Business Line

Date:10/12/2008 URL: http://www.thehindubusinessline.com/2008/12/10/stories /2008121050010800.htm

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IPI: A pipeline of risks

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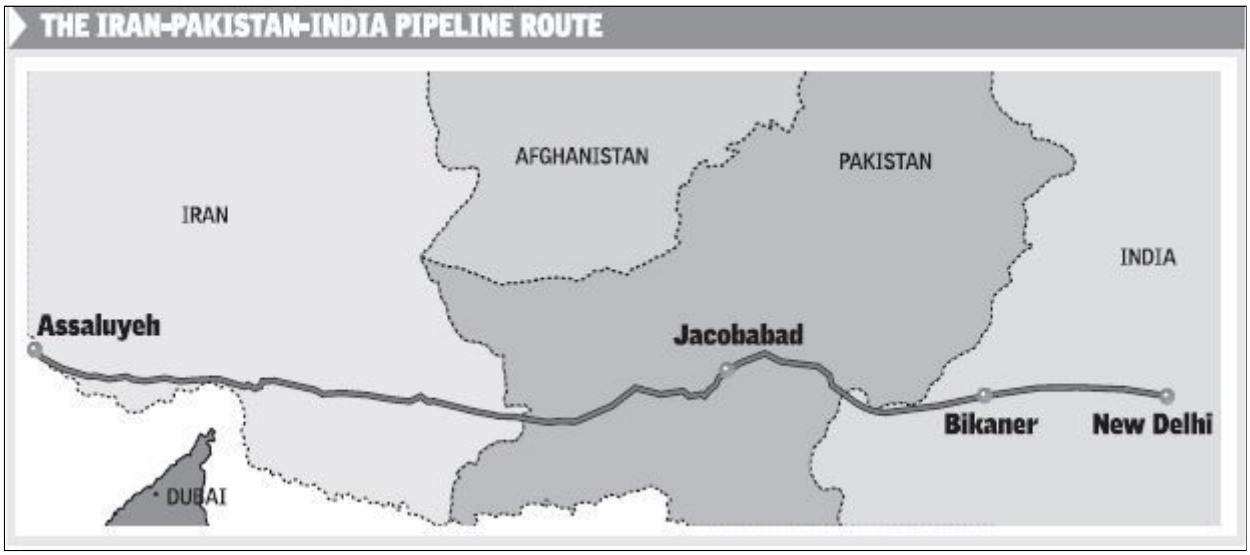
There are critical unresolved non-economic issues surrounding the IPI pipeline such as the transit through a troubled Pakistan and American opposition to the project. Given these problems, it would be reasonable to go in for an alternative, more secure system of gas supply via liquefied natural gas, says BHASKAR BALAKRISHNAN.



The Iran-Pakistan-India (IPI) gas pipeline project often called the 'peace pipeline' is seen as a "win-win-win" project for all the three countries and a confidence-building measure and stimulus for regional cooperation.

Despite these attractions, some critical unresolved non-economic issues need to be addressed, as they pose major risks for the project, which impact differently on each of the three countries. Also, this is not the only way for gas to be transported to India.

Liquefied Natural Gas (LNG) offers a viable alternative, without the risk of blockage by a hostile Pakistan. This factor assumes considerable significance in view of the Indo-Pak tensions following the involvement of Pakistani elements in the terrorist attacks in Mumbai.

The IPI project is a 2,775 km overland pipeline for carrying natural gas from Assaluyeh, Iran, near the rich South Pars gas fields (reserves 360 trillion cubic metres (tcm) on the Iran part and 900 tcm on the Qatar part) to the fast growing gas market of India, landing at Barmer, in Rajasthan, where it would link up with the domestic gas network of India.

The pipeline would cost around $7.4 billion and three-five years to build, and would carry 22 billion cubic metres (bcm) of gas per annum, to be raised further to 55 bcm per annum.

The project seems justified on purely economic grounds taking into account India's gas needs, projected to rise from 49 bcm per annum in 2006-7 to 125 bcm by 2025. Pakistan would be a transit country as well as a consumer, taking some of the gas.

Trade and transit issues

The physical security of the pipeline and compressor stations en route could be compromised by unrest in Baluchistan, the scene of an ongoing insurgency. The transit country, Pakistan, through which 1,035 km of the pipeline would run, could shut down the pipeline in the event of a conflict or tension with India. Trade and transit with Pakistan has always been a hostage to the Kashmir issue, and Pakistan has still not accorded India the most-favoured nation (MFN) status (which India extended to Pakistan in 1996, and which is the normal trade relationship between countries), and rejects normalisation of trade relations. There would be no legal recourse in case Pakistan decides to shut down the pipeline.

Pakistan has suggested that the pipeline could extend to China in case issues with India are not resolved. Iran and China have reacted positively to this suggestion. This would imply that gas supply, if cut off to India, could still be made to China, thereby increasing the risk for India.

The gas transit fee demanded by Pakistan remains unresolved, and could easily be a victim of political considerations. The transit country can squeeze out profitability from the operation of the line without the risk of closing it. Once the line is built, bargaining power rests entirely with the transit country. Single country transit oil or gas lines are extremely vulnerable to economic pressures.

Disagreement over pricing

Iran would like to lock-in India into a situation of dependence on supply, rendering it vulnerable to political pressures. Recently, there was speculation that Iran's decision to scrap the LNG deal with India was influenced by India's vote against Iran in the IAEA.

The basis for calculating the gas prices remains unresolved. Iran has asked for higher prices $8 per million BTU, while India would agree to $4 per million BTU. The five-million-tonne per year LNG supply contract between NIOC (Iran) and GAIL/BPCL (India) has also been scrapped by Iran due to disagreement over pricing, though this may be linked to other factors.

There exists no trilateral agreement that provides a comprehensive intergovernmental legal framework governing the energy cooperation regime, such as the Energy Charter Treaty (ECT) which has 51 countries in Europe as members.

The ECT strengthens the rule of law on energy issues, by creating a level-playing field of rules to be observed by all participating governments, thereby mitigating risks associated with energy-related investment and trade.

India and Iran have conflicting positions on the liability for disruption of gas supply and obligation to arrange alternative supply by means such as LNG, especially in the event of a conflict. The US remains opposed to the IPI project, which it sees as undermining economic sanctions imposed against Iran, in view of its perceived support to terrorist entities in the region.

Therefore, the IPI project is seen as a direct challenge to US strategic policy, and its advancement could negatively impact India-US relations. If, however, Iran-US tensions could be resolved, this factor would disappear.

Alternative route

Given these problems, it would be reasonable to go in for an alternative more secure system of gas supply via liquefied natural gas (LNG). This mode of supply would be more expensive than the pipeline route, due to the investments required in the supply chain, such as liquefaction plants, tankers, terminals, and re-gasification plants. However, it would offer certain advantages.

The LNG market is growing, with large consumers such as Japan, South Korea increasing imports, and supplying countries setting up LNG facilities. The technology for LNG production, storage, transport and use has matured, and is now easily accessible. Investment in LNG tankers and LNG terminals would be more economic in the expanding LNG global market. If new gas reserves are discovered in other parts of the world, these could be integrated into the global LNG market.

In the case of LNG supply, both the supplier and consumer would not necessarily be bound to each other, and a range of suppliers and consumers could be available in the rapidly growing LNG market. This would introduce some competition in pricing and delivery. There would not be any problems with transit countries, since LNG would be carried directly between the exporting and importing ports.

LNG imports

Global LNG imports are expected to go up from 155 million tonnes per annum (mmtpa) in 2006 to 400 mmtpa by 2015. Japan and South Korea alone accounted for 86 mmtpa of imports in 2006. The LNG industry is set for rapid and sustained expansion as improved technology has reduced transportation costs of isolated natural gas reserves as a liquid to consumer markets. Global LNG tanker fleet is presently around 230 and LNG production capacity is 220 mmtpa, while regasification capacity is 400 mmtpa. Qatar by itself will have the world's largest LNG facility of capacity 77 mmtpa by 2012.

India already has one LNG terminal at Dahej (5 mmtpa) and another coming up in Kochi (2.5 mmtpa). It has a contract with Qatar for import of 5 mmtpa LNG for 25 years at a very favourable price of $2.53 per million BTU. Qatar is considered a reliable long-term supplier for India.

LNG could be brought to a variety of terminals along the Indian coast, both on the West and East side. This could provide flexibility in supply covering also south, west and east India, and reduce internal distribution costs.

For these reasons, India should continue to pursue LNG import deals with exporting countries, while seeking a comprehensive Energy Charter Treaty for the South Asian region as a whole. The IPI project now remains a risky venture, and extreme caution is called for.

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