

Help Wanted: Energy Coordinator

A global energy policy could alter the balance of power in energy markets and obviate resource wars

Josef Braml | **A new global energy framework is long overdue. The Obama administration could well be interested in teaming up with the European Union to create one. In addition to enhancing security, it would also spur economic growth and curb global warming.**



JOSEF BRAML is editor-in-chief of the DGAP's *Jahrbuch Internationale Politik*. The current volume is a comprehensive analysis of energy-related issues by leading experts.

For the present, Europe's goal of creating a unified and dependable EU domestic market for electricity and gas remains wishful thinking. One of the most striking—and backward—aspects of the European energy market is its lack of market integration, especially in electricity. In order to ensure that member states open their energy markets, we not only need unified standards of implementation but a European regulatory agency with sanctioning mechanisms that can counter unfair competition.

The European Union should also develop a unified policy in its external relations. Europe has neither a clear idea how the changes of government in Moscow and Washington can be exploited, nor does it have a plan for how to deal with states that pursue regional power through energy policies, including nuclear power ambitions. Europe's dependence on crude-oil exporting nations makes it equally clear that it must continue to develop multilateral structures to deal with these market failures and market powers.

Energizing Transatlantic Relations

In terms of energy and climate issues, neither the United States nor the European Union have gone beyond declamatory and non-binding goals. Barack Obama's election as US president and the realignment of established interest groups in the American energy policy debate presents a fine opportunity to cooperate in a political area that is of central importance to the future of energy-dependent economies.

During his campaign, Obama explained that an immense economic potential resides in alternative energy. Accordingly, the annual global demand for sources of energy with minimal fossil components will reach \$500 billion by the year 2050. In view of the acute economic crisis, President Obama asked the US Congress to get the ball rolling on an \$800 billion economic stimulus package. Investment in modernizing the energy infrastructure is not only intended to create jobs in the short term, but has the long-term objective of reducing America's oil dependency and carbon footprint. First and foremost, the United States is concerned with developing alternative fuels and efficient technologies for the transport sector. Here is where German and European policy can have an impact: a transatlantic energy and environmental partnership could promote research and investment in new technologies as well as free trade in alternative fuels. It would be in their mutual interest, moreover, to counteract the Russian tendency to make traditional energy relations bilateral.

Cooperation with Russia

Europe still has no blueprint for its future strategic relationship with Russia. A new partnership and cooperation treaty is necessary, particularly as Russia sees the European Energy Charter (EEC) as a relic of the early 1990s when Russia was weak and still had to play by the West's rules. The EEC served more to protect Western interests vis-à-vis Russia's energy supply rather than mutually benefiting both sides. Under the terms of the charter (which were never fully ratified by Russia), Russia's energy supplies became open to free trade, and foreign investments in Russia's energy infrastructure were protected. By means of exclusive bilateral agreements with European companies, Moscow can use its newly won status as an energy superpower to intensify the competition among European states and companies for Russian energy sources and play them off against one another. Pipeline plans are also guided by the Kremlin's geopolitical considerations. The Blue Stream Project undermines European diversification efforts (Nabucco Pipeline) as it would allow Russia to route energy supplies to Turkey via a trans-Black Sea pipeline.

Nevertheless, the financial crisis and recent developments in the energy markets have created possibilities for cooperation. Due to sinking energy prices, Russia's self-confidence has been reduced to a level allowing for negotiations between equal partners. According to some observers, crude oil prices of less than \$60 a barrel endanger the financing of necessary economic reforms in Russia and possibly—if the petroleum dollars fail to materialize before long—threatening its political stability. The financial crisis has only heightened Russia's interest in foreign investments and its willingness to cooperate.

Nuclear Nonproliferation Regime

Cooperation with Russia is also critical to the nuclear nonproliferation system being able to adapt to changed technical and economic circumstances. As civilian use of nuclear energy for the generation of electricity increases, so too has

Cooperation with Russia is critical to the nuclear nonproliferation system.

the need for enrichment and reprocessing facilities as well as the demand for natural uranium reactors. These reactors all have one thing in common: they employ materials that can be used to make nuclear weapons. North Korea and Iran illustrate the international nuclear order's vulnerable areas. What is required is a group of states that are ready and able to defend the nuclear nonproliferation system against such challenges as the North Korean and Iranian nuclear programs.

Even without the nuclear option, Iran poses a massive potential threat. Iranian troops stationed not far from the Strait of Hormuz, a strategically critical position, could halt the daily delivery of 17 million barrels of oil, which according to American security experts equals 40 percent of the world's oil trade.¹ Were the "Iranian oil weapon" to be deployed, a marked rise in oil prices would take place, causing lasting damage to Western and Asian economies.

OPEC's Strategic Market Power

In addition, the growing power of the Organization of Petroleum Exporting Countries (OPEC) threatens the energy security and economic strength of oil-dependent nations. OPEC's potential power becomes clear in considering the fact that those ten countries with the largest proven oil reserves—with the exception of Canada and Russia—are all OPEC members.² OPEC controls over seventy percent of all known oil reserves. Though OPEC's share of world production remains constant at forty percent, in the long term the cartel's power is increasing in the same proportion as resources of non-OPEC countries are dwindling. To ward off the strategic market power of OPEC, innovative governments could raise anti-cyclical taxes on fossil fuels that are coupled with the market price for oil. Investments would then be protected from potentially sudden price collapses—that may be engineered by OPEC—and tax revenues could be utilized for the research and development of renewable energy.

The growing power of OPEC threatens the energy security and economic strength of oil-dependent nations.

When the Market Fails

The usefulness of energy prices for governance should be purposefully exploited. When energy prices, particularly in the industrial countries, are systematically raised, then one can more reliably plan adaptive measures with regard to energy supply and demand. Unaccompanied by political flanking measures, markets are as unable to meet the challenges posed by OPEC, climate change, and sketchy research efforts as they are to solve the distribution problems associated with high oil prices. Energy security, environmental protection, and human rights are all public commodities that should not be left to imperfect

¹) Anthony H. Cordesman, "Iran, Oil, and the Strait of Hormuz," March 26, 2007, pp. 2, 7, http://www.csis.org/media/isis/pubs/070326_iranoil_hormuz.pdf.

²) "Worldwide Look at Reserves and Production," *Oil & Gas Journal* 103, no. 47 (December 19, 2005), p. 24–25.

(energy) markets distorted by the suppliers. Market imperfections such as oligopolistic structures and the neglect of negative external effects (carbon dioxide pollution, nuclear waste, proliferation) or positive ones (research and development) not only justify but in fact cry out for state intervention.

An example of market failure through “negative externality” is the impact on the global climate of the burning of coal, gas, and oil. But for users of oil and other fossil fuels, the market price for such fuels is hardly an indicator of the social costs arising from their polluting emissions. Politicians can take countermeasures against these external costs by integrating them in the price mechanism. This can be achieved through climate policy instruments such as an emissions tax or emissions allowance trading. If EU states wish not to forfeit the credibility gained through their pioneering role in promoting a global and internationally binding post-Kyoto Treaty—and the associated market chances for energy-saving technologies and renewable energies—then they should not deviate from their climate objectives despite the current economic crisis.

The market also disregards the positive external effects of research and development. Technological innovations benefit many oil importers; they cannot be prevented from using a certain innovation—as would be the case with private commodities. The trailblazing innovator himself would thus have to bear the high costs, but with little hope of profit and small incentive to invest in research. Without political control—for example through patent protection or subsidies—too little research and innovation takes place. To remedy market shortcomings one must increasingly promote the research and development of energy-efficient techniques and renewable energy. There are incentives for multilateral action particularly in terms of alternative fuels and in the development of marketable technologies. A further reason to create such structures for collective research efforts is the problem of “free-riding,” or the worldwide application or “copy-cating” of pioneering research achievements by third parties. With multilateral financing, an international group of scientists and economic experts could develop new technologies and market strategies.

Reform of Multilateral Organizations

In order to meet the new challenges, a whole array of multilateral organizations and transnational structures must adjust to the new conditions; but affected, first and foremost, are the International Energy Agency (IEA) and the World Trade Organization (WTO). In particular, the IEA’s system for securing the fuel supply must undergo further development. The IEA’s establishment as an autonomous unit of the Organization for Economic Cooperation and Development (OECD) in the mid-1970s was a tacit recognition that securing the oil supply should not be entrusted solely to the oil companies and that long-term energy policy measures were necessary—measures that transcended the national framework. This OECD club must now be expanded. All of the important oil-producing and transit and consuming nations should be integrated at

Medium- and long-term cooperation with countries such as China and India is indispensable.

both the regional and global level, and within new structural frameworks if necessary. Above all, medium- and long-term cooperation with countries such as China and India is indispensable. All of the great Asian economic powers have hitherto tended to pursue a neo-mercantilist or nationalistic approach to securing energy imports and their routes of transport, which makes the development of cooperative and market-oriented approaches difficult.

In trade policy, negotiations between energy-rich candidates for accession and energy-importing members could lead to long-term development of the WTO's rules and regulations. In particular, rules must be developed that would harmonize the interests of oil and gas exporters with those of producers of renewable energy. The growing global trade in biofuels has created numerous issues for international trade policy that go far beyond the present core competence of the WTO. They concern climate protection, the securing of fuel supplies, and world hunger.

Mr. Energy's Multitasking

To guarantee energy security in the widest sense of the term—that is, to bring the partly complementary and partly conflicting goals of energy security, economic efficiency, environmental compatibility, and human rights into greater accord with one another—the first requirement, at the individual state level, is to establish a non-partisan interagency apparatus. In Germany, this would take the form of a kind of federal security council. The next step, at the European level, would be to set up an “energy coordinator.” This would be necessary if only to have a contact partner for other nations that, like the United States, will have established similarly comprehensive structures.

A global energy policy could improve security of the energy supply, give fresh impulses to economic growth, and curb the greenhouse effect. Such a sweeping political plan could reduce or obviate human suffering by readjusting the balance of power in the energy markets and forestall further wars over resources. Germany, as a nation dependent on energy imports, should play a leading role.