



NATO DEFENSE COLLEGE FOUNDATION

RUSSIAN FEDERATION

STRATEGIC TRENDS

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Executive Summary

The first official visit abroad by the new President of China, Xi Jinping, was in Russia: an important symbolic gesture followed by the signing of some agreements among state-controlled energy companies, Chinese CNPC with Russian Rosneft and Gazprom. Despite the optimism shown by Putin and Xi during their meeting, salient issues between the two countries remain still unresolved, i.e. the longstanding gas pricing disputes and the Chinese demographic pressure on Russian Far East. Therefore China-Russia relationship will probably continue to be uncertain and difficult to forecast.

At the end of March the Russian and Chinese presidents met again in Durban, South Africa, for the BRICS summit (Brazil, Russia, India, China and South Africa). Ahead of the BRICS summit, speaking with the Russian press, Putin demanded to turn BRICS group into a greater geopolitical force.

Some analysts accuse Moscow to try to exploit the Cypriot financial crisis in order to take control of an important base in the Mediterranean Sea, where Russian Navy declared it will station permanently a fleet in the near future. Nicosia's financial minister flew to Moscow in order to ask

for a loan, and in exchange offered Russians some Cypriot banks at a convenient price and to participate in the development of relevant off shore gas fields recently discovered in Cypriot waters. Nevertheless so far Moscow showed little interest in getting involved in the problems of Cyprus, despite the generous proposals and the fact that billions of Russian money are deposited there.

Regarding domestic developments, Russian law-enforcement authorities searched thousands of NGOs, especially those receiving funds and sponsorship from abroad, notably USAID and other Western institutions. New York-based Human Rights Watch in a statement called these inspections “unprecedented” and reinforcing “the menacing atmosphere for civil society” in Russia.

Situation Report

The new Chinese President Xi Jinping chose Russia for his first official trip abroad. The 22nd of March he met with Vladimir Putin in Moscow. Before the meeting Xi declared that choosing Russia for his first foreign tour is “testimony to the great importance China places on its relations with Russia”. Welcoming Chinese President at the Kremlin, Putin stressed that Xi visit gives “new impetus” to Moscow-Beijing relationship and that “Russian-Chinese relations are a crucial factor of international politics. Our trade is growing, both countries are involved in large humanitarian projects, and all of that serves the interests of the Chinese and Russian people”.

On the sidelines of the summit, agreements were signed among the state-controlled energy companies. Chinese CNPC (China National Petroleum Corporation) finalized a deal for oil deliveries to China with the Russian Rosneft, now the world leading oil-producing firm. In fact Rosneft declared it had acquired TNK-BP, Russia’s third-largest oil and gas producer, previously owned by BP (British Petroleum) and by a consortium of Russian shareholders (21/3/2012).

Besides, CNPC signed a memorandum of understanding with the Russian natural gas monopoly Gazprom on the construction of a new methane pipeline to China. This could be a significant development because the pipe building had been postponed for many years, due to price disagreements. Aleksei Miller, Gazprom’s CEO, declared that by the end of 2013 the Russian major will sign a contract with CNPC for deliveries of 38 billion cubic meters of gas per year starting in 2018, with the option of almost doubling the volume. Nevertheless, the most important issue - gas price agreement - remains unclear and probably unsolved.

At the end of March (26-27th) Xi and Putin met again in Durban, South Africa, for the BRICS summit. Ahead of the BRICS summit, speaking with the Itar-Tass News Agency, the Russian president called for transforming BRICS group into a greater geopolitical force. Putin anticipated Russia's plan to create a BRICS Business Council in order to advance trade and investment within the five member states.

In order to avoid its bank sector collapse, Cyprus asked for Russian financial support, but Moscow refused, regardless the generous quid pro quo Nicosia offered (22/3). In the following section possible explanations are provided for the Russian position.

According to New York-based Human Rights Watch, in March thousands of NGOs' offices based in Russia have been searched by law-enforcement authorities, including those of Memorial, one of Russia oldest and most respected human rights organizations. Several of these NGOs receive funds from abroad, notably USAID and other Western institutions. Human Rights Watch released a declaration stating that "the scale of the inspections is unprecedented" and that these actions "reinforce the menacing atmosphere for civil society" (22/3).

Regional Trends

Russia's choice for its first official visit abroad, is an important symbolic gesture by the new Chinese President Xi Jinping. The same can be said the memorandum signed by CNPC and Gazprom to build up a new gas pipeline to China. However, the lack of a clear agreement on gas price will remain as the main obstacle for a solid China-Russia strategic energy partnership, and a source of persisting troubles in the future.

As a matter of fact, Beijing does not want to depend solely on Russia for its energy needs, to be just a gas client like most European States. Instead China prefers to invest and take direct control of energy fields abroad, for example in Central Asia and Africa. Despite symbolic gestures, the Russia-China relationship remains a difficult one, with many problems still unsolved, i.e. the strong Chinese demographic pressure on the almost empty Asian territories of the Russian Federation.

In connection with Cyprus financial crisis, some analysts and commentators accused Moscow of exploiting the crisis with the final aim to take control of the island and therefore gain a strong position in the Mediterranean.¹ Indeed, this would reflect Russia's eternal desire for access to warm Southern waters. Besides, to make the risk more concrete, by mid-March the Russian Navy declared that it will send a permanent fleet into the Mediterranean Sea.

Arguably Cyprus would be a perfect base for this fleet, especially now that Syria, the old Russian ally in the area, is in turmoil. Moreover, gaining a permanent base in Cyprus would represent the first major victory for Moscow after more than two decades of setbacks and NATO/EU perceived encroachment in the former Soviet Union space.

As a matter of fact, the reality is more complex. In the Cyprus' affair Moscow showed, so far, a pattern of behaviour not according to the "Cyprus' crisis-exploitation" conspiracy theory mentioned above.

To avoid bankruptcy, Cyprus asked for Russian financial support (22nd of March). In exchange Nicosia offered Moscow shares in Cyprus banks at a nominal price and to participate in the exploitation of recently discovered important off-shore natural gas deposits in Cyprus' Southern waters (Aphrodite gas field). Regardless of the generous Cyprus proposal, the Russian government said *niet*, thus forcing Cypriot authorities to reconsider an EU plan to impose a levy on depositors holding more than €100.000 in Cypriot banks, in order to get a bailout from EU. Interesting enough, just the day before, during a joint conference in Moscow with EU Commission's President Barroso, Russian Prime Minister Medvedev called the EU's original Cypriot bailout idea "to put it mildly, surprising ... absurd ... preposterous" (21st of March).

In fact, a levy like that would especially impact on wealthy Russians who put billions of euros in the Mediterranean island's banks, in order to profit from its favourable tax and investment terms. It is said that one third of the 68 billions of euros in Cyprus deposits is owned by Russian citizens.

So why Russia refused Cyprus apparently generous offer of banks and gas fields at cheap price? As regards the banks, first of all, Putin knows that this is a poisoned apple: to be involved in the disrupted Cypriot bank system is a very dangerous risk, even for a wealthy gas-state like Russia. Secondly, the Russian government would be happy to get back at least part of the enormous amount

¹ See for instance Edward Lucas, "If Cyprus falls into Putin's grip, the West will have lost the first battle in the new Cold War", *Mail on line*, published: 23:59 GMT, 21 March 2013.

of Russian money deposited by its fellow citizens in the Cypriot banks during the last years in order to escape taxation in Russia and the Kremlin would like to make sure that this will not happen again in the future. What better argument than the present bankruptcy to convince Russian citizens to leave their money at home?

As for the gas, the Aphrodite off shore fields is very promising indeed: it may contain up to seven TCF (Trillion Cubic Feet) of natural gas; and Russia needs more and more gas to satisfy its traditional European and new Asian (China) clients. Nevertheless Aphrodite may give more problems than satisfactions. The gas field is disputed by the breakaway Turkish Republic of Northern Cyprus that claims co-ownership of Cyprus natural resources. Moscow knows that getting involved with Aphrodite could create serious diplomatic tensions with Ankara that recognizes and protects the Turkish-Cypriot Republic. Moreover Ankara wants Russian and Central Asia gas to flow towards Europe through Turkey, and therefore Ankara considers as a very dangerous threat a possible Cyprus/Greece export route for the South-Eastern Mediterranean gas to feed European markets. Ankara is an important partner for Moscow, especially now that the submarine South Stream pipeline is under construction in the Black Sea, near the Turkish coasts. It appears evident that Moscow has scarce interest in provoking unnecessary tensions with Ankara.

In conclusion, Putin knows that the Cyprus card, despite its apparent value, is uncertain and risky. Moscow wants free access to the Mediterranean Sea, but not at the risk of colliding with hidden troubles in the Southern waters.