Natural Gas in the Mediterranean: A Note for the Barcelona Process 10th Anniversary

By Hadi Hallouche*

Introductory Remarks

A wise man once said “politicians build walls between nations, industrials build bridges”.

In the case of the Mediterranean, a region with millennia-long history and a rich cultural and social mix of peoples, this statement is only half true.

On the infrastructural level, the Mediterranean region has witnessed over the last decade -and still is- tremendous integrative changes, notably through natural gas projects.

The complementarity between the EU and the South and East Mediterranean (SEM) countries, on the energy front, particularly natural gas, is overwhelming: the EU needs secure, reliable partners at proximity and SEM countries are interested, on the strategic level, to have a special and sustainable relationship with the EU.

On the outset, over and beyond the social, cultural, historical and other commercial elements that may link peoples and corporations in the Mediterranean, natural gas is most probably one of few industries that has actually presented strategically enough incentives to create inter-dependent links between countries.

On the political front, the Barcelona Process Initiative in 1995, bringing together the EU Member States with SEM countries, came as an expression of a strong political will for a tighter relationship between Europe and the Mediterranean.

While one might argue that the industry (more particularly here the natural gas industry) *has* built bridges in the Mediterranean, it is not fair nonetheless to subscribe to the idea that politicians have built walls.

This being said, there is general agreement that the spirit of the Process has faded away. There is a pressing need to revive it in light of new political, strategic and economic variables: the EU enlargement, the Euro, Turkey’s prospects for membership, recent developments with Libya, recent developments in the Middle-East, the 11th of September events and important changes in the energy markets, for instance.

The Process will celebrate its 10th anniversary this November and a summit of similar importance is expected, or hoped, to bring the revitalisation of the Euro-Mediterranean partnership.

Europe Needs Gas

There is little doubt that Europe is moving towards a higher dependence on imports for its energy needs. The booming growth of energy consumption in some EU Member States coupled with slow, if any, growth in primary energy production overall means that imports will grow importantly.

It is clear also that with the Kyoto Protocol coming into force, and the concerns of the commission voiced through the Green Paper for Energy on environment friendliness, further pushes for a higher consumption of natural gas in the EU energy mix puts a particular upward pressure on imports of natural gas.

EU Member States are increasingly poorly endowed with natural gas. Security of supply – also voiced through Green Paper- is, therefore, a matter of importance. The EU Commission Directive on Security of Supply for Natural Gas, for instance, notes different logistical (e.g., storage) and economic instruments (e.g., diversification of partners) to move closer towards achieving security of supply. But more can be done.

The longer term strategic tools to move closer to security of supply may come under the form of closer cooperation and the establishment of a state of inter-dependence between the EU and SEM countries as well as consistent dialogue.

Dialogue is probably the long term solution. The Euromed Forum for Energy, which came about in the spirit of the Barcelona Process, provides the platform for such dialogue. The Forum was, however, not able to efficiently solve some of the issues related to natural gas trade that have arisen between the EU and some of its southern neighbours.

SEM Countries and Current Projects

Algeria, the world’s oldest LNG exporter, has a strong market share in the EU. Algeria is linked to Europe by two underwater pipelines, one via Morocco serving Spain through to Portugal and the other one via Tunisia serving Italy and Slovenia. These two pipelines, while providing an extremely important basis for security of supply to the buyers (and security of market for Algeria), also effectively brought both transit countries into the gas trade value chain.

Construction of the the Medgaz project, a pipeline linking directly Algeria to Spain (and potentially France), is due to start this year. The GALSI project, a direct under-water pipeline to Sardinia, Italy (and again potentially to France), has seen the commitment of the Algerian and Italian governments as well as a number of companies.

It is worth mentioning that Spain’s legislation states that imports from any one producer cannot exceed 60% of total imports, a security of supply motivated measure. Algeria, having the strongest absolute advantage in selling gas to Spain due to the proximity, finds its exports artificially impeded. If gas cannot be exported, electricity can; bearing in mind that electricity drives most of the gas consumption growth. Indeed, along the construction of the Medgaz project, an electricity connector cable is expected to be laid.

Further, discussions are underway between the Algerian and Nigerian governments for the construction of a Sahara-crossing pipeline, called NIGAL, linking the Nigerian fields to the Algerian-EU pipeline export infrastructure. This project has been greeted with some scepticism by some market observers but has witnessed strong political will from the Algerian and Nigerian governments, even at the level of heads of states, through the New Partnership for African Develop-

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ment Initiative. This project will offer Nigeria flexibility for its exports (besides LNG) and will place Algeria, in some terms, as a natural gas hub in the sub-region.

Another important pipeline project is the Greenstreem, inaugurated last year, linking Libya to Italy offering Italy a more diversified portfolio for its pipeline exports. Libya's LNG exports, which stagnated for a long time, are also expected to grow sharply in the light of recent developments of Libya's relations with the EU.

Egypt's pipeline, under construction, transporting gas to Jordan, Syria, Turkey and subsequently to the EU is probably the project that unites the largest number of countries. It also offers the opportunity to other potential exporters to join in, for example Iraq and Saudi Arabia.

Turkey also has the potential of becoming, if it is not already, a natural gas hub, due to its geographical situation as transit country for Iranian, Azerbaijani and Russian piped gas. Lower than expected demand due to the recent monetary turmoil meant that Turkey is over-contracted for some time. There is, therefore, potential for Turkey to become a seller of LNG (through redirections) as well as a transit country.

Southern Integration

As a group, North African countries have not done enough to create an environment of integration at least remotely similar to that in the EU. The UMA (*Union du Maghreb Arabe*) has been at a standstill for more than a decade and so are many projects that were expected to be conducted under its umbrella.

The UMA is composed of Mauritania, Morocco, Algeria, Tunisia and Libya. Egypt has also expressed interest in joining.

On the energy front, the Maghreb electricity ring is one of the projects supported by the Euromed Forum for Energy and is one that should benefit from high political sponsorship. There should also be more "soft" cooperation (uniformisation of standards, common data banks, common energy charters…etc).

The Maghreb integration makes sense in the dynamic of the Euromed Partnership and more generally in the dynamic of globalisation. More importantly, the synergies that exist between North African Countries, particularly in energy and natural gas, mean that this integration is in the national interests of all. Its failure over the last decade can only be credited to political immobilism. The recent initiatives to revitalise the UMA, especially the energy working groups, can only be encouraged.

Natural Gas Pipelines: Trust and Integration

Natural gas in the Mediterranean, has been, is, and is likely to remain an industry of trust.

Indeed, natural gas projects (Liquefaction terminals, regasification terminals, pipelines and others) are highly capital intensive and front loaded. Long Term Contracts, about 25 years, come to bind companies and indeed countries.

While it might be a matter of debate to grant natural gas the status of strategic commodity, natural gas projects, at the buyers and sellers side, are most surely of a high strategic importance, from the supply and from the finance viewpoints.

As a result, the tremendous natural gas infrastructural changes, besides fulfilling their logistical aim, have served to establish strong links between large (until lately) monopolistic corporations – in effect extensions of the State – in EU Member States and SEM countries. Beyond this, they have indeed established and sustained a higher level of trust, at the highest political levels, between governments.

Beyond the well-known commercial and strategic impact that pipelines provide, their construction provides unparalleled economies of scale required to lay other important projects such as electricity interconnections and fibre optic cables for telecommunication. This is particularly true for under-water projects. Given the fact that these industries (gas, electricity and telecommunications) are slowly liberalising on both sides of the Mediterranean, commercial integration - and more - will undoubtedly follow.

Dialogue

The Euromed Energy Forum should have played a much more central role especially with regards to the recent debates on the Gas Directive and the Natural Gas Destination Clause: some SEM Countries complained that they were not consulted by the EU Commission on the former, which was about to bring important changes to the market, and the EU Commission deemed the latter as anti-competitive in spite of the fact that it was common market practice for a long time. Both these issues have been – mostly – resolved, but in a way that was not as smooth as it should have been in an industry where trust is so important.

These misunderstandings, together with high U.S. gas prices, will certainly make more North-African gas go to the U.S. Security of supply also means that the EU should make itself an attractive buyer.

The Euromed Forum for Energy is young, loosely structured and meets infrequently. Given the importance of natural gas in particular, and energy in general, in playing a pivotal role in Euro-Mediterranean integration, this forum cannot afford to stay at its present state. It needs to gain more importance and more structure.

Political Will and Integration

The Barcelona process provided, ten years ago, a good starting point for a blueprint of the relationship between the EU and its southern neighbours. The Process is undoubtedly of a high strategic importance, in more aspects than one, for both sides. The Process aimed, amongst other things, to establish a free trade area in the Mediterranean by 2010, to provide structural funds to the SEM countries in a comparable fashion as those channelled to the Eastern European countries, and to promote projects of importance (a number of which infrastructural, and energy).

The Process achieved a lot, not least of which were the association agreements ratified by many SEM countries and a substantial increase in investment. The Process, however, did not do enough, by the standards of many commentators. The Process came further to be overshadowed by the "EU

Neighbourhood Policy" which, as it puts countries of fundamentally different relationship patterns in the same basket, was to be criticised by many experts.

The situation in the Middle-East is, also, a highly destabilising element. While the Barcelona Process was launched in a time of momentum – only two years after the Oslo Agreement was signed, it finds itself today in a much different situation. Obviously, notwithstanding the effect that the conflict has on the integration of the East Mediterranean Region, it also puts high barriers, long term, on a potential institutional consolidation at the Euromed level.

Concluding Remarks

The complementarity and the proximity between the EU and its Mediterranean neighbours, especially in the natural gas trade, offers opportunities for a strong alliance between them.

Natural Gas trade, being an industry based upon trust between partners, infrastructural natural gas projects, especially pipelines, have succeeded in achieving more of it between partners: sellers, buyers and transit countries.

Besides the economic repercussions directly and indirectly, natural gas projects, again especially pipelines, offer economies of scale for electricity and telecommunications (fibre optic) connections which further enhances the general level of integration in the region.

Along with trust comes dialogue. The Euromed Forum for Energy probably did not do enough to tackle the major energy related issues. This forum should gain in importance and in structure. Above all, the forum should be used more often by the SEM countries and by the Commission for consultation on mutually important energy issues.

Above all, such dialogue should be looked at in an optic of security of supply by the EU Commission. With the U.S., Indian and Chinese LNG markets growing and the LNG market becoming more liquid and slightly shifting from demand-led to supply-led; the EU has to make itself more attractive as a buyer.

From its side, SEM countries – more particularly North African – should deploy the political efforts required to integrate and consolidate their energy infrastructure (and other aspects) further. The example of the Maghreb electricity ring as well as natural gas interconnections should be at the forefront of discussions.

The 10th anniversary of the Barcelona Process this November is expected to be an attempt to revitalise the partnership taking into consideration the new security, social and economic imperatives. It should also give energy, and natural gas, the importance that it deserves in the integration of the Mediterranean by strengthening the dialogue tools and further facilitating investment.

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