

# Więcej niż sąsiedztwo More than Neighbours

Warsaw, January 2007

## Belarusian-Russian Energy Conflict: The Game Is Not Over

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In 2007 new rules will apply to the deliveries of Russian energy supplies to Belarus. Moscow's decision to raise the price of gas and to impose a duty on oil export caused the gravest crisis in Russian-Belarusian relations after 1991. Thus, Russia commenced to withdraw from subsidizing the Belarusian economy. The process is aimed at gaining control over the strategically important energy sector of Belarus and thereby ensuring the possibility to exert stronger influence over the political situation in this country. Supplies of cheap Russian oil and gas have been so far the most important factor determining economic stability of the Lukashenka regime and a proof of Russia's political support. Although Minsk managed to negotiate the alleviation of Russian restrictions, they will anyway result in serious reduction of Belarusian budget income. It seems, however, that Belarus is not endangered by an economic crisis in the coming year, which would be inevitable should the initial announcements of the Russian side be implemented. The crisis will, however, happen if Belarus does not start introducing market mechanisms, especially as the prices for Russian oil and gas are going to rise in the coming years.

The outcome of the Russian-Belarusian dispute has not been determined yet. Gazprom formally succeeded to commence to take over control over Beltransgaz, which the Russian monopolist has been trying to do for many years, but, as the experience of the past years shows, it is by no means obvious how the process will end. Probably the refusal of Belarus to hand over the strategically key enterprise may lead to a new phase in the Russia-Belarus energy conflict. The stake in this game are the future of Lukashenka regime and the economic sovereignty of Belarus.

### Belarusian dependence on Russian energy supplies

Belarus is one of the world's largest natural gas consumers *per capita*. Gas consumption in 2006 amounted to 21 billion cubic meters and was 20% higher *per capita* than in Ukraine (78 billion cubic meters), whose economy is considered to be extremely energy consuming. In the last year Belarus imported natural gas from Russia paying about 47 dollars for one thousand cubic meters (tcm) (see Table 1).

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**Table 1. Natural gas consumption in Belarus 2001–2006**

Year	Amount of gas (billions of cubic meters)	Price (USD for 1,000 cubic meters)
2001	17,26	31,1
2002	17,57	30,6
2003	18,11	36,9
2004	19,64	47,7
2005	20,12	47,2
2006*	21	47,2

Source: Ministry of Statistics and Analysis of the Republic of Belarus; Beltransgaz. Quoted in: *Republic of Belarus: Statistical Appendix*, IMF Country Report No. 06/316, August 2006, p. 38–39.

\* Estimates.

The price was not much higher than the price for Russian consumers and it was several times lower than the prices for other countries of the region. Cheap Russian natural gas forms the basis of the competitive advantage of many Belarusian enterprises, including several largest chemical companies, whose production amounts to about 15% of the Belarusian exports.

In 2005 Belarus imported 19.31 million tons of Russian oil, paying 60% of the world price. It consumed 5.85 million tons for its own needs, and the remaining 13.48 million tons, after processing in two Belarusian refineries in Mozyr and Novopolotsk, were exported to the West as petroleum products. This system was very profitable for Belarus in the last years – the value of petroleum products exports amounted to 4.85 billion dollars in 2005 (see Table 2).

**Table 2. Import and export of oil from/to Belarus in the years 2001–2006**

Year	Oil import (millions of tons)	Petroleum products export (millions of tons)	Oil import value (USD billions)	Petroleum products export value (USD billions)
2001	11,91	7,65	1,37	1,20
2002	14,02	9,87	1,50	1,47
2003	14,88	10,56	1,98	1,96
2004	17,81	12,96	3,23	3,29
2005	19,31	13,48	4,22	4,85
2006*	19,7	14,5	5,41	6,72

Source: Ministry of Statistics and Analysis of the Republic of Belarus; Beltransgaz. Quoted in: *Republic of Belarus: Statistical Appendix*, IMF Country Report No. 06/316, August 2006, p. 40–41.

\* Estimates.

Consequently, income from the sale of processed Russian oil amounted to 35% of earnings from the Belarusian exports<sup>1</sup>. As a result, the country owes almost 50% of the value of its exports (petroleum and chemical products) to low prices of oil and gas.

Belarus' total dependence on Russian energy supplies is partially compensated by the country's position as an important transit country for gas and oil export from Russia to the European Union. Sixteen percent of the Russian gas exported outside the CIS was sent through Belarusian territory<sup>2</sup>. In 2006 it amounted to 44 billion cubic meters, out of which 29.5 billion cubic meters were transported through the Yamal gas pipeline, which belongs to Russia, and 14.5 billion cubic meters through Beltransgaz' gas pipelines<sup>3</sup>. Belarus is even more important as far as transportation of Russian oil is concerned. In 2006, 81 million tons of oil and 8.5 million tons of petroleum products were transported through its territory. Total exports of Russian oil to EU countries amounted to 130 million tons in 2006. Hence, Belarus is the key transit country for exports of Russian oil and gas into EU markets.

### Natural gas in Russian-Belarusian relations before 2006

Russian deliveries of natural gas to Belarus have been a very political matter since the beginning. Already in August 1993 Gazprom cut off natural gas deliveries for Belarusian consumers for the first time, due to Minsk's increasing payment arrears. A month later the Russian gas giant made the first attempt to take over Beltransgaz. The agreement signed at that time stipulated that the Belarusian company's assets would be leased to Gazprom for 99 years in exchange for increasing gas deliv-

<sup>1</sup> In the period between January and October 2006 total value of the Belarusian exports amounted to 16.4 billion dollars, while the value of petroleum products export reached 5.75 billion dollars. Source: Ministry of Statistics and Analysis of the Republic of Belarus.

<sup>2</sup> 80% is sent through Ukraine and 3.4% to Turkey through a gas pipeline on the bottom of the Black Sea.

<sup>3</sup> Beltransgaz was established in 1992 and is the owner of the Belarusian pipeline system, including transit pipelines of total traffic capacity of 21 billion cubic meters annually. 100% of the company's shares is state-owned.

eries to Belarus and for Gazprom's consent for the gas to be reexported. The document, however, has never been ratified by the Belarusian parliament. Already at that time Minsk came to understand how strategically important an enterprise Beltransgaz was and that it was a key instrument in its relations with Moscow.

In the second half of the nineties the recurring Belarusian debt to Gazprom was written off or credited by the Russian budget. Until 1998 almost all the Minsk's amounts due for gas were covered by barter exchange. Nevertheless, it was a time when Moscow still wanted to believe that it was possible to create a really functioning Belarus-Russia Union State and tried to turn a blind eye on the subsidizing of Belarusian economy, which increased every year. Lukashenka pointed to special Belarusian-Russian relations and demanded that the price of natural gas be identical with the price for Russian consumers. Although he did not fully succeed, the price of gas was nevertheless two times lower than the price paid by e.g. Ukraine. Despite these preferential conditions, in the years 1997–2000 Gazprom reduced gas deliveries several times due to arrears of the Belarusian side.

On the other hand, Gazprom enjoyed preferential transit conditions when transporting gas through the Belarusian territory. Under a bilateral agreement concluded in November 2000 the Russian gas giant agreed to keep delivering cheap gas in exchange for minimal transit rates (0.55 dollars for sending 1,000 cubic meters over 100 km through Beltransgaz pipelines and 0.46 dollars for sending gas through Yamal gas pipeline). These rates were three times lower than the Ukrainian or Moldovan fees.

Gazprom was the owner of the Belarusian section of the Yamal gas pipeline from the very beginning, nevertheless it adamantly tried to gain control also over Beltransgaz pipeline network. In April 2002 a Belarusian-Russian agreement was signed, pursuant to which Belarus would still be able to buy cheap gas from Russia, but in exchange it had agreed to create before 1 July 2003 a common gas company on the basis of Beltransgaz. Gazprom was to own 50% of the shares. An agreement was added to the contract, stipulating that in the 5 years to

come Belarus would be able to purchase natural gas paying internal Russian prices. The part of the document, which ensured that Gazprom would acquire a part of the Beltransgaz shares, has never come into force. Officially, the parties have never been able to reach an agreement concerning valuation of the company. Minsk claimed that it was worth at least 5 billion dollars, while Gazprom estimated its value to 600 million dollars. Despite of this, Belarus took the view that it was entitled to pay internal Russian prices for the gas and, indeed, in the next months it was what Minsk paid for the gas it purchased from Gazprom.

The first serious gas crisis between Belarus and Russia took place in February 2004. Gazprom started to lose patience because Minsk actually stopped the process of creating a common company on the basis of Beltransgaz and it announced an increase of natural gas price to 50 dollars, while Minsk did not accept this raise. After a few days, when gas deliveries were temporarily cut down, on 18 February 2004 the Russian gas giant stopped to send gas to Belarus through Beltransgaz pipeline network for 18 hours. It affected not only Belarusian, but also Lithuanian and Polish consumers. It was for the first time that Gazprom halted exports to one of the most important transit countries.

Alyaksandr Lukashenka harshly accused Russia of gas terrorism and threatened that Minsk could, as a sign of protest, withdraw from the Union State and impose retaliatory sanctions: demand payments for Russian military bases in the Belarusian territory and increase gas and oil transit prices. Moreover, Beltransgaz started to take the missing gas from the Yamal pipeline. The crisis ended with a *de facto* surrender of Gazprom. The gas giant was forced to turn the gas on, and the price was fixed to 46.68 dollars. Not only did Russia not gain control over Beltransgaz, but also it extended a 200 million worth credit to Belarus to compensate the results of price increase and it agreed to increase the transit rates to 0.75 dollars. Surprisingly, it turned out that it was Minsk who had more leverage in the negotiations with Gazprom, especially because the latter acted without working out earlier a strategy and assumed that Belarus would immediately accept its conditions.

Belarusian-Russian gas crisis also affected Gazprom's creditability as a natural gas supplier and provoked serious concerns about the security of deliveries in the EU and in EU candidate countries. Just like in the case of a later Russian-Ukrainian gas crisis (January 2006), the Russian gas giant was blamed for provoking the conflict.

Then, until mid-2006 Belarusian-Russian gas relations developed without any conflicts. Belarus purchased gas for about 47 dollars and avoided price increases, which affected other post-Soviet republics in the beginning of 2006. Ukraine started to pay 95 dollars, Armenia, Azerbaijan and Georgia 110 dollars, Moldova 150 dollars. A lower gas price for Belarus was kept, although the negotiations on transferring a part of Beltransgaz shares to Gazprom were *de facto* halted. It was a sign of political support for Lukashenka before the presidential elections of March 2006.

### Russia changes its policy on natural gas...

On 30 March 2006, eleven days after the end of Belarusian presidential elections, Gazprom unexpectedly announced that it was going to raise gas price for Belarus up to a 'market level' from 2007 on. Shortly thereafter prices between 140 and 200 dollars were mentioned. On 9 May, according to the usually well-informed daily *Kommersant*, Vladimir Putin signed a special decree, ordering to stop subsidizing, directly or indirectly, the Belarusian economy, and also to prevent reexporting Russian goods, including gas and oil, through the Belarusian territory. This information was not officially confirmed for the next six months. On 3 November the Russian ambassador in Minsk, Alexander Surikov, explained the situation partially, saying that new gas price may amount to 140 or 200 dollars, depending on whether Belarus will agree to sell 50% of Beltransgaz shares. He also added that 'when a Union State is created, all such questions like gas prices increase will be taken off the agenda. We do not intend to pay only for a Belarusian promise to join the common state.' Minsk was also threatened by Valery Yazev, Chairman of the State Duma Committee on Energy, Transport

and Communications, who confirmed that Gazprom intended to sell Belarus gas for 230 dollars from 2007 on.

Minsk initially tried to avoid commenting on the situation concerning Russian energy supplies, but finally it was forced to take a position. Chairman of the Standing Committee for Foreign Affairs and National Security of the Belarusian Parliament, Nikolai Cherginets, said that Putin's statement 'was, if not dictatorial, then in the form of an ultimatum', and threatened that Belarus might revise the conditions upon which Russian military facilities were located in its territory. Alyaksandr Lukashenka issued a statement, saying that 2007 was going to be 'a very hard and catastrophic year' and publicly asked 'where would Belarus take a billion of dollars from, if Russia increased the price of gas so much?' He also instructed the government to seek alternative sources of energy supplies wherever it was possible, including especially Venezuela, Iran and Azerbaijan. Lukashenka himself paid an official visit to Tehran at the beginning of November. A Belarusian delegation was also sent for negotiations to Baku. Nevertheless, it is virtually impossible for Belarus to diversify its oil and gas supply in the next several years.

During Russian-Belarusian negotiations on gas prices Alyaksandr Lukashenka and Vladimir Putin met three times – on 10 November, 29 November and 15 December 2006. During the second meeting, which took place within a CIS summit in Minsk, the Russian president talked about the necessity to move to market prices and informed that both parties reached an agreement concerning creating a consortium on the basis of Beltransgaz. Nevertheless, the information was not confirmed by Minsk. Consequently, all the meetings met with a failure. Russia did not want to give up its demands, while Belarus refused to accept them.

In the second half of December 2006 the gas dispute turned into an open conflict, and the situation became similar to Russian-Ukrainian gas negotiations a year before. Gazprom threatened that if a new agreement was not signed, it would halt deliveries from 1 January 2007 on. There also was information in the press that the gas giant prepared to cut off Belarus' gas, gathering earlier additional amounts of natural

gas in tanks in Germany and Lithuania. Minsk answered with a threat that it would take gas from the Yamal pipeline, if the deliveries were stopped, all the more so because the Belarusian authorities wanted to make the signing a new agreement on Russian gas transit through Belarus' territory conditional on simultaneous signing of a contract on gas delivery for their own needs. Should there be no document on gas transit, the gas sent through Belarus to the EU would in fact be equal to contraband. Minsk took the view that it had the right to purchase gas for an identical price as the border Smolensk region (where in 2007 the price of natural gas amounts to 54 dollars), quoting the agreement with Russia concluded in April 2002.

On 26 December Gazprom unexpectedly lowered the proposed price from 200 to 105 dollars, out of which 75 dollars would be paid in cash and 30 dollars with Beltransgaz shares. Nevertheless, Belarus rejected this compromise offer and tried to achieve in the negotiations a price of 45 dollars in cash and 30 dollars in the company's shares. The talks reached an impasse.

An agreement was reached almost in the last moment. On 31 December, just before midnight, Gazprom chief Alexey Miller and the Belarusian First Deputy Prime Minister Vladimir Semashko signed two documents: 1) an agreement on deliveries and transit of gas, which will be binding to 1 January 2011 and 2) a protocol on creating a common company on the basis of Beltransgaz. The price was set to 100 dollars for 1,000 cubic meters. However, in the subsequent years it is going to amount to 67% of the market price in 2008, 80% of the market price in 2009 and 90% of the market price in 2010<sup>4</sup>. The price of natural gas transit through Beltransgaz pipelines rose from 0.75 dollars to 1.45 dollars<sup>5</sup>.

According to the signed document, until 2011, 50% of Beltransgaz stock will be sold to

Gazprom for 2.5 billion dollars in four installments, each consisting of 12.5% (625 million dollars) and paid every subsequent year. The first 12.5% of the Belarusian company's shares is to be sold before 1 June 2007. Therefore, Gazprom accepted the maximal valuation of Beltransgaz (5 billion dollars), proposed by the ABN Ambro bank.

### ...and oil

On 12 December 2006, when intensive negotiations on gas price took place, Russian government informed that from 1 January 2007 a duty on oil exports to Belarus will be imposed 'in order to protect Russia's economic interests'. Currently, the duty amounts to 180.7 dollars per ton. Previously, it was possible to import Russian oil and gas into Belarus without duty due to the customs union with Russia, concluded in 1995, which abolished the customs boundary between the two countries. However, the agreement also stipulated that the duty income from petroleum products exported from Belarus would be divided between the budgets of the two states according to a specified proportion: 85% for Russia and 15% for Belarus. In 1998, however, Minsk ceased transferring the duty income to the Russian budget, leaving them in Belarus. The introduction of export duty is in fact tantamount to ending the customs union.

Should Moscow's decision be implemented it would mean the increase in Russian oil price from 275 dollars in 2006 to 455 dollars in 2007, and therefore it would be more harmful for Minsk than the rise of natural gas price. The expenses for purchasing oil would rise from about 5.41 billion dollars in 2006 to about 8.94 billion dollars in 2007<sup>6</sup>. Furthermore, processing the oil in Belarusian refineries and then reexporting it to the EU would be close to the limit of profitability.

Russian oil companies also took advantage of the fact that there was no customs boundary between Russia and Belarus, because Belarusian export duty on petroleum products

<sup>4</sup> 'Market price' was not defined. Gazprom's statement said only that the price for Belarus will be calculated 'adequately to how the price is calculated for deliveries of Russian gas to Europe'.

<sup>5</sup> According to Gazprom's representatives statement the price will be constant until 2011; according to the Belarusian side the price was fixed only for 2007 and afterwards it will rise together with the raise of gas prices.

<sup>6</sup> In 2006 Belarus spent about a billion dollars to purchase 21 billion cubic meters of Russian gas. In 2007 it will cost Minsk about 2.1 billion dollars to buy a similar amount of gas.

was lower than the Russian one – in 2006 it amounted to 57–75 dollars per ton, while the duty on export from Russia was 108 dollars per ton. Using preferential tax conditions the Russian oil companies delivered crude oil to the Belarusian refineries, a then exported it – as Belarusian petroleum products – to the EU countries<sup>7</sup>. According to the Russian Industry and Energy minister, Victor Khristenko, ‘all Russian oil companies pushed through to able to be send oil through Belarus in order to avoid higher taxes’. Consequently, the Russian budget lost yearly about 1,8 billion dollars due to this mechanism.

Moscow explained the decision to impose a duty on oil export to Belarus saying that Minsk rejected its demands to transfer 85% of the income from Belarusian export duty on petroleum products to the Russian budget. Minsk suggested an alternative division: 70% for Belarus, 30% for Russia, which in turn was rejected by Moscow. However, this radical measure was not unexpected. As early as in April 2006 Russia tried, in vain, to convince Belarus to give it a half of the income from the duty. The aforementioned Putin’s decree from 9 May 2006, which was confirmed in December, was another signal. Finally, the Russian president himself mentioned the issue on 25 October during a television ‘interview with the nation’<sup>8</sup>. Official reaction of Minsk was initially exceptionally moderate. The Belarusian Ministry of Foreign Affairs announced that ‘Russia imposing duty on oil deliveries to Belarus is in violation of a number of binding agreements, concerning the principles of free trade between the two countries’. Nevertheless, one may as-

sume that during the negotiations on gas prices the question of abolishing duty on oil was raised and that both issues were negotiated ‘in one package’. President Lukashenka mentioned it himself, saying on 3 January 2007 that he instructed the government to sign the gas agreement, because ‘Russian government and leadership promised us to solve the oil problem. It was announced that once the question of a contract on natural gas and transit had been solved, the question of oil deliveries would also have been solved’.

Belarus proposed a compromise solution – to divide the duty equally between both states’ budgets. As Moscow did not react, on 3 January 2007 Minsk imposed duty of 45 dollars per ton on the transit of Russian oil through the Belarusian territory. The Belarusian Ministry of Foreign Affairs declared it to be a ‘retaliatory measure’. Belarus’ surprising decision violated several bilateral agreements and made Moscow raise its objections and declare that ‘such an approach has no analogy in the world’ and that Russia already paid a transit fee. Nevertheless, this also shows how determined Lukashenka was to return to importing Russian oil without duty.

In the next days the crisis became deeper and deeper. Belarus refused to purchase the Russian oil at the new price and started to steal oil from the transit pipeline ‘Druzhba’. Consequently, on 7 January Transneft, the pipeline operator, stopped sending oil to Belarus, thus stopping to deliver oil for consumers in the European Union, most importantly Poland and Germany. Initially Russia blamed the Belarusian side for stopping the export of oil. However, after a dozen or so hours the Vice President of Transneft, Sergey Grigoryev, admitted that it was his company that had turned off the oil due to the fact that Belarus had illegally taken oil from the pipeline. This is how the results of the Belarusian-Russian conflict also affected EU consumers. Minsk defended itself, claiming that the oil it took from the pipeline was a fee for the transit duty Russia had not paid. Moscow initially refused to negotiate, demanding that Belarus had to abolish its transit duty before any talks could commence. The situation was only clarified after a phone talk between Vladimir Putin and Alyaksandr Lukashenka. As a result, on 10 January Belarus

<sup>7</sup> The structure of Russian oil suppliers to Belarus was as follows: Surgutneftegaz 30%, Rosneft 25%, Sibneft (currently Gazpromneft) 13%, Lukoil 11%, Slavneft 10%, Russneft 6.5%, others 4.5%.

<sup>8</sup> Vladimir Putin said that in the relations with Belarus ‘some things really concern us. For example, we see the amount of our crude oil, which is delivered to refineries in Belarus, we know the needs of the republic and we see how much petroleum products are later sent abroad. And here we must obviously put the situation in order through a normal dialogue with our Belarusian colleagues (...) If we are not able to reach an agreement, we will have to introduce some restrictions, which is something we very much would not like to do’. 25 October 2006 [http://kremlin.ru/appears/2006/10/25/1303\\_type63376type63380type82634\\_112959.shtml](http://kremlin.ru/appears/2006/10/25/1303_type63376type63380type82634_112959.shtml).

announced that the transit duty was abolished, and Transneft resumed oil deliveries through the 'Druzhba' pipeline.

On 12 January, the prime ministers of Russia, Mikhail Fradkov, and Belarus, Siarhei Sidorski, worked out a compromise agreement. The rate of Russian export duty was diminished from 180.7 to 53 USD per t. It shall be imposed only on crude that is to be re-exported after processing in Belarusian refineries (14 mn t) and will not include oil used in the internal market (6 mn t)<sup>9</sup>. Belarus will also retain full income from the export duties it imposes on petroleum products<sup>10</sup>. Meanwhile, Belarusian export duty rate has been raised to the level of Russian one. The agreement introduces sanctions for the violation of this condition, i.e. raising the Russian duty on oil to standard level. The agreement managed to temporarily regulate the Belarus-Russia energy conflict, which lasted for a few weeks before.

### Conclusion and prognoses

- It is the principal objective of the Russian policy towards Belarus to achieve permanent political control over the country through making it fully economically dependent on Russia. It is about creating such conditions, which will make Belarus unable to function separately from Russia, while formally keeping its independence. Moscow no longer believes it to be possible to create a really functioning Union State and – although it has not abandoned the integration rhetoric yet – it tries to influence the situation in Belarus through gas and oil. Russia's policy towards Minsk is new, because it has never so determinedly and radically used 'the energy weapon' against its 'most loyal

<sup>9</sup> The parties agreed also that in 2008 Belarus was going to pay the duty on Russian oil in the amount of 33.5% of its standard value, and in 2009 – 35.6%. Presently, the standard rate is 180.7 USD, and if it is maintained, Belarus would pay 60 USD in 2008 and 64 USD in 2009.

<sup>10</sup> The agreement includes also a complicated scheme of dividing Belarusian duties on petroleum products export. In 2007, 70% is to be kept by Russia and 30% by Belarus; in 2008, the proportion is to be 80%:20%, and in 2009 – 85%:15%. In fact, the division scheme is virtual, since all duty income is going to be supplied to Belarusian budget, whereas Russia will receive its share through duties on oil crude export (53 USD per t).

ally'. Gaining control over Beltransgaz and other strategic economic assets (most importantly refineries and chemical plants) is supposed to be a means for making the Belarusian economy fully dependent on Russia, without the possibility to offset this dependence somehow through the control over transit gas pipelines, through which Russian gas is sent to the EU. Consequently, every future attempt by Minsk to break dependence from Moscow will translate into a severe economic crisis.

- Nevertheless, the signed gas contract is not a surrender of Belarus and Gazprom achieved only a moderate success. Indeed, the Russian gas giant was able to force through an increase of the gas prices, but Belarus is going to pay the lowest price among all the CIS states, after all. Minsk was also able to separate two issues: concluding an agreement on natural gas deliveries and creating a common company on the basis of Beltransgaz. One may assume that it is going to be a difficult task for Gazprom to take over even a part of the Belarusian enterprise. It cannot be ruled out that the 2002 scenario will be repeated, when after signing a similar agreement Belarus infinitely postponed its implementation, as a result of which the contract has never come into force. Furthermore, many factors indicate that Belarus, as it did many times in the past, will have problems to settle payments for gas in time. In the beginning of January the Belarusian Prime Minister Siarhei Sidorski said that the Belarusian economy could not cope with the provisions of the concluded agreement and stated also: 'if we will not have enough money to pay, we will ask our partners from Gazprom to postpone the payments'.

- Belarus has succeeded in radically diminishing Russian export duty on oil imported from Russia. The agreement, however, is less profitable than expected by Minsk, which, during the negotiations, aimed at the abolishment of duty on imported oil. *In fact*, such a solution is going to limit the income for the Belarusian budget, and due to the standardization of Russian and Belarusian duty the export of petroleum products to the EU will become less profitable, yet it will be less harmful than in the case of introducing Russian oil export duties on the initially announced level.

- Russia, although it intends to limit the subsidizing of the Belarusian economy, agreed to sign the compromise agreement, because is in fact not interested in provoking an economic crisis in Belarus, as such would be the result of the increase of gas prices and introducing a 180.7 dollars duty on oil combined. Destabilization of the economical situation in the country could provoke social unrest and lead to a uncontrolled change of the government, which is not in accordance with Russia's interests. Even more so, as in the months to come Moscow will be preoccupied with the coming Russian parliamentary and presidential elections.

- Russia's increasing gas prices and, most importantly, changing oil delivery policy mean the beginning of the end of the Belarusian economic model, whose main foundation were deliveries of cheap energy supplies. Belarus will be forced to implement economic reforms and market mechanisms, because otherwise its economy is going to suffer from a very grave crisis, which will be followed by a political crisis. Hence, the economic changes will have to be accompanied by changes of the political regime, while it is still an open question how long they will last and how far reaching they will be.

- Results of Moscow's decision will be noticeable already in 2007. The introduction of duties on oil export will result in losses for the Belarusian budget in the amount of ca. 1 bn USD per year, and increasing gas prices will cause additional losses of about 1 billion dollars. Consequently, cumulated Belarusian costs resulting from Russian actions may amount to the loss of about 6% of the country's GDP. According to some estimations, further increase of gas prices will make 45% of Belarusian companies operating on the domestic market and 60% of those who are active in foreign markets no longer competitive. Increase of the gas price will be partially compensated by the rise of transit fees to 1.45 dollars and acquiring 625 million dollars from

the first installment for Beltransgaz (if Minsk is really going to implement the agreement with Gazprom). Belarus can also raise the fee for the transit of Russian oil. The current rate of 0.51 dollars for transit of 1 ton over 100 kilometers is one of the lowest in Europe.

- Russian-Belarusian negotiations on gas and oil have also proven that not only is a gas customer dependent on the deliveries, but also the supplier is dependent on a transit country. Minsk has proven that it is able to use some retaliatory measures, which may relatively painfully affect Russian interests. One of such measures was the unprecedented decision to impose a duty on the transit of Russian oil and to illegally take oil from the transit pipeline, which made Russia fully stop its deliveries to the EU. The decision should, however, be interpreted solely as an attempt to exert pressure against Russia to abolish the duty on oil export to Belarus.

- The events of the first days of January did not finish the crisis in the Belarusian-Russian relations. Should Belarus not fulfill the agreement regarding gradual sale to Gazprom of Beltransgaz shares, or fail to make payments for natural gas in time, the crisis may enter a new phase the future months. Moscow has already warned that it might decide to impose duties on some Belarusian foodstuffs. This might lead to Lukashenka fulfilling his warnings of early January, when he instructed the government to send Russia 'proposals of payments for all that Moscow now gets for free, starting with military installations and transit'. Should Belarus-Russia relations deteriorate, it may not be excluded that Minsk would raise the issue of Yamal gas pipeline ownership. Consequently, it is probable that in the next months the Belarusian-Russian relations will remain very unstable. The energy crisis with no doubt initiated a transition of the relations to a completely different level.

*The text was completed on 15 January 2007*