

# The Mediterranean is back

BY PASQUALE SALZANO

Between calls for diversification of natural gas sources and new basins being developed in the Mediterranean and North Africa, a geopolitical axis shift is occurring.

Recent political turmoil in Ukraine is reviving the long-standing European debate on energy security and competitiveness. The European Union today relies on Russia for a significant proportion of its gas imports – around 24% in 2012 at some 160 billion cubic meters, half of it passing through Ukraine – with Central Eastern and South-east Europe almost entirely dependent on this supply. If the Old Continent wants to further diversify its energy sources in the short to medium term, the Mediterranean will become increasingly relevant along with other options, such as shale gas or LNG from the United States. Significant gas resources in North Africa and in the Levantine basin, unconventional hydrocarbons and renewables, confirm that our energy future will still pass through the Mare Nostrum.

In order to fully take advantage of the regional potential, the EU should develop a more consistent foreign energy policy and effectively integrate its internal market.

Today the southern and eastern edges of the Mediterranean seem afflicted by structural instability and economic uncertainty. The security situation is precarious in several energy exporting countries and social turmoil is simmering just below the surface. However, Europeans are reliant on the Mediterranean and its rising political and economic significance. Firstly, from a strategic standpoint, Europe is exposed on its southern flank to an array of actual and potential sources of instability and risks. Secondly, the Mediterranean plays a crucial economic role as a commercial basin, contributing to a significant portion of Italy's overall export (12.8% of Italian exports flow to Middle Eastern and North African countries). Lastly, and perhaps most importantly, energy security considerations make the Mediterranean a vital playground in which a

substantial share of Europe's future strategic clout will be decided.

One of the most promising recent gas discoveries, the Levantine Basin, could potentially benefit several economies in the region. Cyprus, Lebanon, Israel and potentially also Egypt are determined to reap the economic benefit of the new energy discoveries, which could also have a positive knock-on effect with respect to Europe's energy security. The impact of such discoveries is not going to be immediate, as it will take some years for the new supply to reach consuming countries and for the geopolitical standoffs to be eased. In the medium-term, however, the Levantine basin has the potential to provide a major source of diversification for Europe.

Moreover, the Mediterranean is highly promising in the unconventional gas sector: the EIA estimates that shale gas reserves in Algeria alone could reach up to 20 trillion cubic meters, an amount sufficient to cover 40 years of European consumption.

Political instability notwithstanding, energy interdependence between the two shores of the basin is growing. If Europe is highly dependent on oil and gas from North Africa, the opposite is also true, since the region strongly relies on energy revenue to sustain political consensus and economic growth.

Today's energy markets are undergoing profound changes: starting from the shift towards emerging markets, and Asia in particular, passing through the shale gas boom that revolutionized the gas market. In

A worker at the Zarzaitine gas field in Amenas, 1,600 km southeast of Algiers.



LOUAI LABRI / REUTERS



A tanker carrying liquefied natural gas in the Mediterranean, some 10 km from the coastal Israeli city of Hadera, January 22, 2014.

Europe the gas market was also upset by the climate driver in energy policy, which has increased renewables in power generation, and the big drop in gas demand, due to the economic crisis and the use of cheap coal imported from the US. But while Europe's natural gas consumption is expected to recover, its domestic gas production will continue to shrink. Against this backdrop in production, the traditional supply paradigm based on Long Term Contracts and oil-linked prices is being increasingly replaced by volumes sold on the spot market.

Extracting mutually beneficial economic rent was in the past a viable strategy for both exporting and importing countries across the Mediterranean: Europe enjoyed security of supplies while its North African partners could benefit from stable financial revenues. However, going forward the sustainability of this dynamic is put into question. While Europe demands lower prices to continue to import gas from North Africa, a combination of domestic, social, demographic and economic pressures could seriously jeopardize stability and growth prospects, unless energy policies becomes vehicles for economic diversification. This would also involve fostering deeper regional cooperation and consistently adhering to standards of good governance.

As far as economic diversification is concerned, North African countries still rely heavily on the energy sector. For instance, almost 40% of the Algerian economy depends on gas production and export. Without diversification, Algeria, like other countries in the re-

gion, will be highly vulnerable to structural changes in global and regional energy markets.

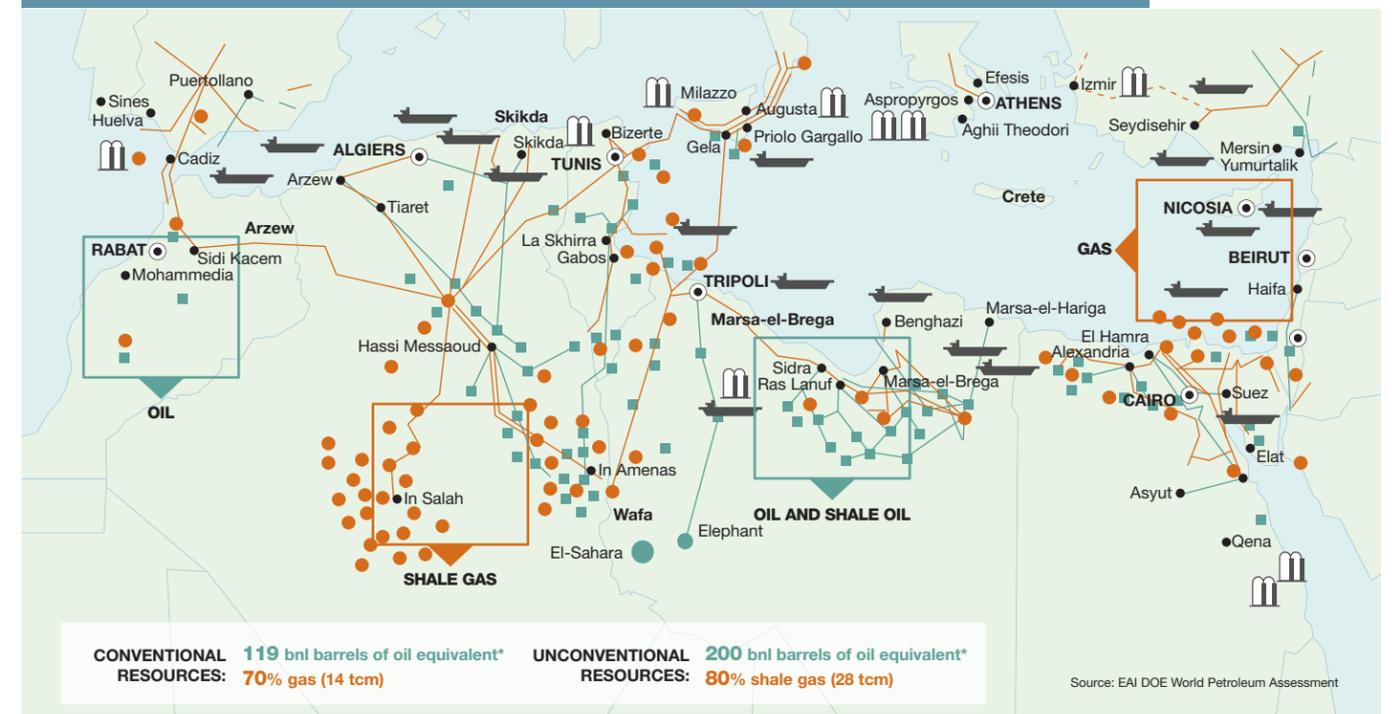
Regional cooperation – greater economic and commercial interdependence – means building political trust. There is scope for significant gains in this area: in the Arab world inter-regional trade ranges between 6% to 9%, versus, for example, 55%-66% in the EU and 11%-23% in MERCOSUR. Stronger regional cooperation would be particularly beneficial for these countries and could help mitigate the effects of the global economic downturn. The net economic benefit would then reduce the risk of social and political unrest spreading further in the region. Egypt, for instance, is today relying on regional energy supplies to sustain its very fragile economic and financial situation.

Good governance across the region is a core precondition for sustainable economic growth. In addition, enhancing transparency and regulatory stability would favor investments in North Africa. In this context, the political will and the ability of local governments to utilize resources efficiently and to the benefit of the population will be decisive factors.

What is the role of Europe against this rapidly evolving scenario? There is a set of all-encompassing priorities which should guide European decision-makers.

First of all, the EU needs to implement a more consistent external policy to provide strong political and diplomatic support to its partners in the region, to boost security cooperation and to further promote commercial and cultural links. A key challenge in this respect will be to combine energy security and com-

#### HUGE HYDROCARBON POTENTIAL IN THE MEDITERRANEAN BASIN



petitiveness, the former being a precondition for the latter. A unified European external policy directed at guaranteeing security of supply and at projecting Europe's influence in the region will greatly benefit European businesses and consumers by creating the conditions for lower energy prices.

A second key factor for boosting regional partnership in the Mediterranean basin is the consolidation of a fully integrated EU domestic energy market. Effective interconnection of electric grids and pipelines would allow member states to share and trade energy more flexibly and economically than today, mitigating the impact of supply disruption and dependence on non-EU suppliers. Obviously this ambitious goal requires significant infrastructure investment – estimated at over €1 trillion by the European Commission – and will produce effects only in the medium term. Nevertheless, the right policy trajectory has been set to strengthen EU energy security and strategic cooperation with Mediterranean producers.

Technology transfer from the EU could also prove decisive in promoting economic reforms and creating opportunities for the young North African and Middle Eastern workforce.

Energy security and competitiveness, which are today strategic priorities for the EU, will benefit from stronger cooperation among Mediterranean countries.

This will in turn further diversify European energy supplies and create a more competitive regional market. These tangible benefits will strengthen the appeal and legitimacy of the EU in a time when the foundations of the European project are called into question by a resurgent wave of nationalism, regionalism and populism.

The region offers tremendous opportunities in the energy sector, which should be at the heart of a new Mediterranean renaissance. Against a background of instability, the EU – with Italy in the front row – should continue to promote regional cooperation and project its influence across the Mare Nostrum, at the crossroads of economic growth and energy security.

The Mediterranean is regaining importance and centrality from a geo-strategic point of view. This will bring significant benefits to Italy and more generally to Europe, which has the opportunity to regain its relevance in the international scene.

PASQUALE SALZANO is a diplomat and Vice President for International Governmental Affairs for ENI.