

What did Russia get from its gamble with the Kurdish Regional Government in Iraq?

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Energy giant Rosneft struck major deals with Iraq's Kurdish region in 2017. Today, it has yet to cash in on them.

Erbil, Iraq - Two years after Iraq's new constitution in 2005 officially recognised the autonomy of the Kurdish region of northern [Iraq](#), Russia established formal relations with its regional government (the KRG) by [opening](#) a consulate in its capital Erbil.

By then, the [United States](#), the United Kingdom, [Iran](#) and Turkey had become the main political and economic players in the oil-rich region, which holds proven reserves of some 45 billion barrels of oil (10th biggest in the world) and is estimated to have between 2.8 to 5.7 trillion cubic metres of natural gas (roughly as much as [Algeria](#)).

Although [Russia](#) boasted "historic" relations with the Kurdish leadership (Mustafa Barzani, the father of the former KRG president, [Masoud Barzani](#), spent 12 years in exile in the Soviet Union), it seemed there was little space for it to play a major role in the autonomous region.

But when, in the early 2010s, Russian energy companies sent delegations to probe for potential oil deals, KRG's western partners became nervous. According to a former Russian diplomat who spoke to Al Jazeera on condition of anonymity, the [UK](#)'s foreign office, in particular, was worried.

In a 2012 conversation with him, British officials expressed their concern that the Russian companies' entry into the Kurdish energy sector could stir trouble by giving the KRG political backing to go against the common consensus among the UK, US, [Turkey](#) and Iran that the Kurdish region should remain part of Iraq.

In 2012, Russian state-owned energy giant Gazprom signed a contract for exploration and oil production in two blocks in the Kurdish region and just a year later KRG's President Masoud Barzani went on a four-day visit to Moscow, meeting with Russian President [Vladimir Putin](#) and Gazprom CEO Alexei Miller.

Four years later, the fears of the British Foreign Office proved justified. A series of energy deals that another Russian state-owned energy company, Rosneft, concluded in 2017 with the debt-laden KRG, saved it from economic collapse and helped it gain enough political leverage to [pursue an independence referendum](#) on September 25 of that year, against the advice of all of its close allies, including the US and the UK.

It was not the first time Rosneft, whose CEO Igor Sechin is perceived to be one of Putin's closest political allies, had come to the "rescue" of a foreign government in financial distress and under political duress. Over the past few years, it has continued to invest heavily in crisis-stricken [Venezuela](#), despite [losing millions](#) of dollars in the process. Rosneft's investment has effectively propped President Nicholas Maduro's government and secured Russia a loyal ally in the

“US backyard”. The Kremlin has long been accused of using state-owned energy companies as political tools.

In the Kurdish region of northern Iraq, however, Russian diplomatic gains appear much more limited because of political uncertainty, and regulatory and technical barriers. In fact, Rosneft is yet to turn a profit from the more than \$4bn it invested in oil and gas deals, sources have told Al Jazeera.

So, two years after the Rosneft deals were concluded, what did Russia get out of its KRG gamble?

‘Saving’ the KRG

In 2016, the KRG was suffering from a severe political and economic crisis. It was in the middle of fighting a war against the Islamic State of Iraq and the Levant ([ISIL](#) or ISIS), which had become a source of insecurity and a significant financial burden. Its budget had taken a major hit after the 2014 slump in oil prices had dwindled revenues. And a dispute with Baghdad over the right to export oil independently had escalated and resulted in the cutting of payments from the federal budget.

As the Kurdish region was backtracking on major economic achievements of the post-2003 period, popular anger had grown exponentially. The economic recession and cuts to salaries had [provoked](#) angry mass protests across the region.

Having racked up a debt of between [\\$20bn](#) and [\\$25bn](#) (way above the size of its economy), the KRG was running out of options to save itself from bankruptcy. In March 2016, the KRG [offered](#) major oil assets to Turkey in exchange for \$5bn in debt forgiveness and cash, in addition to the \$1bn Ankara had already lent; major oil deals were also offered to US companies. Both the Turks and the Americans, however, appeared reluctant to take up what was on offer.

In June, Prime Minister Nechirvan Barzani [headed](#) to Russia to attend the St Petersburg Economic Forum - Putin’s flagship investment event - where he met Russian Foreign Minister Sergey Lavrov to discuss “developing relations [...] in the oil and gas sector”.

Seven months later, on February 21, Rosneft joined Gazprom as a major investor in the Kurdish region by signing a deal worth \$2.1bn for pre-paid oil for 2017-2019 and becoming the first major oil company to pre-finance KRG oil. That cash injection was crucial.

According to Bilal Wahab, a fellow at the Washington Institute in the US, these funds helped avert a major financial disaster and international embarrassment for the KRG by enabling it to settle a dispute with Dana Gas and Crescent Petroleum ahead of another hearing by the London Court of International Arbitration scheduled for the summer of that year. The Kurdish authorities paid [\\$1bn](#) to the Emirati companies and restructured the remaining \$1.24bn it owed. The deal also provided some legitimacy to KRG’s oil export operations, which Baghdad had long claimed were illegal without its formal permission, Wahab pointed out.

On June 2, Nechirvan Barzani once again attended the St Petersburg summit and [signed](#) a number of agreements with Rosneft, paving the way for three more deals, including projects worth [\\$400m](#) for five exploration blocks in the Kurdish region’s northwest.

On September 18, just a week before the independence referendum was scheduled to be held, the KRG announced it had signed a contract with the Russian company to develop a gas pipeline project in the autonomous region with a planned investment of [\\$1bn](#), according to Reuters news agency. The project envisions a pipeline with a capacity of 30 billion cubic metres a year to be linked to the Turkish gas network and eventually export Kurdish gas to [Europe](#).

Then, in October, three days after forces loyal to Baghdad [captured](#) the oil-rich city of Kirkuk from the Kurds, the KRG [announced](#) it had sold its 60 percent share in the company that runs the region's oil pipeline to Rosneft as part of a major pipeline project worth \$1.8bn.

All these deals came in combination with an informal commitment for political support from Moscow, according to the former Russian diplomat. Although officially Russia declared a neutral position towards the referendum, the Kremlin unofficially made it clear it was going to stand by Masoud Barzani, he said. This gave enough confidence to the Kurdish leadership to proceed with the vote on September 25, despite serious warnings from Baghdad.

The fact that a number of deals were signed amid unprecedented uncertainty and insecurity in the Kurdish region, and right after Erbil lost control over oil-rich Kirkuk (which accounted for some 40 percent of its oil exports) demonstrated that Russia stayed true to its commitment. As a top KRG official told Al Jazeera, in that grave political and economic situation, "what saved us was Russia!"

Although it displeased the KRG's US and European allies, Russian support helped the region overcome international political isolation through this difficult period and start rebuilding its devastated economy. Rosneft's financial injection boosted its energy sector. The arbitration settlement allowed Dana Gas and Crescent Petroleum to start [investing again](#) in the Kurdish region and expand their gas production capacity.

The KRG also had enough leverage to start negotiations with Baghdad. In March, the Iraqi government sent money for the salaries of government employees in the Kurdish region [for the first time since 2014](#); as a result, for the first time in many months, KRG civil servants received their pay in full.

Russia's elusive gains

While the KRG has been reaping the benefit of these deals, Russia and Rosneft's gains from this high-risk investment are yet to materialise in full. In fact, pursuing these and other deals in 2017 got the Russian energy giant heavily in debt at a time when the Russian economy was just emerging from a two-year recession. It had to [borrow](#) some \$17bn in that year alone and by 2018, its debt stood at [\\$55bn](#), which worried investors.

What appears to be the main accomplishment of the Rosneft investments in the Kurdish region is securing the gas pipeline contract in September 2017.

According to an official from the KRG's ministry of national resources, who spoke on condition of anonymity, Rosneft's entry into the Kurdish energy sector "is about gas, not oil".

"Russia just wanted to reserve the right to develop the gas pipeline [to Europe]. Nabucco failed, that's why Russia came. The Europeans are to blame," the official told Al Jazeera, referring to a pipeline project which was supposed to provide countries in Southeastern Europe with an alternative source of gas and decrease their dependency on Russian gas imports and which has since been scrapped.

Currently, Gazprom holds monopoly over Russian gas exports to Europe. According to Salih Yilmaz, an analyst with Bloomberg Intelligence, by securing a gas deal with the KRG, Rosneft seeks not only to increase gas exports under Russian control to Europe, but also challenge Gazprom.

"Bringing the Kurdish natural gas to Turkey [and then] to Europe is probably Rosneft's best bet for rivalling Gazprom's gas export monopoly, [which] Rosneft and peers have been lobbying the Russian government to end," Yilmaz told Al Jazeera.

Rosneft's acquisition of 30 percent of Egypt's Zohr gas field in the Mediterranean Sea - a deal which was closed in October 2017 [just two weeks](#) after the KRG one was signed - also reflects these ambitions. Although both companies are majority state-owned, they are perceived to be driven by divergent oligarchic interests within the Russian economic elite.

According to Yilmaz, the development of the gas pipeline project in the Kurdish region could take a couple of years under ideal conditions, but given ongoing tensions in the region and the fact that there is no immediate and urgent demand for such gas exports, it could take much longer.

"Right now, it's probably more of a good-to-have [project], so I suspect that it won't be done any time soon," he explained.

However, there is another major obstacle to realising this and the other deals Rosneft and the KRG have signed: Baghdad has [rejected](#) them since they were concluded without its approval.

The Iraqi government has long argued that the KRG does not have the right to unilaterally sell oil without its permission; Erbil has countered by pointing out that a provision in the Iraqi constitution allows it to exploit natural resources on its territory.

In the past, the central Iraqi government has successfully undermined KRG oil trade on a number of occasions, with courts in the US and Canada ruling in [its favour](#) and blocking attempted sales. It has filed lawsuits in both [international](#) and [local](#) courts seeking to block the KRG from exporting oil through the Kirkuk-Ceyhan pipeline. In the past, these regulatory challenges have kept major oil companies out of the Iraqi region.

The lack of a final agreement between Baghdad and Erbil on the question of energy resource development and revenue transfer has effectively rendered the status of Rosneft's deals uncertain. When asked about the official position of the Iraq government on the Rosneft contracts, Asim Jihad, a spokesperson for the Iraqi oil ministry told Al Jazeera: "Successive federal governments have expressed their reservations, opposition, and rejection of the KRG's activities [exporting oil and concluding contracts] ... This government intends to solve this problem through serious dialogue."

But according to Hoshyar Ali, the head of diplomatic relations for the Kurdish opposition Gorran movement, the newly-formed government of Iraqi Prime Minister [Adel Abdul-Mahdi](#), who has so far pushed for negotiations with the Kurds, is unstable and lacks a unified block of support in parliament. A potential collapse of his cabinet could derail the current efforts to reach an agreement with Erbil and undermine the Rosneft deals, he pointed out.

"To reach permanent agreement on the issue of oil specifically - that is, that Baghdad disputes all the deals that the KRG has signed with foreign companies - you have to have a law for oil and gas in Baghdad. Then [based on] the constitution we can work which side has what rights and of course, these deals would be either recognised by Baghdad or they would be rejected," Ali told Al Jazeera.

"There is this famous saying in the Middle East: The weak sign the contracts, the strong tear them apart," he added.

Although Kurdish media outlets have [claimed](#) that Russia is mediating between Erbil and Baghdad, a number of officials and close observers have confirmed to Al Jazeera that Moscow has rather limited political sway in Iraq, including in the Kurdish region. The US and Iran remain the main power brokers, flanked by Turkey and the UK. Even though the Rosneft deals "saved" the KRG, they were not enough to upset this balance of power that the two countries that led the 2003 invasion and Iraq's two most influential neighbours had tacitly agreed on.

The limit of Russian influence in Iraq was demonstrated by the temporary deal that Erbil and Baghdad [struck](#) in mid-November 2018 to restart the pumping of oil (50,000-100,000 barrels per day) from the Kirkuk oil fields through the Kurdish pipeline to Turkey. The US had pressed for the agreement in order to put an end to a [deal](#) Baghdad had struck with Tehran, while trying to avoid the use of the Kurdish pipeline. It had agreed to ship Kirkuk oil on trucks to Iranian refiners in the north in exchange for Iranian oil being delivered to Iraq's southern ports. Full compliance with the new [set of US sanctions imposed on Iran](#), however, meant this deal had to be scrapped and Baghdad had to resume exports through the Kirkuk-Ceyhan pipeline.

According to the former Russian official, the Russians are very much aware that the status of Rosneft contracts is still in doubt. The US mediation efforts between Baghdad and Erbil got them nervous, as they feared their interests may be undermined, he said.

The fact that the KRG lost control over oil-rich Kirkuk not only slashed its exports [almost in half](#), and hence decreased the potential revenue for Rosneft from the share of the pipeline it owns, but also put under question the payment of its dues as a whole. In March 2018, Nechirvan Barzani [told](#) the media that one of the conditions for the KRG resuming the transfer of all funds from oil exports to Baghdad is the payment of tariffs to Rosneft for the use of the pipeline.

However, the November deal did not include a provision for the payment of tariffs to Rosneft. According to Delshad Shaban, the former deputy head of the oil and gas committee in the Kurdish parliament, the payment of tariffs is pending a final political deal between Erbil and Baghdad. As per its agreement with the KRG, the Russian company should be paid \$1.5 per barrel, in addition to \$1 per barrel for storage at the port and other extra costs, he told Al Jazeera.

Rosneft's deal for the five blocks in the northern part of the Kurdish region might also prove difficult to make profitable. According to Govand Sherwani, an oil expert and professor at Erbil's Cihan University, oil exploration in Iraq's Kurdish region is considered high-risk because there are just a few studies available of the area and there is no guarantee that a company investing hundreds of millions in a block would actually find oil. In fact, just before Rosneft signed this deal, major companies like Exxon-Mobil and Chevron, had started pulling out of exploration blocks that had yielded disappointing returns; between 2014 and 2016, [19 such blocks](#) had been relinquished.

Only one of the deals Rosneft concluded in 2017 seems to have started generating some revenue. The KRG started transferring oil to the Russian company just [two months](#) after the \$2.1bn deal was signed, and as per the agreement is supposed to export between 15m and 25m barrels annually for period 2017-2019. Neither Rosneft, nor the KRG have released exact numbers on how much Kurdish oil has already been shipped, but according to Sergey Aleksashenko, a former Russian deputy minister of finance, between 50 and 65 percent of the \$2.1bn has been paid back in the form of oil.

Rosneft and the KRG's ministry of natural resources could not be reached for comment.

Overall, it appears that Rosneft's investment in the Kurdish region of northern Iraq has been a risky gamble and, like in Venezuela, whether it pays off or not, will depend on how the geopolitical situation evolves. In both places, the US appears to be the main player, whose actions could determine the outcome of Rosneft's deals.

If Washington decides to escalate its campaign against Iran, Iraq is one of the main battlegrounds where the Iranians could push back. And there is nothing easier than destabilising an already unstable government and mobilising once again pro-Iranian militias in the country.

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