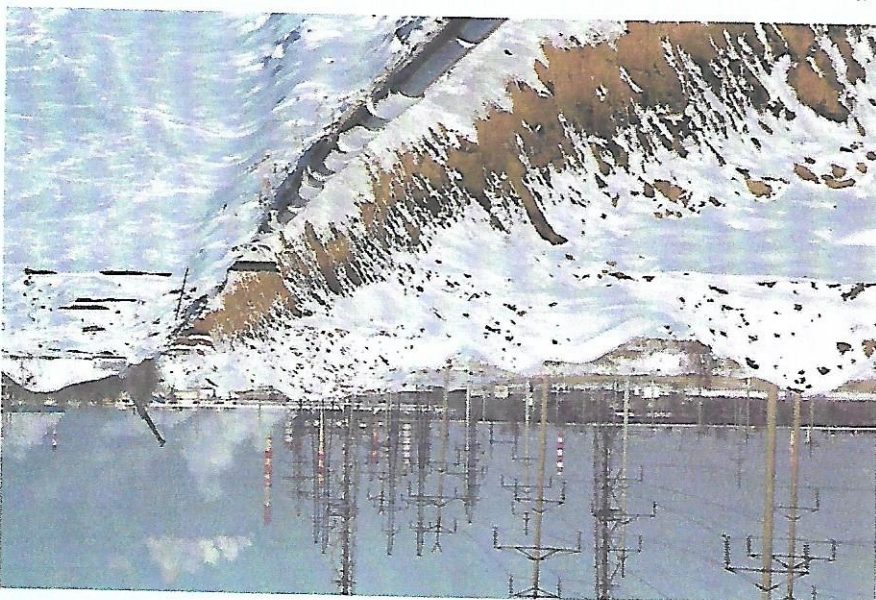


OPENING CASE STUDY

The politics of gas in Russia



Russia's extreme Arctic conditions present challenges for the oil and gas industries. Source: iStock.com/Berkut_34.

With claim to the world's largest gas reserves, Russia has huge potential for wealth generation from energy exports. The strong state tradition of its vast territory, along with satellite territories over which it has historically exerted control, has made the exploitation of gas pivotal in the eyes of rulers in Moscow. This was true in the former Soviet Union, and remains true today. The break-up of the Soviet communist dictatorship in 1991 marked the start of a period of political and economic instability. The sale of former state assets led to the rise of powerful business oligarchs, the leaders of newly privatized industries. New democratic political institutions promised accountability of government, but became mired in corruption and infighting among new business and political powerbrokers. The election of Vladimir Putin as president in 2000 promised to restore order and refocus the economy. His nationalist message was clear, and he intended to reassert Russian influence in former Soviet territories. This was a message that appealed to the Russian populace, boosting the popularity of his United Russia party. His success would

depend heavily on the country's main source of wealth – its gas industry. Bringing energy under Kremlin control would be crucial to consolidating the political power. Political legitimacy and economic power seemed to go hand in hand. Gazprom, the former Soviet gas ministry that had been privatized in the 1990s, was restored to state control, headed by a Putin associate. Other resource assets went the same way. Yukoil, the privatized oil company, was broken up and its owners imprisoned. The assets were awarded to Putin associates. In the Russia of Putin, Kremlin-linked individuals became the new oligarchs, able to gain rich rewards but on condition of loyalty to Putin. The economy became concentrated in the hands of these individuals, and, ultimately, under Putin's political control. In addition, Gazprom bought out Russian media businesses, helping to consolidate Putin's control of the media. In a world of rising energy prices, the potential for wealth generation was seen as phenomenal. Russian optimists foresaw Gazprom overtaking companies like US giant, ExxonMobil. Global investors enthused, and

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Figure 1

- In what ways is Gazprom an example of subservience of a company to political leadership rather than business decision-making?
- How has the global political environment affected the Russian energy sector?
- What are the risks faced by western companies when working with Russian companies?
- How stable is Putin's rule in terms of political and economic conditions?

Russia was branded a BRIC economy, along with the fast-growing emerging economies of China, Brazil and India. But Russia was different, with a history of industrialization dating from the Soviet era, when its energy resources were a source of its power. In the post-Soviet era, however, the exploitation of Russia's gas has been dependent increasingly on partnerships with western oil companies. In particular, reserves in harsh locations, such as offshore and in Arctic locations, have seen the involvement of BP, Shell, ExxonMobil and the large service companies such as Schlumberger. In 2008, when Gazprom's confidence was high, it was valued at \$367 billion, but the deterioration in the economic environment by 2015 saw its value slip to just \$51 billion (Burke, 2015). The fall in energy prices globally was a big factor. The price of oil had fallen from \$100 a barrel to \$50 by 2015. The other big factor affecting Russia was sanctions imposed by the western countries whose companies had been active in Russia. Russia sits on the world's largest reserves of shale oil, which make up 25% of its total reserves. The US has seen a boom in shale production, and Russia, which has greater shale reserves than the US, hoped to duplicate its success. Exploiting these resources, however, involves fracking technology, in which western companies have developed expertise. In the days of the Soviet Union, all the equipment used in the energy industries was Soviet manufactured. Nowadays, western oil-service companies hold the key, in fracking as well as in the technology to explore and tap resources offshore and in the Arctic regions. Without these companies, Russia's energy sector is vulnerable to dwindling production. These companies' activities were restricted by sanctions imposed on Russia when Putin ordered the annexation of Crimea in Ukraine in 2014. Although appealing to Russian nationalist sentiment, the move was damaging economically, and Ukraine became politically destabilized, with violent conflicts between