

---

# REPORT

---

**Dr. Ali Biniiaz**

Director – International Economy and Energy Studies Centre, IPIS, Iran

8-12-2009

## IRAN AND EUROPEAN GEOPOLITICS OF ENERGY

When seeking to address this topic it is firstly necessary to determine what the relationship is between energy security and foreign policy. In addition to this, it is important to identify how and when the issue of energy became a high priority on the foreign policy agenda. The classic theory is that it has been incorporated fairly recently and probably at some stage during the 1990s.

The second issue addresses how we understand energy security in the context of the bipolar world, different from that in the quadripolar world. After the fall of the Berlin Wall it seemed that we then had a unipolar world, but in terms of energy it was bipolar. And that has been changed to a quadripolar world. It is important therefore to take note of this changing dynamic.

The third issue examines the relationship between the free markets and geopolitics as far as energy is concerned during the 1990s and 2000s.

The fourth issue focuses on what the implications are of these developments as far as Iran's energy diplomacy is concerned vis-à-vis the Europeans.

When determining the relationship between energy security and foreign policy it is important to look firstly at the events occurring promptly after the fall of the Berlin Wall. One such event was a tide of democratization in the world and the second was the attractiveness of the free market norms because of the collapse of the Soviet Union and the collapse of the central planning way of thinking about the economy.

In terms of energy security, the consequence of these two phenomena was thinking of energy security in a bipolar world consisting of the US and the EU because it was unipolar in the sense that the US was the hegemon of the whole world and therefore everybody was looking to mimic their norms and standards. The two big players in the world at that time, as far as energy was concerned, were the EU and the US. They were making plans as to how to use the energy, how to securitize that matter and how to actually bring about security in the long term perspective.

Thinking this way, it would be accurate to conclude that even though energy security was a latent element in the foreign policy of the EU and the US and therefore not particularly visible.

It can also be seen that between the US and EU there is a division of labor in energy security. Evidence of this division can be found in the report produced by the International Crisis Group in 2007.<sup>1</sup> It states that “The EU is in practice increasingly beholden to the US’s hard security power in places such as the Middle East and Central Asia being deployed to safeguard the interests of the market-democracy West as a whole”.<sup>2</sup>

When analyzing this passage two critical phrases can be identified. The first is “hard security” which is provided by the US, and the second is “the interests of market democracy”, and these phrases serve as our key reference points. From this report we can determine that the US and the EU are divided in their specialty and their labor based on their comparative advantages. One is taking care of the security and other is taking care of the free market norms, and extension of the free market norms to the neighboring countries and where producer states are located.

If one were to examine closely the role of the US, it can be seen that they are in charge of “regions and empire”, which represents a geopolitical dimension, and they also have a responsibility as a guarantor of last resort for international security.

In comparison, the role of the EU is to be in charge of the “markets and institution” approach. It is sometimes referred to as a liberal superpower, sometimes a normative power, sometimes geopolitical imperialism, civilian power or even regulatory imperialism. These terms all represent the labors of the EU as far as energy security is concerned. This demonstrates that despite the use of words such as imperialism and geopolitics, it is equally as accurately described as normative which indicates that it is a soft power.

Having determined these categories it is now necessary to determine why this division of labor occurred. This can firstly be attributed to the fall of the Berlin Wall. It is also due in part to the revolution in information technology and other related industries such as bio-technologies and nano-technologies, meaning that there were a lot of new developments in the world. The fact that there was a new wave of globalization is also has a role in the purpose of division.

The principle that should be applied here is that of economic comparative advantage, looking at the ability of each side to take care of a sufficient part of the issue and finally their self-interest, which is the driving force behind this.

If one should approach an analysis of the energy security of the EU, firstly it is necessary to look at The Grand Strategy of the US in order to develop a picture of the background as they were also part of this issue. The US Grand Strategy focuses on the division of labor globally on the basis of the principle of comparative economic advantage. A valuable account of this issue was provided by Thomas Barnett in his book entitled “The Pentagon New Map”, which was published in 2005. This leads us to the question of what having a comparative economic advantage is. Well, this manifests itself in having a world currency reserve medium such as the Dollar, which allows for leverage. This also embodies having the best army in the world and the most efficient economic system in the world. This in turn leads to having the strongest and

---

<sup>1</sup> Ensure that this is correctly referenced

<sup>2</sup> Reference this quote to its source

biggest financial centre of the world. These are all extremely valuable factors to possess. With all of these advantages, however, it is necessary to finance security.

The next issue is that you must have a global transaction. On one hand you can have goods manufactured elsewhere in the world and on the other hand it is possible to produce and supply security to them. So these are the reasons why the US was acting as the supporter and promoter of security for the world.

When looking at a map of the world in relation to globalization, this can be divided into two parts. Firstly there is the centre which we call "the Core" then the rest we call "the non-integrated Gap" Within the Core the US had a large number of military responses but beyond the non-intergraded Gap the issues were minimal. So they were looking at shrinking the Gap and taking over the Core. This creates a new Core and an old Core. Within the old Core there is Western Europe and within the new Core there is Russia, China, India and a number of others. This was very integral to the energy security.

I will now go on to describe the world's four flows that are relevant to this issue. These are energy, people, capital and security. When looking at the flow of people, currently there are 6.78 billion people in the world and by 2050 this figure will have risen to 9 billion. Upon analyzing the distribution, we can see that 2 billion of these will be within the ages of 0-15 (A), 2 billion will be over 65 (B) and 5 billion will be between the ages 15-64 (C). This means that in order to determine the support issue the number of people in group C should be divided by A plus B, therefore determining those people who can work, and dividing the figure between those who cannot.

This provides a very meaningful interpretation. In developed countries the support ratio would currently be represented as 5 over 1, meaning that 5% of the population can support 1%. In 2050 there will be only 2% supporting 1% which illustrates a very sharp decrease. In less developed countries there is currently 10% of the population to support 1% and this figure will remain the same even in 2050. This clearly illustrates that it is necessary to have a flow of people moving from developing countries to the developed countries.

Secondly, we must address the flow of energy. All of the regions of the world that have supplies of energy are located in the non-integrated gap so the supplies have to be exported from the non-integrated gap to the Core. The implications of this is that China and India may have political rivalry with other countries that have energy, so this is a pretext for the US to move forward, put these countries aside and prompt them to use their defense budget.

This situation presents itself as a transaction, and the US can therefore export goods to the rising powers, such as China and India, in a way that means they don't need to have rivalry in areas where there is energy. When addressing the above transaction, China is a country which is a good producer of global goods which can be exported to the US. India, however, is in a good position for information technology, and so they can export these I.T goods and in exchange the US will support security. So this is an illustration of a logical transaction.

The third flow is of capital. Capital clearly moves between the old and the new Core, and not from the non-integrated Gap to the Core or vice versa. So the capital goes from the old to the new as they want it to keep flourishing and that's why countries which have energy do not have sufficient amounts to invest in the energy infrastructure as is needed. This subsequently means that the new Core remains capital dependant on the old Core.

However, Asia has identified many problems with this US strategic view, the first being the existence of strong states such as China who prevent the development of private markets. It is necessary to have weaker states throughout the world, and to export democracy and free market norms. The new thinking is different from classic thinking as in the classic model you have to counter-balance powerful states however in the new thinking, you think of bad bargaining and exporting free market norms to weaker states so the weaker states cannot do anything. Therefore the existence of the stronger states, from the US strategic view point, is something bad.

An additional problem with this concept is that there exists unfair legal treatment amongst all the market players. Concision is given to domestic producers which is unreasonable as it is necessary to have consistent levels of fairness applicable to whoever may undertake the activity.

The final issue is the existence of chronic crisis stricken spots such as Afghanistan and Iraq which must be dealt with. The US rationale for their strategy however, is that the US military presence will reduce the defense budget allocations and will also help the regions to grow more economically.

Looking at the US security strategy in detail it has many aims. Firstly, to strengthen the security at the Core and help markets to expand. Secondly, to shrink the current gap by controlling it, and pre-empting military action if necessary. Thirdly, by protecting the gap against potential threats of terrorism, and the spread of disease, and lastly, to export US security to the crisis-stricken spots of the world.

Having looked in detail at security provision by the US, it is now necessary to once again address the EU. When looking at the markets versus geopolitics debate in the context of energy security, there are a number of indicators available which demonstrate that the markets are working better. This belief is based partially on historical facts in relation to how the markets have flourished and extended over the years and are ultimately working better.

Then it is necessary to look at the markets interpretation. It can be seen that prices are going up but this is not a cause for concern as it can be attributed to the catch up process. This dynamic means that during the 1990s the prices were low, investments in oil and gas were low, and because of these factors the supplies were reducing. But by the time the demand increases there is a misbalance between supply and demand. It is necessary to have international co-ordination mechanisms which mean you must have good governance, multi-lateral institutions and cooperation but then there are conditions attached to this. Competition must be encouraged by the markets whilst also considering future investments.

Historically we have had growing international markets vis-à-vis oligopolistic markets since the oil crisis in the 1970s. There was the expansion of commodity and financial markets, including oil which is now more susceptible to market dynamics. A connected set of commodity markets developed where competition is the rule and the economy is very effective. The imbalance of power between the states works very unfavorably for the smaller exporting states so that they are left behind and end up shrinking further so that they are no longer able to support themselves in their own right. So these are the developments which happened in favor of functionality.

There is a lot to be gained from the power of market interpretation and as I have previously stated, after 2003 the oil prices rose as part of the catching up phenomenon and there was an oil peak mistake as people estimated that it would peak around the year 2000, however we still haven't yet reached the peak. Due to these miscalculations, there was ignorance to the fact that when prices rise there is also an increase in the cost of further explorations and advances. At the end of the peak there comes a sustainable plateau of oil production. Future prices will be less stable but the key point here is that you have to temper the natural ebb and flow of the market adjustments. These are a few of the things that we can discover from the functionality of markets so why should we be concerned with geopolitics. The implications of these above factors are that we should not be concerned with the dependence on imports and instead concentrate our efforts on market extending policies. This is therefore the way that practices were developing in the 1990s and into 2000.

Under the feasibility argument we discussed how the US is the guarantor of the last resort. The international coordination is centered on market-based solutions from these treaties in which the comparative advantage of the EU is located, international good governance standards, multilateral institutions and cooperation.

Previously the issues surrounding bipolar and unipolar structures were discussed. One is acting unilaterally so the US is acting unilaterally. When assessing the mechanism of the business of the US with war, the US was focusing on FTAs,<sup>3</sup> while Europe didn't. This means that you think unilaterally, and you join people and join countries who are thinking favorably about you. So you build up as many FTA's as you can.

The EU is a multilateral institution. Thinking about the model of a central institution building, you try to join people and think multilaterally. This demonstrates the division of labor between the unilateral way of thinking and multilateral thinking and both of them will constitute a world of bipolar. This was the way of thinking during the late 1990s. But then the stories changing and that's the new thing that is happening and that's why we have to take care of energy security.

Then you have the political challenge if one is going to be a promoter of the free market, so there is a requirement to encourage competition without discouraging investment in infrastructures and productive capacities. Here the role of the oil and gas multinational companies is important because they are the corrector of the capacity, they have to have the job done very well otherwise they would be in trouble with this way of thinking.

The market then lost the game to the geopolitics of energy because the US withdrew from the European energy game. This was due to the occupation of the US in wars such as Afghanistan and Iraq, so they could not focus their attentions elsewhere.

This quadripolar world of energy consist of the US, the EU, Asia and the Middle East. The core of the mistake is exactly here because they did not think of the Middle East and big players of the game like Iran were in the early designation of the game. This was the source of the problems that have occurred recently. We didn't take care of Asia either. The energy that you have is located in the non-integrated countries. If you are going to help them it is in such a way that they gain access to the energy and grow further but then you do not have sufficient resources of oil and gas left in the world for you. And if you prevent them from accessing and

---

<sup>3</sup> Free Trade Agreements

gaining energy then this will present a number of conflicts in the future. So the energy poverty is something that puts a state in a challenging position. This is because all of the issues are not adopted together but instead addressed separately. However by taking this approach, gradually the other issues appear and cause problems.

The multi-national companies were being handicapped because there were no longer any resources available to them except in the case of Iran because they tried to have access into the Iranian markets but the mechanism of contracts was such that no access to the reserves were given to them. That's why they say that Iran is a Greenfield.

In future there will be a growing concentration of oil and gas producing states as for example you have Russia, Afghanistan and Iran, therefore half of the oil reserves of the world are allocated to these countries. This means that there are no free market norms dominating the oil and gas market in the future because with a small number of the players it is like an oligopolistic game not a free market game. These are the challenges. Then there is the politicization of energy and the mismatch between producers and the consumer's expectations.

If you want to explain about the energy politicization, it is a very critical element that must be considered and in order to do so we must address the question of how the EU is an international energy actor. The EU was wrong in its conceptualization of this issue as firstly experts say that oil and democracy do not appear to mix. More importantly, it is said that the first law of petro-politics is that the price of oil and the pace of freedom always move in the opposite direction in oil rich petro states.

I shall address something at this point which is quite to the contrary. Ok, say those in OPEC, countries are contending high prices, but why? It is because of the political liberalization. Because of that they ask for higher prices and from the other side they say that the first law of petro-politics is that the price of oil and the pace of freedom move in the opposite direction. One of the implications of this first law of petro-politics is that the price of oil is brought down, in such a way that you can free these countries from dictatorship. This way of thinking does not provide energy security in the long run. And you can do your business; you can topple down a number of regimes, big ones. But they're not the same, at the end of the day you're not having the stability in the long run or the security. Long run security has a triangle. That's food, water and energy. In a long run perspective we meant that time when we did not have any distortion. All the distortions occur in the short run; therefore this way of thinking is not going to help.

Another proposition is that with energy prices rising and supplies dwindling, the tide of democratization seems to have met a match in the black tide of petrol authoritarianism. So we are setting a very bad example to the people, to the allies, people who are thinkers, the youngsters of these countries, and saying please try to topple down the regimes because that would be authoritarianism, that would not be democracy. This is the way you look at it and the way the arguments go on.

The autocratic regimes in producer states increasingly subsidize domestic fuel prices to shore up their own legitimacy. This is another conventional way of thinking. But if you think carefully, in countries like Iran as far as I know, there is no relationship between the legitimacy of the government and rising of the fuel prices. You know Iran is a large country as a civilization. When we say civilization, we think of history. It's not history, it's a current status.

If you have a big civilization you have the elements of emotion, the elements of value and the elements of wisdom, all incorporated in the same place and your people think in that way. So they think civilly. They have objections. They come to the street and say this is not true, this is true, these are the functions of civilization. Not many countries learnt how to run their bureaucracy, how to insulate their bureaucracy from outside pressures and how to embed sufficiently good norms into their bureaucracy. And that is a source of concern. You have a strong civilization but you do not have a bureaucracy which is suitable for your agenda.

But then it would appear that there is a legitimacy problem. There is around here a state with all those conventional things. I do not challenge them at explaining something. So they explain A cause B, this causes C but then at the same time there are other considerations. So you have to have a full picture of the whole story so you are not conducted to the wrong way.

And the second thing is that there was insincerity with the EU in supporting democracy. For instance a cloak for pursuing oil interests. The Milosevic overthrow in the 1990s, people say that it was because of the pipeline reaching from Russia to the west of Europe, so that was the reason. It's their way of thinking. You can challenge it but at the same time you have a pattern which is compatible with other things. You do not have something that is odd with other evidences. So for instance, it is possible to look at peace deal in Sudan. Some people say that's because of oil being bought from the south. People say that the removal of the Taliban. People say pro-democracy policies in the Middle East, that's because of oil and that's because of gas. So this, in a long way of thinking is kind of insecure.

The third factor is EU's soft politics against producer states, for instance we have new oil wars vs. the old oil wars. It was a competition and it was a fight against superpowers of the time over energy resources of one country or region. So what are the new oil wars? It involves countries that are in a dominant position like the EU going to producer states and negotiating talking or fighting with them over the resources that they have. This way of thinking is not however going to produce security. And a state building agenda, they are just promoting state building. Then you have the counterbalancing which was the old way of thinking and band-wagoning arguments, which is the new way.

Now I come down the road to the energy game that was supposed to explain about it. And focus on the theoretical challenges and theoretical perspectives. Then you think of the European energy game in the sense of the issue of the 1990s. What are the characteristics? US provider of security and pipeline designers. We have BTC, later on we had BTE and then the TCP.<sup>4</sup> They were designed in such a way that provides the issues and stories of the 1990s. So they were supposed to be produced to transport the oil and gas created in central Asia after the fall of the Soviet Union.

Then the EU was a free market actor and norm promoter in a globalised world. So I say, ok, I am going to extend my internal market to your market, so in such a way that we take likewise and you produce oil and gas and I give you the money or other things or the support that you need. Russia at that time was a fair player, a fair producer and a fair transit country, and we had a number of networks coming from Russia and the former Soviet Union to the West, so it was in a good position. Ok, we honor your right, you are there, and you should be there, there is no problem with that. Turkey is a natural energy hub because it is located in the part of the world which has access to central Asia and to Russia so we have to honor that right.

---

<sup>4</sup> Trans Caspian Piping

Central Asia is a producer, so that's ok. The only player that should be out of the game is Iran. While Iran is a good producer and a good transit country, it is located in a crossover where countries have access to the oil and gas. Then we do not consider you, we ignore your natural right and put you aside. And that was the game in the 1990s.

Then, what happened in 2000? There was a reversal. In 2000 the US withdrew due to its engagement in the Iraq and Afghanistan wars. And we had China and India's rise. We had the geo-politic way in the energy common free market. And we have energy politicization as I have already mentioned. A very important factor is Russia's assertiveness. Look, if you see I'm Russia, I see that there is some delicious stuff here - its Iran. It is put aside. And then there is a country that is Turkey here in a shaky position. So I use my power to bring security for me and to take advantage of it. So there you have the Russian assertiveness. And then by the time the other players in the EU are thinking, like Germany and others, they realize that the previous game is not working. Without in a latent way and without mentioning in a demonstrative way they try to change their position. So we have the Nord Stream pipeline coming directly from Russia through the sea and into Germany. So that is not on the basis of the EU as such.

You therefore have a reversal of the game that started with the Russian assertiveness and was followed on by other countries like Germany. Then Turkey started to change the game. Look at the equilibrium. You have the equilibrium of the game. If that equilibrium is going to be sustained then you have to have to have honored the natural right of each player. Once you do not honor the natural right of each player then an incentive is provided for deviation from the equilibrium. That deviation started by Russia was followed by Germany and other places and very recently by Turkey. So Turkey tried to diversify in foreign parts. Turkey recently could be considered united with the EU as it has been nominated for EU membership. It could be incidentally united with the US. It could be considered united with Israel and it could be united with Iran. So it demonstrates a diversification of foreign policy thinking and puts you in a much more difficult position compared to before.

Then, what will be the implication of these things? Early in the 1990s you had a coordination game. You had two equilibrium, one is coordinated and one which is not. This game has been changed to have a low equilibrium and high equilibrium. Once they will not coordinate then you are forced to take place in low equilibrium. And in low equilibrium you are in a sub-optimum position, not in an optimum position. So this is the game which is in Europe.

Then, what will be the role of Iran? Iran constantly, under the coordination game of the 1990s, or the incipient prisoners dilemma game Iran is a residual player then you have to decide after the other players have decided. They maximize their benefit and you can take advantage of whatever is left. This is the meaning of a residual player. So in this context what should Iran do?

If I was Iran, I would prioritize the gas resources oil enhanced recovery. You know that the functioning of the oil wells, sometimes the pressure comes down and then you have to enhance that pressure by an injection of gas. And the structure of "oil mountains" of Iran would be such that it is more beneficial if you inject gas. If you inject gas, then the gas would be reserved there. You can take advantage of that in the future when the prices go up with the rising trends. So there should be no hesitation about being ignored from the roots, because gas can be injected which will enhance the recovery of oil, the oil can be sold at high prices and gas can be reserved for future use.



The second priority is to build up a regional processing center as you are located in a crossroad so the best thing to do is focus on the processing because we have good technical ability and good engineering. So those engineers and that legacy of the past probably gives you a good position in terms of building up a processing center.

Then the third one is to focus on LNG production. Even Cyprus can take advantage of that. You know you are a small country, you are allocated by the sea, so you are in a good position to build LNG terminals, and you are in a good position because you are part of the EU, so you probably have to have good lobbying power. So you can close up the conflict between Iran and the EU and the US and take advantage of that and make business with them. So it needs to allow for LNG facilities.

And then the fourth priority would be to follow the crossroad rule. It means that you have to eliminate the rivalry in your country. Releasable gas must be allocated and not the gas that you have. It is necessary to take care of individual priorities and if there is anything left then it must be allocated equally to the west and the east to reduce assertiveness against you. Europe is a player which needs gas or LNG in future so I am going to release to you half of my releasable reserves of gas. Then they will either be a direct partner of mine or they may stay away in a non-reconcilable position. They will not be taking care of it and if that is the case then I will divide that allocation into half and give half of it to Russia in order to take care of you and the other half for Turkey to take care of. There is then an incentive for them to use it rather than export it. Then I release half of my gas to you because you are a consumer and I am not going to ignore you. Then I will allocate half of it to the Eastern country, and to the East of my country there are two big players, China and India. So I will separate India from Pakistan and put China and Pakistan in the same axes and provide them with one source of releasable natural gas. Then the other half would be for the India and Asian axes and that would be in LNG form because they do not have common territorial borders with me.

\* \* \*