Introduction

Europe's dependency on Russian gas, especially in Central and Eastern Europe, has become a major strategic liability for the West. This is especially true as the war in Eastern Ukraine has brought relations between Moscow and Brussels as well as many of the European capitals to new lows. Russia enjoys a de facto monopoly on gas supplies to the Baltic States, Bulgaria, Moldova, Serbia, and Slovakia, as well as dominating the energy scene in Hungary and other European countries. This raises serious questions with regards to the Kremlin's political influence in capitals from the heart of Europe to the Mediterranean. Allegations of corruption permeate political debates about the Russian gas supply and are putting increasing pressure on the EU and the nation-states to find economic alternatives.

This is not the first time the Central and East European countries find themselves in a vulnerable position vis-à-vis Moscow. In early 2009, Ukraine rejected Russia's proposal to raise gas prices from $179.50 to $250 per 1,000 cubic meters. Vladimir Putin, then Prime Minister, accused Ukraine of siphoning off gas and ordered Gazprom to shut down all gas transit via Ukraine. As temperatures dropped below zero degrees Fahrenheit, it wasn't just Ukraine feeling the effects of the disruption, but also 18 other European countries: Austria, Bosnia, Bulgaria, Croatia, Czech Republic, France, Germany, Greece, Hungary, Italy, Macedonia, Moldova, Poland, Romania, Serbia, Slovakia, Slovenia, and Turkey. The cut off, which led to a state of emergency in Slovakia and the closing of several factories in Bulgaria, served as a wakeup call for the EU.

The situation today is not as dire, and based on Energy Security Stress Test released by the European Commission last month, if all member states cooperate, protected consumers would not be affected during a prolonged disruption. The Commission's report also states that Bosnia, Bulgaria, Estonia, Finland, Herzegovina, Macedonia and Serbia are most vulnerable.

There is somewhat different picture when it comes to the nuclear sector. To reach its energy security and 2020 carbon emission goals and to reduce its overall exposure to energy security risks, Europe will have to diversify its sources of electricity beyond still very expensive renewables and recognize the continuing importance of nuclear energy, a sector in which the security of supply is driven by market competition. The Russian government has made a conscious effort to support, promote and build this flagship industry. Rosatom's turnkey solution allows for competitive pricing, which has led to a doubling of the company's international construction portfolio from the $50 billion in 2012 to an expected $100 billion by the end of this year. Meantime, US-based Westinghouse has tried to secure long-term contracts in Europe, and it is now taking advantage of the political and security tension between the EU and Russia over Ukraine. Thus, the stage is set for a competitive match.

Energy supplies to Central and Eastern Europe, and especially the Balkans, have become a "football" in the worsening relations between Russia and the West – and the countries of the region. What is needed is dispassionate policy analysis taking into account both geopolitical and

economic factors, which this article attempts to provide.

Europe's Natural Gas Dependency

According to the European Commission, the European Union consumed around 530 billion cubic meters (bcm) of gas in 2010. The European gas demand has been stagnating since 2010, when it peaked as a result of a colder winter than usual. Nevertheless, analysts do not foresee any significant growth in future gas consumption. At least until 2020, the European gas demand is unlikely to increase due to a weak economic recovery in the gas-intensive European industry sectors, if any. Improved insulation of apartment buildings and more efficient use of renewable energy sources all across the continent will also contribute to the stagnation of gas demand.

The following table demonstrates Europe's energy dependency on Russian gas:

Gas Imports from Russia (bcm)	**2012**
Percentage of Russian gas in total imports (%)	**2012**
Austria	
5.2	
76.1	

Bosnia

0.2

n/a

Bulgaria

2.9

100

Croatia

0.2

n/a

Czech Republic

7.9

58.6

France

8.6

26.1

Germany

41

31

Greece

2.6

55.6

Hungary

6

100

Italy

25.3

32.6

Poland

12.9

81.3

Romania

1.4

100

Serbia

2

n/a

Slovakia

5.5

83.5

Slovenia

0.5

60.2

(Source: Oxford Energy , Eurogas, Moody's Analytics)

To prevent gas crises from happening again, and to diversify the European Union's sources of

gas, a series of projects have been proposed. These include interconnectors, liquid natural gas (LNG) terminals (such as at Krk Island, Croatia), and an additional pipeline, which would bring Caspian gas to the region. The goal is to supply Caspian and eventually Central Asian gas to Europe from and through countries that are more reliable and less politically motivated partners than Russia.

The most promising are Nabucco-West, the Trans Adriatic Pipeline (TAP, connecting Greece, Albania and Italy), and the Trans Anatolian Pipeline (TANAP, connecting Georgia and Greece through Turkey). It is planned to connect TANAP to the already operational South Caucasus Pipeline, supplying Turkey and Georgia with gas from the Caspian basin. This raises the question of whether Turkey's geopolitical dynamics today make Ankara a more reliable partner than Moscow. Time will tell.

If the "Islamic State" is defeated and the outstanding issues between the Kurdish Regional Government and the central government in Baghdad are resolved, proposed pipelines from Iraqi Kurdistan to Turkey might be added to the mix. Even more promising is the development of offshore gas that could be exported to Europe from the Eastern Mediterranean (Israel, Cyprus and Greece) as LNG or via a pipe.

To shield the EU countries, its most important clients, from potential disruptions that might occur along the Ukrainian pipeline network, Gazprom, together with its partners in the Balkans and Central Europe, launched construction of the South Stream project in 2012. The pipeline will bring Russian gas through the Black Sea to Bulgaria, Serbia, Hungary, Austria, and Greece.

South Stream will transport gas directly from Russia through the Black Sea to its consumers in the Balkans and part of Central Europe, with plans to become operational in late 2015. Even though 58% of the public in Bulgaria, Hungry, Italy, Serbia and Slovenia believe that "the advantages of South Stream outweigh the disadvantages," it must still meet all EU regulations in order for its onshore terminal to operate.

Following the April 17, 2014 decision by the European Parliament to adopt a non-binding resolution against South Stream, Bulgaria has declared that the construction halted in June. In April, Russia turned to the World Trade Organization (WTO) and launched a complaint against EU's "Third Energy Package." The WTO decision will play an important role in the future of EU-Russian energy relations and will affect the energy mix in the Balkans.

The lack of common energy policy within the EU makes consensus on major projects and policies virtually impossible. Each member is following its own political and/or economic goals. For example, Slovakia has been vocal in opposing South Stream. Hungary, Austria and several Balkan countries on the other hand are very welcoming of the potential jobs and transit fees

resulting from a successful completion of South Stream.

While some EU countries have been able to or are actively trying to diversify their energy sources and loosen the Russian grip on their economies, the energy tug of war between the EU and US on one side and Russia on the other has only intensified in the Balkans.

Serbia, Russia's Best Friend?

Serbian ties to Russia harken back to the 19th century, when the Romanov Empire supported Belgrade in its struggle against the Ottomans and the Hapsburgs. Russia has been a vocal supporter of Serbia when it opposed Kosovo's independence.

The economic ties between the two countries are especially strong in the energy sector. Gazprom owns 56.15% of Serbia's oil monopoly Naftna Industrija Srbije (NIS). The undergrou nd gas storage , Banatski Dvor, is owned by a Gazprom (51%) and Srbijagas (49%). As Serbia continues its push for EU accession it seems that the country will have to make some difficult political and economic choices.

In late October 2014, Russia cut gas to Serbia by 28% because of its debt of $224 million and a general decrease in exports to Eastern European countries due to the Ukrainian conflict. The supply returned to normal just couple weeks later following talks between Aleksandar Vučić, the Serbian PM, and President Vladimir Putin and a subsequent repayment schedule agreement. Many Serbs turned out to pro-Putin demonstrations in Belgrade.

Serbia's energy sector is already strained due to coal shortage caused by floods, limiting the supply to the Nikola Tesla power plant that generates about half of the country's electricity. The Serbian power utility Elektroprivreda Srbije (EPS) announced that it will have to purchase electricity from abroad. Serbian reserves, in storage facilities largely owned by Gazprom, can meet household demand for three months.

Even though the South Stream project would make the country a regional energy hub while creating about 20,000 jobs, Belgrade will not advance on the South Stream pipeline without EU consent. The Serbian Prime Minister Aleksandar Vucic made his position clear when he declared , "As I said in front of Vladimir Putin … our strategic goal, our strategic aim, is our EU path. And I do not lie to anyone, all the politicians from all over the world know that."

Map: South Stream


AUSTRIA
BUDAPEST
Tarvisio
Ratece
Lendava
HUNGARY
GAZPROM
mvm
South Stream Hungary Zrt.
GAZPROM
Plinovodi
SLOVENIA
South Stream Slovenia LLC
LJUBLJANA
Pecs
Backi Breg
CROATIA
ZAGREB
Slobodnica
Banja Luka
GAZPROM
plinacro
Republika Srpska
Novi Sad
BIJAGS
SARAJEVO
BOSNIA AND HERZEGOVINA
Zajecar
ITALY
SERBIA
ROME
MONTENEGRO
GAZPROM
СРБИЈАГАС
South Stream Serbia AG
PODGORICA
SOFIA
ADRIATIC