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Why is Russia Looking For Natural Gas in Africa?

SUMMARY

- Recent news that Russia’s state-owned natural gas company Gazprom, despite controlling the largest natural gas reserves in the world, is in talks to exploit Nigerian natural gas resources reveals the next step in an aggressive expansion strategy.
- Gazprom is already fighting hard to prevent competitors from intruding on its traditional markets in Europe.
- The move into Africa will allow the Russian state company to expand both production and distribution and, more importantly, could position Gazprom to found a new energy cartel—an OPEC for natural gas—in a process that may be set in motion as early as this summer.
- The U.S. and the rest of the world need to consider the consequences of the formation of a natural gas OPEC, with Russia as its controlling member.

ANALYSIS

If the natural gas market was a game of Monopoly, Russia would already control Boardwalk and Park Place. But you can’t win with just those two properties, and Russia knows it.

Russia’s Newest African Investment

The Russian state-owned natural gas behemoth Gazprom was already building a liquefied natural gas (LNG) plant in Equatorial Guinea when it announced in January that it is in talks with the government of Nigeria to spend up to \$2.5 billion to develop Nigerian natural gas resources. The investment is a staggering one, especially for a nation that already supplies most of Europe with natural gas produced within its own borders. The question is, why: why would Gazprom—and the Russian government—make this move at this time?

Domestic Production Not Enough for Gazprom’s Plans

The first reason for Gazprom’s move into Africa is the simplest: there’s not enough gas in Russia. Or, more precisely, not enough gas in fields that Gazprom wants to use. Russia sits upon more than a quarter of the world’s natural gas; they control 1,700 trillion cubic feet of proven conventional natural gas reserves, nearly 75 percent more than their nearest

competitor. But the three largest Gazprom fields in Russia have peaked, and are now declining at an average rate of 700 billion cubic feet per year. Much of the remaining Russian gas is located in smaller fields that the state-controlled company isn't interested in developing. And no one else can: private companies are effectively barred from trying to compete with—or even operate alongside—the state-owned monopoly.

While domestic supply has become more problematic, natural gas consumption within Russia has continued to grow. Interestingly, the consumption growth has been largely due to economic expansion that in turn was due to Russia's profitable oil and natural gas industries. In other words, Russians are using more gas as a direct result of having sold more gas in recent years. And Gazprom is the only source of it: as the official government-controlled monopoly, it is required to deliver gas domestically at government-determined prices, regardless of profitability. Combined with aging, poorly maintained transportation infrastructure, and bureaucratic inefficiency, the end result is that Gazprom is looking across the world for new sources of production.

The Fight For Europe

Gazprom also wants to make sure competition doesn't threaten its familiar stomping grounds outside of Russia. Europe depends on Russia for its natural gas, and Gazprom depends on Europe for its business. More than a quarter of the natural gas consumed in Europe is imported from Russia, representing half of Russian exports. European nations are not comfortable with that dependency on Russia and are looking for other sources of gas. At the moment, their effort to diversify has not done enough to keep up with rising consumption and falling domestic production. But pipeline supplies from former Soviet states, along with LNG from Africa, have the potential to someday threaten Gazprom's market share in the Russians' traditional European markets.

Today only Azerbaijan has direct pipeline access to Europe that bypasses Russia, but discussions are underway to extend that pipeline to the much larger gas fields of Turkmenistan and Kazakhstan. Gazprom has moved aggressively to counter that movement and continue to dominate Europe through the pincers of the proposed Nordstream and Southstream pipelines. Nevertheless, the Russians are obviously becoming aware that they must reach out to customers further afield, especially in the U.S. market, which Nigeria is well-placed to supply.

Russia's New OPEC

The move into Africa helps fulfill that next step in Gazprom's aggressive strategy, and more: the African investment could in fact give Russia substantial control of world gas production ... and therefore world gas prices. Today, natural gas is a regional commodity. But meetings in Moscow as soon as this July are expected to formally discuss formation of the Organization to Gas Producing Countries, an OPEC for natural gas in which Gazprom would play the role of swing producer, similar to the role that Saudi Arabia plays in oil markets. Such a multi-state cartel would create a global market for natural gas, a market over which Russia would have tremendous influence.

The implications for the United States are real and significant. For decades, we have struggled with a distorted world oil market and unpredictable oil prices thanks at least in part to price manipulation by OPEC. Now, we could be facing an entirely new challenge as we are exposed to gas security concerns for the first time. Policymakers need to ask whether a Russia that is extracting natural gas from Africa, supplying to the entire world, and leading a new monopolistic consortium of gas-producing nations is in our best interest.

Gazprom already has Boardwalk and Park Place ... and they could control most of the board soon enough.