

The Geopolitics of Energy in the Silk Road Region and
its Implications for Hungary and Europe*

by

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I want to start by connecting some geopolitical dots that are relevant to the question of the EU's energy security and the role of Azerbaijan in this context, as well as touch upon the role of various neighbors in this regard.

And that means starting with Ukraine.

We would not be having a deadly serious conversation about Azerbaijan's essential—*indispensable*—role in the diversification of energy supply to the EU and the Western Balkans were it not for this war. More specifically, the trend of strategically deepening EU-Azerbaijan engagement is a consequence of the choices the EU made to impose sanctions on Russia and divest from its dependence on Russian oil and gas.

Now, since the onset of the war, the EU has engaged more deeply in the South Caucasus part of the Silk Road region on two basic fronts: *one*, peace; *two*, connectivity—so, you know, energy and transport and so on. I'll say something about each in turn, but I'll focus more on the second because this is what I have been asked to do this afternoon.

So, the first is to strengthen the role of Brussels as a facilitator in the peace talks between Armenia and Azerbaijan. The EU saw an opportunity to engage politically in the talks because Russia got tragically engulfed in a neighboring theater.

Now, it's important to note that this EU engagement predates 24 February 2022, but also that it has gotten more intense since then—since the onset of the present stage in the conflict over Ukraine.

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I'm happy to get into the details later on. But my basic takeaway is that February 2022 has tilted the geopolitical balance in favor of overall strategic engagement with Azerbaijan by the EU.

I want also to add, notwithstanding the *strategic* argument, there have been some *tactical setbacks*, and this is largely due to internal EU reasons—intra-EU power dynamics...the insistence by Emmanuel Macron to be a part of the EU-led—the Charles Michel-led—peace process is one of the main reasons. And I'm happy to get into the nitty-gritty later on.

But it does not affect the big picture. My general point holds: the trend of strategically deepening EU-Azerbaijan engagement is a consequence of the choices the EU made in terms of its response to the onset of the present stage in the conflict over Ukraine.

And this is manifested through the deeper EU engagement in facilitating the peace talks between Armenia and Azerbaijan. Now, this is the first time the EU has gotten involved in this conflict.

And there is another manifestation of this strategic deepening—and that's connectivity.

Here, there has been no tactical setback.

Now, connectivity in this context has two interdependent aspects. The first is energy, and the second is land-based transportation corridors between the EU and Asia—you know, Global Gateway, Middle Corridor, Belt and Road Initiative...all that stuff. And with respect to both of these (energy and connectivity), Azerbaijan is *indispensable* to the fulfillment of EU strategic ambitions.

Again: for the EU, Azerbaijan has become the indispensable country of Eurasia—of what I like to call the Silk Road region.

Again, and obviously, this new approach by the EU is part of the EU's response to the conflict over Ukraine—and in that sense, it's *reactive*. But it's also *proactive*—in the sense that it seems like the concrete development of earlier threads of thinking within the context of intra-EU debates about “strategic autonomy.” And I suppose you know that this is a term that people like Macron brought to the fore a few years back, and that it was resurrected by Borrell in Samarkand late last year, during his keynote address at the first-ever EU-Central Asia conference on connectivity centered on the Global Gateway.

But strategic autonomy from whom?

Well, the obvious answer is Russia.

But I think it may also point to the quest for strategic autonomy from two other superpowers, as well: China, but in some respects, America, too.

My point is that—it seems to me—one important aspect of EU strategic thinking, embodied in the European Political Community initiative that was launched last year in Prague, is that the EPC was designed by the EU to better define the conceptual distinction between greater Europe and the great powers.

So, Russia and China—I'm forecasting that Macron's forthcoming state visit to China will feature some sort of manifestation of this strategic autonomy approach.

The last part of my "strategic autonomy from whom?" answer is the United States. I see a kind of attempt by the EU and some of its leading member states to establish some sort of equilibrium with America.

To demonstrate that there are *two* pillars of the West—not just *one*.

To demonstrate that greater Europe—this greater Europe led by the EU and the attraction it offers to the other participants in the EPC initiative, including Azerbaijan but not the Central Asian states—to demonstrate that this greater Europe is not going to be satisfied with being simply an *extension* of American power, or of being *completely dependent* on American power.

Now, I think that some of the threads of this line of thinking have been woven together in the context of Azerbaijan.

And I want to illustrate this with two examples.

The first a relatively obscure, but I think it's important and so I want to spend a few minutes on this.

It concerns the ongoing attempt to complete the negotiations between Baku and Brussels on something called the Comprehensive and Enhanced Partnership Agreement (CEPA).

Well, these negotiations have been going on since 2017 and got intense about a year ago.

So, what's the holdup?

Without getting into the details, I want to underline that Azerbaijan has been able to make these negotiations into *real and substantive* negotiations.

What do I mean by that? Well, the EU is used to conducting what amounts to a one-sided negotiation with the countries on its periphery. And from the perspective of Brussels, this is completely reasonable. It has to do with the disbalance of power. Right?

So, look at how membership accession negotiations really work. I'm Serbian, and I was involved in these things from 2004-2012, so I have some basic understanding of this. And we're in Hungary, so what I say will be immediately recognizable to you, I think. By analogy.

Now, in practice, the EU says, basically, "here's what you need to do, and we will evaluate your progress, and when we are satisfied, then you get to move forward." And the other side spends all its time doing what the EU tells it to do. The other side doesn't get to evaluate the EU or get the EU to compromise on its starting position.

So, this type of negotiation is not really a negotiation in the everyday language sense of the term. It's more like taking your car for an inspection before you're allowed to register it. There's no room for compromise. You don't negotiate with the people doing the inspection. Your car has to fulfill the criteria and if it doesn't, then it fails the inspection.

Now, my point is that Azerbaijan has managed to turn the negotiation on this new Comprehensive and Enhanced Partnership Agreement (CEPA) into a *real and substantive* negotiation. So, *not* like a car inspection. And it has done so better than any of the other Eastern Partnership states—most of them “negotiated” like the official candidate countries.

And lots of other countries are paying attention to what Azerbaijan is doing. Because it could set an important and far-reaching precedent for the way the EU negotiates with sovereign states—and not just in the context of greater Europe or even the Silk Road region.

Ok?

Now, my second illustration about how Azerbaijan fits into an EU line of thinking that attempts to establish some sort of equilibrium between the United States and the EU—that Europe is not going to be satisfied with being simply an *extension* of American power, or of being *completely dependent* on American power—well, Azerbaijan fits into this in the context of the EU’s growing connectivity ambitions.

And this holds true both in the context of internal EU ambitions and external EU ambitions...

Internal because of the desire to diversify energy supplies and strengthen its economy, which is predicated on the reliable and predictably priced supply of energy.

And *external* because of the EU’s desire to project its power and influence beyond its borders to the east (Silk Road region). This is the EU version of the “the rules-based international order”—as Borrell put it in Samarkand, which he defined as “making states secure, people free, and companies willing to invest.”

Now, aside from energy (which I’ve already discussed) connectivity here means all sorts of things: digital infrastructure, security architecture, food supplies, and access to critical raw materials, and so on.

And I don’t want to get into the connectivity stuff here for reasons of time, except to say that all EU connectivity with Central Asia is predicated on the EU’s successful strategic engagement with Azerbaijan.

Here’s is the fundamental point: Global Gateway and the Middle Corridor and all the rest of it cannot be realized without Azerbaijan’s full-on participation and engagement. Azerbaijan is the indispensable predicate. It’s the indispensable country.

Ok? Again, this is the fundamental point.

Azerbaijan is the strategic prize for the EU.

And I reiterate this to you today knowing that Hungary early on understood this, in some way. Hungary’s engagement with the Turkic world—let’s call it that—with the Turkic world in general and Azerbaijan and Turkey in particular, well, it started a while ago. Way before the conflict over Ukraine escalated.

So, with that, let me get into Azerbaijan’s role in providing energy security to the EU.

There is a pre-history here. The Contract of the Century was signed in September 1994—the first contract from the FSU that supplied oil to the West without going through Russian territory, using Soviet-era pipelines.

This was a \$7.4 billion contract, in 1994 numbers. And it enabled Azerbaijan to gradually become an important exporter of crude to European markets via the Baku-Novorossiysk, Baku-Supsa, and, particularly, the Baku-Tbilisi-Ceyhan pipelines. Today, the country supplies around 5 percent of the EU’s oil imports. Four out of the top five importers of Azeri crude are EU member states, with Italy being the largest buyer, followed by Croatia, Germany, and Portugal. These numbers are from late 2022, but nothing much has changed since then.

Now, with the discovery of the Shah Deniz natural gas field in 1999, Azerbaijan gradually transformed itself into an important gas supplier to the EU, too. The launch of the first phase of the Shah Deniz field in 2006 allowed the country to cover its domestic demand and export natural gas to Georgia and Türkiye. The second stage of the Shah Deniz field, which was launched in 2013, added a further 16 bcm of natural gas production capacity per year to the 11 bcm production capacity resulting from the first stage of the project.

These became the source base for natural gas supplies to the European Union via a chain of pipelines collectively known as the Southern Gas Corridor.

And the Southern Gas Corridor project was another “first”: it increased and diversified European energy supply by bringing gas resources from the Caspian Sea to markets in Europe.

SGC is an initiative of the EU Commission for a natural gas supply route from the wider Caspian region to Europe. It was proposed in 2008 to diversify the EU’s energy supplies with AZ gas.

The corridor’s route from Azerbaijan to EU markets consists of three pipeline projects: the South Caucasus Pipeline (SCP) and its expansion (SCPX), which moves natural gas from the Shah Deniz field to the Georgia-Türkiye border. Then the Trans-Anatolian Natural Gas Pipeline (TANAP), which runs across Turkey. And then the Trans Adriatic Pipeline (TAP), which starts at the Turkey-Greece border, transverses Greece, Albania, and the Adriatic Sea, and then comes ashore in southern Italy to connect to the Italian natural gas network.

Now, with the completion of TAP—the corridor’s final leg—Azerbaijan began direct commercial gas supplies to the EU on 31 December 2020. Crossing six countries and stretching across 3,500 kilometers, the \$40 billion SGC has become one of the most complex gas value chains ever developed.

Somewhat outdated statistics indicated that the corridor supplied a bit more than 10 bcm to EU markets annually via TAP, providing at least 8 bcm to Italy, and nearly 2 bcm each to Greece and Bulgaria. Just a few days ago, I saw reliable figures indicating a more than 10 percent increase in deliveries via TAP. In any event, there are long-term ship-or-pay contracts for 25 years in place.

Now, while the initially planned volume of 10 bcm into the EU via TAP might not look considerable, the strategic importance of SGC is hard to overestimate, due both to the new supply source and the route it provides.

Now, all three pipelines within the SGC project were designed to be expandable. TAP—the European leg of SGC—can double its capacity and expand in stages: up to 20 bcm within 45 to 65 months. And I'll say more about this in a few minutes. If it happens—and I'm confident it will—then this suggests that Azerbaijan's share in Europe's gas market will hit double digits.

Look, in various ways Azerbaijan supplied 4.9 percent of Europe's gas needs in 2021. In 2022, the number was 6.9 percent. So double digits—via TAP but also via Georgia and then across the Black Sea—by 2027 is almost certainly going to happen.

And because of the way the global gas market is structured—if you take Russia out of the equation as far as the EU is concerned—then without this Azeri gas, the EU does not have enough. Certainly not without driving spot market prices through the roof. And even then, Azeri gas will be needed. I can get into the nitty-gritty later on, if you'd like.

Ok?

Now, let me say a few words about the Memorandum of Understanding that was signed in July 2022 between Azerbaijan and the European Commission.

This is the document that deepened the strategic energy partnership. Its centerpiece was a shared commitment to double the capacity of Azerbaijani gas flowing into the EU and the Western Balkans by 2027.

This is a document that also reaffirms and deepens the *strategic energy partnership* between Baku and Brussels.

Thus, Azerbaijan is understood today by all relevant actors to be *and* to remain an integral part of the EU's energy equation—not just in the short term, but for many years to come. This is evidenced by the fact that the MoU I just mentioned commits the EU to support what the document calls “long-term, predictable, and stable contracts.”

BTW, this clause constitutes one of two policy reversals by the EU, because for the past several years the EU has had a policy in place that prevented its member states from signing new contracts of such length.

The *second* EU policy reversal found in this MoU has to do with financing the deal. It looks like the EBRD will help finance it, and I have heard some rumors that the European Investment Bank will also find a way to participate. And for the past several years such institutions have had a policy not to finance new hydrocarbon deals.

So, there you go. The negotiations on the terms of this truly strategic MoU were *real and substantive*—so, again, not like a car inspection. There was give and take. And it produced at least two EU policy reversals, as I just mentioned.

Both are sound EU policy decisions that reflect the new geopolitical reality. The EU did the right thing by advancing its interests.

And all this is good news not only for Azerbaijan, obviously, but for the EU as well. Because the record is clear: there is, effectually, no more reliable non-Western oil and gas supplier to the EU than Azerbaijan.

In other words, we're talking about a predicable, stable, secure, and friendly partnership. One that both Baku and Brussels are *and* should remain proud to champion well into the future.

Something else that's important to emphasize is that Azerbaijan is already increasing natural gas supplies to the EU—this goes above and beyond what the contracts require, which is around 10bcm. I've mentioned this already. So, officially, 11.4 bcm was delivered to EU member states in 2022. So, by 2027, we're talking at least 20 bcm, probably 21bcm, maybe even a bit more than that if the Georgian ports are used to full capacity.

Now, the success of the Southern Gas Corridor—and of TAP in particular—is a major reason why the EU only needs limited additional gas to expand its diversification capacity going forward.

And, again, doubling the capacity of Azerbaijani gas through the SGC in the next five years, in line with REPowerEU, is an integral variable of that strategic equation.

In other words, gas supplied by Azerbaijan represents the biggest energy security blanket for the European Union.

Now, I want to say clearly that I believe it is in the interest of the European Union and its member states for the Commission to continue to support the expansion of SGC in general, and the doubling of TAP's capacity, in particular.

So, support in a political sense; support in a technical sense; and support in a financial sense, however much is possible.

There is no discernable, serious, and responsible downside to doing so. Obviously, the focus will be on TAP, given the nature of the TEN-E Regulation.

Now, next point. We know that the Commission is now engaging with Azerbaijan, EU member states, and the pipeline operators to achieve clarity on the terms for the expansion—and this includes extending its strategic benefits to the Western Balkans, which is important.

And these talks are in the final stages, and they're moving in the right direction.

The additional volumes to be brought by doubling the capacity of the SGC would be especially crucial for the markets of East and Southeast Europe, which have long been called the Achilles Heel of Europe's gas infrastructure.

In the Eastern Balkans, the recent completion of the 3 bcm/year Interconnector Greece-Bulgaria (IGB) paves the way for the delivery of Azerbaijan's gas northward to Bulgaria—the capacity of this piece of infrastructure will increase to 5 cm/year. Also, an interconnector

between Bulgaria and Serbia should become operational by late 2023. In April, a deal will be signed for Hungary to be supplied with 1 bcm of Azerbaijani gas via the BRUA Interconnector, also known as the Vertical Corridor, which is one-third of your needs. Romania and Austria will probably get in on this, too. There is the proposed Ionian Adriatic Pipeline (IAP) could connect TAP in Albania with Montenegro, Bosnia and Herzegovina, and Croatia.

In any event, my point is that focusing on the Balkans is a financing and a political priority for the EBRD, and these talks are concluding as we speak.

Alright? So, lots of moving parts.

And Azerbaijan knows how to coordinate such deals—it has lots of experience in putting the various pieces of the puzzle together. It has done it before...Contract of the Century, original Southern Gas Corridor, etc.

The last thing I want to talk about in this context is the quadripartite agreement signed in December 2022 in Bucharest on the supply of green electricity from Azerbaijan and Georgia to Romania and Hungary, and probably some other countries in Southeast Europe.

This deal also derives from the July 2022 MoU.

Right? The first part of that document dealt with doubling the capacity of the Southern Gas Corridor.

And the second dealt with the export of green electricity from Azerbaijan to the EU.

So, in Bucharest, the deal made was this:

Generate electricity from solar and wind, both onshore and especially offshore, in Azerbaijan, and hydro power in Georgia. And then feed this into a cable that flows below the Black Sea and then enters into the grid in Romania and goes into Hungary.

And this green cable will be built to carry much, much more electricity than the initial contracts indicate.

One important reason is that Azerbaijan has a rich potential of about 27,000 MW of onshore renewable capacity.

Azerbaijan also has enormous offshore wind potential: the World Bank says it's 157,000 MW—that over 20 times Azerbaijan's current installed energy capacity, including all the hydrocarbon production. In fact, it appears that the Caspian Sea ranks second in the world for its offshore wind energy potential.

Ok? This is tremendous.

I can get into the details later...but I'm looking at the clock...so let me wrap up.

Let me just say that the market tests will not be completed before the end of 2023. And my guess is that the numbers will not be spectacular. Break even or thereabouts. But my forecast is that this will not be a major impediment to making it happen. And, again, I can get into the details later on.

Now, audience, take a look at the map. You know, picture it in your mind's eye, or find it on your phones.

Azerbaijan is the keystone country for EU ambitions in the Silk Road region—in terms of energy and transport and connectivity and all the rest of it. Try as you might, you just can't go around Azerbaijan, because to its north is Russia and to its south is Iran. And the EU is committed to its sanctions and export restrictions regime in both of these places. And this will not change for the foreseeable future.

And you know what this means to me?

It means that the EU needs to make itself more attractive to Azerbaijan—more so than the other way around.

If the EU fails to attract Azerbaijan, its strategic foothold in the Silk Road region will not be sustainable. And that would surely constitute a missed opportunity. One could even say it could amount to both geopolitical and geo-economic malpractice.

A good example of this is Azerbaijan's role in facilitating the transport of Kazakh oil across the Caspian into its existing pipeline infrastructure, which I can get into if you'd like.

Let me just say that 1.5 million tons of Kazakh oil will be exported through BTC per year, and 3.5 million more tons will end up at the Black Sea coast of Georgia. This, too, will go to the EU. All of it will bypass Russia. Again, this is impossible to do without Azerbaijan.

Now, last point.

And this again goes back to the July 2022 MoU between the EU and Azerbaijan.

The other important area of strategic cooperation in the field of energy is the green cable—the wind and solar and hydroelectricity project. The one I just finished talking about.

Let me just say that ultimately, all this strategic engagement is a political question.

Does the EU want to engage seriously, comprehensively, with Azerbaijan, in full awareness of the geopolitical and geo-economic consequences of the fact that Azerbaijan is the indispensable state for the fulfillment of EU strategic ambitions in this part of the world?

Does the EU have what it takes to align its interests fully with those of Azerbaijan on energy and connectivity issues?

If so, it will have an optimal partner in Azerbaijan. There's one thing you all need to know about Azerbaijani statecraft—particularly about how its president conducts himself with foreigners: he never bluffs, and he always keeps his word.

So, from the EU's strategic perspective, there's really no downside here. And for all the suboptimal state of relations between Hungary and other EU member states—not to mention the EU bureaucrats in Brussels—this area is one in which Hungary can play a serious role. A constructive role.

Because the prospects for win-win are truly extraordinary.