Iranian market by producing one or more of their products in Iran, and importing a much larger quantity of the rest of their products. Turkey can't compete with India and China in Iran, but can compete with the Europeans.

There is also a potential for re-export of third country goods from Turkey. The United Arab Emirates (UAE) presently exports about \$16 billion of goods to Iran. These are not UAE products—they are European and sometimes American and Chinese goods. Iranian leaders want to diversify their economic channels and not be so dependent on Dubai. There are 550,000 Iranians living in the UAE and government institutions and individuals have huge real estate holdings and financial assets, to which they have access through the *hawala* system. The UAE government, afraid that the Iranians were taking over Dubai, has stopped issuing permits to Iranians and UAE banks stopped doing business with Iran under U.S. pressure. Hence, Iran is moving commercial activity to Turkey and other states including Armenia, Azerbaijan, and Turkmenistan. Turkey offered Iran major re-export facilities in Trabzon, but couldn't convince the Iranians to come. Still, there are over 2,000 firms financed by Iran with operations in Turkey. The number of Iranian firms in Turkey grew by 40 percent between 2010–2011, raising concerns among Turkish officials that many of these may be front companies set up to circumvent Western sanctions.

Other Turkish participants questioned the prospects for expanding trade relations with Iran. One stated that a preferential trade agreement with Iran was discussed during President Gul's trip in February 2011; however, nothing came out of it. Currently, Turkey is in arbitration with Iran on trade issues. It was also noted that there are strong protectionist tendencies in Iran and the business climate remains very opaque and difficult.

An Iranian participant argued that if Turkey continued to show respect to Iran and maintained economic ties, bilateral relations will be fine despite the differences over Syria and the Arab awakening. The Iranian regime is not that committed to Assad's survival; they want to maintain their regional constellation of influence. The speaker suggested that if Assad is removed from power but the current establishment is still in place, Iran will play along. The main source of tension with the West is when Iran feels disrespected. The current Iranian leaders' personalities were shaped during the Iran-Iraq war. They are not afraid of and don't respond well to threats.

Russia-Iran Economic Ties Remain Limited

There was broad agreement that the Russia–Iran relationship is the least developed and most difficult of the three sets of bilateral ties, with a history of rivalry and occasional cooperation. The regional, economic, and energy interests of the two countries are not convergent, yet there are elements of strategic partnership. Several participants argued that Russian leaders find Tehran's anti-Americanism useful as a way to balance U.S. political influence. Iran has developed its cooperation with Russia despite abiding historical suspicions about Moscow and its policies toward Muslim communities, in support of its common strategic goal of counterbalancing U.S. dominance and promoting a multipolar world.

An Iranian participant observed that Iranians across the board have a genuine distrust of Russia. Putin's Russia is a model to nationalists in Iran—President Ahmedinejad tried to implement a Medvedev-Putin transition plan, but it didn't work. The notion of following the Russian model of leveraging energy and economic relations to enhance Iran's global clout is also appealing to nationalists. However, the other three Iranian mindsets have no real counterparts in Russia. Russia-Iran relations reflect expediency—when Iran couldn't get technology or weaponry elsewhere, Russia became an option. Iran's efforts to improve relations with Russia have also been influenced by a desire to counterbalance the West. Iran showed restraint with respect to the conflicts in Chechnya and Georgia because it didn't want problems with Russia as tensions with the West deepened. This participant predicted that elements of competition in the relationship will become more prominent in the future. The quality of Russian-Iranian relations will depend on the course of Iran's relations with the West, particularly on the nuclear issue. If tensions decrease, the relationship has the potential to grow on the basis of expediency.

During the last decade, the Kremlin viewed Iran as a growing market, including for conventional arms and nuclear power plants, and a potential partner in balancing U.S. and Turkish influence in Central Asia and the Caucasus. The Kremlin has never shared the West's view of Iran as an urgent or even looming security threat. Bilateral relations soured after 2010 due to Russia's support of further UN sanctions on Iran, delays in finishing the Bushehr nuclear plant, and cancellation of the sale of the S-300 air defense missile system. However, as differences with Washington on arms control, missile defense, Syria, and other developments in the Middle East have grown over the past year, Moscow has found new scope for cooperation with Tehran.

Total annual bilateral trade between Iran and Russia is estimated to have tripled over the past decade, but the volume remains quite small—about \$4.2 billion in 2010. Russia accounts for about 2.5 percent of Iranian foreign trade volume, and Iran represents only 0.6 percent of Russia's. A Russian presenter argued that his country's economic ties with Iran have strategic value because it is Russia's largest trading partner in the Middle East and an important market for machinery, steel, and lumber. That presenter said Russia and Iran have common interests in the Caspian region, particularly in production and transportation of hydrocarbon resources, the development of north-south transport corridors, and the protection and sustainable use of its biological resources. The two governments maintain an intergovernmental dialogue on economic issues and have expressed a desire to expand volume to \$10 billion annually, but this does not seem like a priority for either side. There seems little potential for dramatic growth as the two economies are not complementary.

II. The Energy Dimension

The second workshop panel focused on the overall energy strategies of Russia, Turkey, and Iran and how energy trade and transit issues figure in the development of relations among the three countries and their dealings with third countries.

Russia's Energy Strategy to 2030

A Russian presenter noted that Russia's current energy strategy was adopted in 2009 with a long-term outlook. It envisions Russia emerging by 2030 as the focal point of the Eurasian energy pipeline infrastructure linking European and Asian energy markets. Turkey and Iran are important factors in the realization of this strategy. Turkey is one of the largest consumers of Russian energy resources and a major transit country. Iran is seen by Russian companies as a highly desirable potential partner in the development and production of hydrocarbons (mainly natural gas).

Russian energy export strategy seeks to achieve diversification of markets in terms of both types of energy resources and regions. Europe is expected to remain the main market for Russian energy resources, particularly natural gas, and Turkey plays a significant role in meeting that objective. However, the main focus of energy diversification efforts involves developing new markets in the Asia-Pacific region, which by 2030 could account for up to 26-27 percent of total Russian energy exports.

Maintaining Russia's position in Central and Western European markets requires: 1) unimpeded transit of Russian energy supplies through Ukraine and Belarus; and, 2) protection from potential competition posed by other producers from the Caspian region. Transit problems over the last decade with Belarus and Ukraine have undermined Russia's standing in the European market. This led to the decision in 2006 to construct the very expensive marine pipelines bypassing transit states—North Stream and South Stream. These pipelines will increase the volume of export gas transportation facilities available to Russia by more than 75 percent, yielding tremendous reserve capacity and room for maneuver.

Turkey's Energy Strategy

A Turkish presenter outlined Turkey's overall energy strategy. Turkey is seeking to: increase domestic resources by liberalizing its energy market and improving efficiency; ensure diversification of sources and suppliers as well as transportation routes; and, introduce and gradually increase the share of nuclear power in its energy mix. This three-pronged strategy is a consequence of Turkey's reliance on imports for around 91 percent of its oil and 98 percent of its natural gas consumption and an expected annual increase in overall energy demand of over 4 percent through 2020. As Russia and Iran are by far Turkey's two largest suppliers of oil and natural gas, Ankara sees cooperation with them as complementary to its goal of becoming a natural energy bridge between East and West, North and South and to Turkey's more traditional Western strategic alignment.

Over the past decade, in the face of diminished U.S. and EU engagement, Russia has emerged as one of Turkey's main partners in the energy field. Both Turkey and Russia attach importance to the principle of "mutual benefit" in energy relations. This "win-win" principle aims to establish a balanced interdependence to make cooperation possible on large projects. A key Turkish priority in energy dealings with Russia is to develop joint projects to redirect the flow of oil via tankers through the busy Bosphorus and Dardanelles straits, so as to avoid an environmental disaster and security risks in these heavily-populated areas.

Realization of the Southern Gas Corridor for the transport of Azeri and Turkmen gas to Europe has been another of Turkey's main energy policy priorities. Turkey is working with Azeri and Turkmen partners, as well as the EU, to find the optimum way to achieve this objective. In principle, the Turkish government supports all Southern Gas Corridor projects passing through its territory, but it is the Shah Deniz Consortium that ultimately decides which route will be used for transport to Europe.

Hard Bargaining: Russia–Turkey Energy Relations

Turkey is the third largest market for Russian gas and also imports coal, oil, and petroleum products. There have been discussions of joining electrical grids around the Black Sea and cooperation in the development of nuclear power. Turkey is also a partner in the development of infrastructure for the export of Russian hydrocarbons to foreign markets, primarily in Europe. While the Turkish government has taken a pragmatic approach to this cooperation with Russia, it has also driven a hard bargain on various deals to protect its differing interests.

The Turkish government showed interest in Russia's 2005 proposal to build a second Blue Stream gas pipeline between the two countries under the Black Sea (with a similar annual throughput capacity of 16 bcm), but later backed away due to concerns that its construction would undermine development of Nabucco. Turkey has supported the Nabucco project, which would bring hydrocarbons from Azerbaijan and later Central Asia to the European market bypassing Russia, as a way to diversify its supplies. Russia then opted to pursue South Stream, another underwater pipeline to Europe which would bypass Turkey.

Turkey and Russia have also been engaged in difficult negotiations on the Samsun-Ceyhan oil pipeline, which would be constructed across Turkey from the Black Sea city of Samsun to the Mediterranean port of Ceyhan, to bypass the Bosphorus and Dardanelles straits. This would be the Russian oil industry's largest joint project with a projected capacity of 60-70 million tons annually at an estimated cost of \$3 billion. In September 2011 the Russian company Transneft announced the suspension of negotiations on the project. Some observers thought the suspension of talks was taken to pressure Turkey to issue a permit for construction of South Stream, and some in Turkey thought the move was taken to express discontent with Turkey's decision to host NATO missile defense radars. A Russian presenter contended that it is more likely attributable to the project's high cost and uncertain viability.

To secure Turkey's support for the South Stream deal, Russia offered to discuss construction of the Samsun-Ceyhan oil pipeline and of the Akkuyu nuclear power plant as a package deal. Negotiations on the package broke down after Turkey secured a deal with Azerbaijan on the Shah Deniz II gas field and Trans-Anatolia Pipeline that would supply gas to Nabucco and/or the Trans-Adriatic Pipeline. Finally, in December 2011, the two governments were able to close a major agreement on energy. Turkey granted Russia all the necessary permissions for laying an underwater pipeline across Turkey's exclusive economic zone in the Black Sea and the subsequent transportation of Russian gas to Europe. The two governments also struck a deal to extend to 2025, Turkish purchase of reduced volumes of Russian gas through the Trans-Balkan pipeline that traverses Ukraine, Romania, and Bulgaria. They also agreed that deliveries of Russian gas in 2012 will be increased by 2 bcm (to a total of 28 bcm) at a discounted price. It was noted that South Stream will be very expensive and not economically efficient, but reliable routes are more important for Russian leaders today.

While the Russian government and companies are waging a vigorous campaign in Turkey and neighboring countries to prevent construction of the Southern Corridor to protect markets they presently dominate in southeastern Europe, many Turkish officials believe the Russians know it will be completed and is seeking to benefit from it and mitigate its adverse impact on Russian interests. There was also discussion of whether Russia alone could supply the 63 bcm of gas needed to feed into South Stream or whether some of the gas will come from the Caspian, which a Russian expert agreed is likely.

Cooperation between Russia and Turkey in the field of nuclear energy has been more successful. The two governments agreed to build Turkey's first nuclear power plant at Akkuyu in the Mediterranean province of Mersin. The Russian state-controlled firm AtomStroy Export is scheduled to start building four reactors with a capacity of 1.2 gigawatts in 2013 and pay the total construction cost of \$20 billion. Turkey established a joint-stock company to guide commercial exploitation of the power units but all the shares will initially be owned by companies authorized by the Russian side. A Turkish participant noted that heightened public concerns about nuclear power in the wake of the Fukushima disaster has led to additional safety measures that may result in the postponement of construction. There is speculation that Turkey is open to having Russia build a second nuclear power plant. A Turkish speaker said this is still unclear and will likely depend on the success of Akkuyu, but provisions of the current deal, which provide for training of Turkish nuclear scientists in Russia, could help foster expanded cooperation.

Iran's Energy Prospects and Strategy

Assessing the future of Iran's energy sector, an Iranian participant noted that in the past decade many predicted that Iran would become a net importer of energy and that the Iranian energy sector would collapse due to lack of investment and technology. However, the speaker distinguished between the oil sector, which is declining due to lack of technology and investment, and the gas sector, which is growing. Iran seeks to reach production levels of 5 million barrels a day (bbd), but the reality is closer to 3.5 million barrels.

The gas sector has much better prospects. The subsidy reforms, initiated in December 2010, reduced domestic gas consumption and created additional gas capacity (100 million cubic meters a day), allowing Iran to become a net exporter of gas in 2011. Domestic gas savings are expected to support expanded exports and use for other purposes, such as electric power generation. This participant assesses that Iran will not achieve its official goal of producing 1.5 billion cubic meters of gas a day (bcd) by 2015. Between 1998-2005 with considerable Western technology (TOTAL, Gazprom, Shell, ENI, Statoil), Iran developed the South Pars field, organized in 24 phases. Only 10 phases have come upstream so far. Therefore attention should be directed to the development of gas based industries rather than gas.

The major growth sector for Iranian energy exports will likely be electricity more than gas. Iran has connections to the electric power grids in Turkey, Iraq, Afghanistan, and Turkmenistan. Electricity generation from gas has a value added component and creates domestic jobs and investment. Iran now has indigenous technology to build power plants. Cement is another form of exporting energy but with added value. Iran has become the fourth largest cement manufacturer in the world. The presenter expects Iran's raw gas exports will be mainly focused on the immediate neighboring markets.

The Lure of Energy in Turkey-Iran Relations

A Turkish presenter noted that expanded energy trade has long been a major enticement in Iranian efforts to foster cooperative political ties, but it has proven disappointing. Iran has been a less reliable partner for Turkey than Russia. Over the decade that there has been a gas pipeline connection, Iran has repeatedly failed to supply Turkey's contracted 10 bcm of natural gas a year and there have been some concerns about quality. Growing tensions over Syria and Iraq and political change in the region have further diminished Turkish interest in energy trade with Iran and a recent dispute on contractual obligations has led the Turkish government to seek international arbitration. Despite these difficulties, the reality is that Turkey needs Iranian gas to meet its domestic needs. Therefore, Turkey still hopes to cooperate on energy projects such as the development of pipelines from the South Pars gas field and on electricity power stations in Eastern Anatolia.

While Ankara supports international efforts to stop Iran from developing nuclear weapons, bilateral nuclear energy cooperation might be possible if Iran were to bring its program into compliance with IAEA safeguards. Turkish policy is that continued engagement with Iran on energy development projects is important as they can take years to put into operation and none of the countries dealing with Tehran on energy matters can afford to wait until sanctions run their course. Turkey hopes and believes that one day the international political situation will change and wants its companies operating in the energy field to be ready to accelerate activities in Iran.

Russia-Iran: Limited Energy Trade and Market Competition

An American presenter noted that there is presently no quantifiable energy trade between Russia and Iran. The two countries have worked together to exploit gas reserves in the Caspian and signed a treaty in 2008

agreeing to cooperate on development of Iran's gas and oil reserves. The two governments established a bilateral committee in 2011 that developed a "Road Map for Energy Cooperation." A Russian expert said that Russian energy companies are interested in exploration and production of Iranian resources, but have proceeded very cautiously in recent years due to international sanctions on Iran. The supply of Russian oil products to Iran has practically stopped. Lukoil pulled out of an oil exploration project in western Iran and stopped delivery of diesel fuel to Iran in order to protect its investments in the United States. However, state-owned Russian firms are still pursuing oil and gas exploitation, processing, and transportation projects in Iran. There was general agreement that Iran would benefit from access to Russian extraction and exploitation technology, so there is still scope for bilateral cooperation.

Russia and Iran are founding members and promoters of the Gas Exporting Countries Forum, and together hold about 40 percent of global natural gas reserves; however, this cooperation has been largely declarative. Indeed, the two countries see themselves as long-term competitors in the European and global energy markets. Iran's isolation from the West actually helps to maintain Russia's dominance of the European gas market. A Russian presenter commented that engagement with the Iranian oil and gas industry, including development of transport routes, would enhance Russia's position in Central and South Asia and the Middle East while contributing to the energy security of these regions.

In the electricity sector, cooperation between Russia and Iran is expected to intensify as they implement agreements on the synchronization of their electric systems via Azerbaijan, as well as on mutual supplies of electricity to neighboring countries. Russia may supply fuel for the existing Bushehr nuclear reactor, build a second unit at the Bushehr, and participate in construction of new nuclear power plants in Khuzestan province.

Competing Interests in the Caspian

Because of its central position within Eurasia, the Caspian region could become a key segment of the transcontinental systems for transportation of energy along the north-south and east-west axes. A Russian participant explained that the Caspian and Central Asian regions provide critical East-West transit routes for Russian energy. Russia's interests are to control routes for Caspian Basin energy flows while preventing the development of alternative routes. Turkmenistan, Kazakhstan, Azerbaijan, and Uzbekistan have the potential to become serious competitors for Russian exports to Europe. Russia's strategy over the past decade has been to prevent direct access of Central Asian gas to Europe, while retaining maximum control over supplies and subsequent resale of gas from these sources in foreign markets under a system of Gazprom purchases. The collapse of demand for gas in 2009 partially destroyed this arrangement; however, Russia remains the largest buyer of gas in the region. The desire of Caspian countries to diversify their gas markets has also led to changes in regional energy trade.

Moscow and Tehran hold divergent positions on demarcation of the Caspian Sea, but both oppose development of the trans-Caspian pipeline that would bring Central Asian hydrocarbons to Europe. A Turkish participant argued that this difference should not be seen as a major source of friction between the two, as the Soviet Union has left a legacy which is beneficial to Iran. The deepest waters of the Caspian Sea are on the Iranian side, but it doesn't make sense to develop those fields. Iran has the reserves which it can use in the future. It will not develop them but make others feel its presence.

A Russian speaker noted that all the major powers have been actively involved in promoting the redistribution of the oil and gas markets of the Caspian region. The United States has been promoting diversification and seeking opportunities in energy development as a way to advance regional political goals. Russia, China, and Iran seek to reduce U.S. and EU influence in the region as they consider the flow of Caspian gas to the West a threat to their interests. Turkey seeks to use its regional influence and

central geographic location to play a central role of the transit of Caspian hydrocarbons, and is actively supported by the United States.

An American participant noted that Russia is forming the integrated Eurasian transport system between Europe and Asia by building excess pipeline capacity. It now has surplus oil capacity such that it can offer a country like Kazakhstan to transit its oil to market via the Russian pipeline system to Asia or Europe. Russian oil flows through the Black Sea, partly as a result of these pipelines, has diminished in the last few years. Turkey is buying less Russian oil because less Russian oil is moving into the Black Sea. So what is the Bosphorus bypass pipeline project for from a Russian perspective? Is it really to secure the Russian oil flow from the Black Sea which is already diminishing, or is it to extract economic rent from the Kazakh flows into the Black Sea which is increasing? He questioned the need for the Turkey bypass pipeline.

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