

# IPI pipeline and its implications on Pakistan

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## Abstract

*Pakistan and Iran have decided to reinvigorate the Iran-Pakistan-India (IPI) pipeline project to help solve Pakistan's ever-growing energy crisis and bilateral trade relations, with both facing a very challenging environment. For Pakistan, where oil prices are too high and coal is not a very viable option due to global warming, natural gas seems to be the best solution. The IPI pipeline, also known as the 'Peace Pipeline', is meant to deliver natural gas from Iran's Southern Pars fields to both Pakistan and India.<sup>1</sup> Pakistan and India do not have sufficient natural gas of their own to sustain their rising demands for energy due to rapidly increasing populations as well as their levels of industrialization. Iran, rich in natural gas is the most viable source in the region due to its geographical positioning. In fact, Iran has the world's second largest gas reserves after Russia; however, its development as an exporter of gas has been hindered due to its poor relations with other countries, sanctions by the US and delays in the pipeline's construction.<sup>2</sup> This paper will focus on the development of the IPI pipeline, the sanctions the US has threatened to impose on Pakistan for going ahead with this venture, and the implications this will have on the political climate of the countries involved.*

## History of the IPI pipeline

**I**n its initial phases, the IPI pipeline was the India-Iran (II) pipeline. In 1989, in New Delhi, Ali Shams Ardekani, acting Deputy Foreign Minister of Iran, and R. K. Pachauri, the Director General of the Tata Energy Research Institute (TERI) first proposed the idea of a natural gas pipeline from Iran to India.<sup>3</sup> India considered buying natural gas from Iran to be the most viable option for its increasing needs. India and Iran were planning to bypass Pakistan and make an underwater pipeline through the Persian Gulf.<sup>4</sup> Snamprogetti, an Italian firm, was asked to conduct a survey to judge the feasibility of having a 3000m deep-sea pipeline to avoid Pakistan's exclusive economic zone. The results of the study, along with other factors, made India and Iran realize that a deep-sea pipeline would result in too many technical difficulties and would be an unrealistic investment.

India, willing to increase its investment, preferred that Pakistan remain uninvolved, but also wanted Iran to promise oil supplies to India if there were

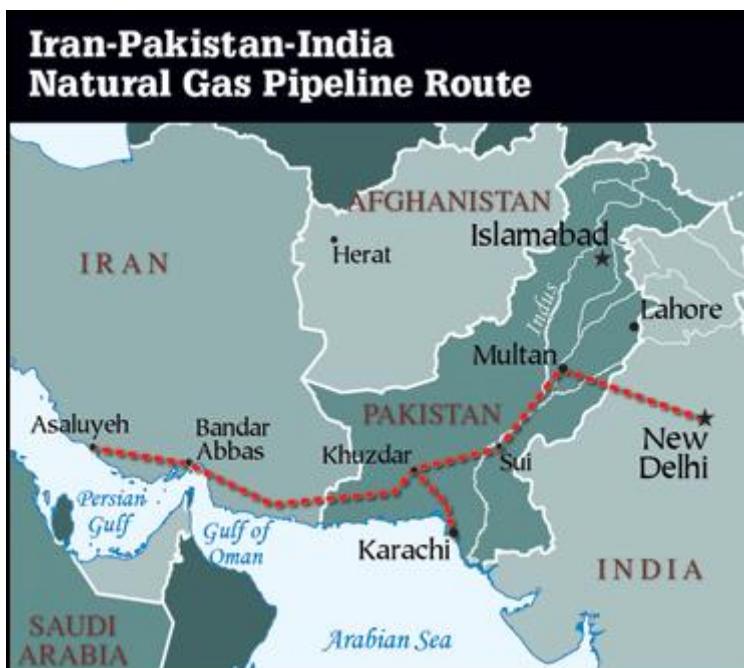
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disruptions in supplies through the pipeline. In January 2005, through bilateral meetings between Pakistan and Iran, and India and Iran, pipeline started becoming known as the IPI pipeline.<sup>5</sup> In December 2005, India agreed to partake in trilateral meetings.<sup>6</sup> Pakistan realized that the construction of the gas pipeline would be in its national interest as well and therefore promised security and stability for the pipeline.

Discussions on the IPI pipeline began as early as 1994 and the estimated cost of this 2700 km pipeline,<sup>7</sup> running from Southern Pars in Iran to Karachi and Multan in Pakistan, and further onto New Delhi in India, was \$7.5 billion.<sup>8</sup> As natural gas consumption is expected to increase exponentially, interest in the IPI pipeline has amplified, as has the construction and politics of the pipeline.

### **IPI pipeline**



### **Iran – Pakistan – India Pipeline<sup>9</sup>**

Iran has already constructed more than 900 km (out of 1100 km) of the pipeline on its territory at a cost of \$700 million,<sup>10</sup> and Pakistan has yet to start constructing its share of around 1000 km of the pipeline from the border, going along the Makran Coastal Highway and onto Nawabshah.<sup>11</sup> The pipeline will have a 42 inch diameter and will cost around \$ 1.65 billion.<sup>12</sup>

The construction of the pipeline on Pakistan's soil is believed to cost \$1.2 billion and the project will be funded through a debt-equity ratio of 70:30.

Pakistan is counting on internal and external investors for the project. It is looking at the Petronas of Malaysia and Gazprom of Russia as major international investors, and the governments of Sindh and Balochistan, Pak Petroleum, Oil and Gas Development Company, Sui Northern Gas Pipelines, among others, as domestic investors.<sup>13</sup>

The IPI pipeline would be a good way to establish economic interdependence between Iran, Pakistan and India, if India was to become a part of the venture as it had originally planned. The pipeline will lead to immense regional cooperation.

#### *Iran and the IPI pipeline*

The IPI pipeline project will boost economic development in Iran, decrease the rate of unemployment and also enhance peace in the region. Iran plans on selling 750 million cubic feet of natural gas per day to Pakistan for 25 years starting from 2014, which is when construction is scheduled to have been completed on both sides.<sup>14</sup> Iran is relatively isolated in the region due to its stressful relations with the US. The IPI pipeline would be a strategic move for Iran to link itself with other countries within the region. It will help break the tensions that may exist between regional countries.

#### *Pakistan and the IPI pipeline*

For Pakistan, there are advantages other than interdependence as well, because a pipeline from Pakistan into India would lower the cost of gas for Pakistan itself and also result in transit fees of about \$600 million to \$700 million annually.<sup>15</sup> Construction of the pipeline will also help develop the Balochistan province and create more job opportunities in Balochistan and Sindh - two provinces that feel they are neglected by the federal government of Pakistan. The pipeline is also believed to enable the generation of 5,000 megawatts of electricity for Pakistan<sup>16</sup> and this would be of utmost help as electricity shortages and power cuts are resulting in unrest.

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#### *India and the IPI pipeline*

According to the Indian Oil Ministry, the consumption of natural gas in India was 189 million standard cubic meters per day (mmscmd) in 2011 and will increase to 473 mmscmd by 2016-17.<sup>17</sup> As the domestic level of output will not

be able meet the required amount of natural gas, India will have to import 55% of its demand.<sup>18</sup> This is why the development and construction of the IPI pipeline is of benefit to all parties that were initially involved.

That being said, there are several issues such as US-Iran tensions, Pakistan-India tensions, and Chinese and Russian interests, that have caused delays in the construction of the pipeline and are currently complicating the matter. India itself backed out of the deal in 2008, almost 13 years after the conception of the pipeline deal.<sup>19</sup> After India stepped out, Pakistan turned to China to invest in the project and help fund the construction in its territory.

In order to try and convince China to become an investor again, Pakistan's Prime Minister Yousaf Raza Gilani held talks with the Chinese deputy premier as well as the Iranian vice president.<sup>20</sup> Pakistan and China have been strong allies that have agreed to stick by each other's side, maintaining sovereignty and territorial integrity 'in all circumstances.'<sup>21</sup> Therefore, Gilani's visit to China during the Boao Forum for Asia (BFA) brought back hope for China's involvement in the IPI pipeline.<sup>22</sup>

**Pakistan says that it is willing to continue with the IPI project, despite India and China backing out, and immense US pressure. This is since the project is of great importance in order to deal with Pakistan's growing energy crisis.**

At this point in time, American threats of the new sanctions on Iran have negative ramifications for Pakistan, but going ahead with the pipeline project seems to be of utmost concern. Pakistan says that it is willing to continue with the IPI project, despite India and China backing out, and immense US pressure. This is since the project is of great importance in order to deal with Pakistan's growing energy crisis.

## **US sanctions**

US sanctions on Iran date back to November 1979 when they came in response to the hostage crisis in the US Embassy in Tehran. Since then, the US has been imposing sanctions for various reasons at different times. In 1995, President Bill Clinton imposed oil and trade sanctions in response to Iran's funding of "terrorism" in the Middle East. In the following year, Clinton strengthened the sanctions by announcing penalties against any firm investing \$40 million or more per year in oil and gas projects in Iran and Libya.<sup>23</sup>

March 2000 marked a decrease in tensions between Iran and the US, with US Secretary of State Madeleine Albright announcing the lifting of sanctions on Iranian exports. In September 2000, Albright met Iranian Foreign Minister Kamal Karrazi at the UN in New York, reestablishing diplomatic ties. Tensions

increased again when the US said it believed that Iran was involved in the bombing of an American military base in Saudi Arabia in 1996.<sup>24</sup>

Today, the main aim of US sanctions on Iran is to discourage Iran from developing its nuclear program. In December 2002, the US, publishing satellite images of nuclear plants in Natanz and Arak, claimed that Iran was secretly developing nuclear weapons. The International Atomic Energy Agency (IAEA) began inspections of Iran, which maintained that these nuclear plants would be used for energy purposes. The UN Security Council imposed sanctions on Iran in December 2006 for its uranium enrichment program.<sup>25</sup>

The next set of US sanctions on Iran was imposed in October 2007, with the US claiming Iranian involvement in terrorism and alleged that it was pursuing nuclear activities. These new sanctions focused on crippling Iran's three state-owned banks and the finances of Iran's Islamic Revolution Guards Corps for their involvement in nuclear and ballistic missile programs.<sup>26</sup> In July 2008, sanctions attacked engineering and construction companies as well as companies that were supposedly providing technological help for the development of nuclear and missile programs. Since then, the US has been imposing sanctions on banks, construction companies, shipping companies, and individuals involved in the Iranian uranium enrichment, nuclear and ballistic missile programs.<sup>27</sup>

**The US is urging Pakistan not to buy natural gas from Iran and wants to play an active role in decreasing global dependence on Iran.**

**This is why the US is encouraging Pakistan to import gas from Turkmenistan and invest in the Turkmenistan-Afghanistan-Pakistan-India (TAPI) gas pipeline**

Earlier on, Richard Holbrooke, the then special representative for Afghanistan and Pakistan (2009-2010), warned Pakistan not to "over-commit" to the pipeline project as new sanctions were being legislated towards Iran, which may have an effect on Pakistan too.<sup>28</sup> In response, Pakistan's Foreign Minister Shah Mehmood Qureshi (2008-2011) said that Pakistan will go ahead with the pipeline despite the risk of sanctions. He noted that sanctions would not affect Pakistan as it is a bilateral agreement between two sovereign states.<sup>29</sup> Qureshi and current Foreign Minister Hina Rabbani Khar have always maintained that Pakistan would respect any sanctions that the UN imposes on Iran or any other country and that the pipeline would not be affected.<sup>30</sup> Even Prime Minister Yousaf Raza Gilani said that Pakistan will continue working with Iran despite sanctions.

There is continued tension between the US and Iran as President Obama put new sanctions on Iran in the beginning of January 2012.<sup>31</sup> These sanctions blocked Iran's access to the world financial system. The US is urging Pakistan

not to buy natural gas from Iran and wants to play an active role in decreasing global dependence on Iran.<sup>32</sup> This is why the US is encouraging Pakistan to import gas from Turkmenistan and invest in the Turkmenistan-Afghanistan-Pakistan-India (TAPI) gas pipeline. Pakistan does not want to risk waiting for the construction of the TAPI pipeline as it believes that there will be further delays due to the problems in Afghanistan.<sup>33</sup> Also, the IPI pipeline is promising four times cheaper energy than TAPI.<sup>34</sup> Instead of letting regional security interests and market forces pave the way when it comes to the pipeline, the US is making a conscious effort to dissuade Pakistan from going ahead with the venture.

*Pakistan's reaction to US sanctions on Iran*

The latest sanctions imposed by the US may cause problems for Pakistan as the US has declared that these will focus on targeting Iran's crude oil sector as well as the financial institutions of any country doing business with Iran's Central Bank. This has disappointed Pakistan but not discouraged it from going ahead with the pipeline deal with Iran. Foreign Minister Khar has announced that Pakistan will utilize all its options, including Iran, to meet its energy shortages.<sup>35</sup> The US has imposed these new sanctions to hinder nuclear development in Iran. However, Iran's self resilient economy continues to remain relatively stable. Attacking its Central Bank will have an effect on oil trade, which seems to be the only possible way to hit its economy hard. Gary Hufbauer, a former US Treasury official and a Fellow at the Peterson Institute of International Economics, ranks the current case of sanctions against Iran as one of the toughest international sanctions of the past 50 years. That said, harsher sanctions have been imposed on Iraq, North Korea and Cuba in relation to nuclear ambitions.<sup>36</sup>

*Reaction of other countries to the US sanctions on Iran*

President Obama has discussed potential sanctions on countries that continue to buy oil from Iran.<sup>37</sup> This is because the Obama administration wants to make the Iranian Central Bank as weak as possible so that it does not have enough funds to develop nuclear projects. India, a country with growing energy needs, imports 12 percent of its crude oil from Iran. India and Iran have set a \$25 billion trade target for 2015.<sup>38</sup> Therefore, to maintain its economic ties, India is not interested in abiding by unilateral sanctions but has promised to abide by sanctions imposed by the UN. In March 2012, a 70-member Indian trade delegation made a visit to Iran to discuss further commercial opportunities between the two countries. India sees Iran as a big market for exporting textiles, rice, wheat, tea, pharmaceuticals, engineering and infrastructure projects.<sup>39</sup>

Although the sanctions are stringent, the US has exempted 10 European countries (Belgium, Britain, the Czech Republic, France, Germany, Greece, Italy, the Netherlands, Poland and Spain) as well as Japan from the warning of

sanctions because they have significantly decreased their oil imports from Iran.<sup>40</sup> A three-month notice warning has been sent out to other countries to decrease or halt their oil purchasing from Iran before sanctions are placed on them as well.<sup>41</sup> This is because the sanctions are to take effect on June 28, 2012.<sup>42</sup> By law, Obama can exempt countries from these sanctions if he feels that they have “significantly reduced” their crude oil imports from Iran. Exemptions are applicable for 180 days, after which they can be renewed every six months.<sup>43</sup>

Currently, the sanctions are of utmost worry to China, India, Turkey, South Africa and South Korea as these countries have not been exempted from sanctions and are major avenues of Iranian oil export.<sup>44</sup> China and India are Iran’s topmost crude oil importers, while South Korea and Turkey are strong allies of the US.

Pakistan was relying on China to help by investing in the construction of the IPI pipeline, but the latest sanctions have had an impact on China’s decision. China is now no longer interested in investing in the pipeline and the Industrial and Commercial Bank of China has withdrawn its deal to invest \$1.6 billion for construction of the Pakistani section.<sup>45</sup> Although one would consider this to be a setback for Pakistan, Foreign Minister Khar has confirmed that Pakistan is still willing to go ahead with the project as other sources of funding will be available for this “viable option.”<sup>46</sup>

The US, aware of Pakistan’s growing energy crisis, has promised to make giving aid to Pakistan’s energy sector one of its top priorities when it comes to helping in development.<sup>47</sup> It continuously encourages Pakistan to look into the TAPI pipeline. Saudi Arabia has offered Pakistan a loan to help it out of its current financial and energy crises. Pakistan and Saudi Arabia are to discuss the details of the offer in a Pak-Saudi ministerial meeting in the near future.<sup>48</sup>

### **Pakistan and the IPI pipeline**

Pakistan, concerned by the developments, hired experts to study the sanctions imposed on Iran. After a discussion with Prime Minister Yusuf Raza Gilani, it was concluded that Russian and Chinese support would be of extreme help if Pakistan was to continue with the pipeline project, as it plans on doing so, and that Russian energy giant, Gazprom should be approached.<sup>49</sup>

The IPI pipeline can also boost Pakistan’s relations with India and China if the two plan to become a part of the project again. If New Delhi gets back into the deal, it can help improve relations of the entire region and also help resolve the Pakistan-India water dispute due to the interdependence of the transportation of resources.<sup>50</sup>

Pakistan views the IPI pipeline as more of an economic issue, while the US sees it as a political concern. Pakistan should keep in mind that sanctions on Iran are not linked with the Kerry Lugar Bill or the IPI pipeline per se. The sanctions will be imposed at the discretion of the US. Pakistan should also keep in mind that Turkey, an important NATO ally of the US, already has a functioning pipeline with Iran and no sanctions have been applied on the country as yet.<sup>51</sup>

Most Pakistani political leaders have voiced their opinions as pro-IPI pipeline, and feel that Pakistan should look into national interests and not succumb to pressure from the US. The governor of Balochistan, Nawab Zulfiqar Ali Magsi, openly spoke out against the pressure from the West and expressed his interest in the pipeline which will be constructed in the Balochistan province.<sup>52</sup> The Baloch people are hoping that the pipeline will bring economic prosperity and stability in the region.

There are still other concerns aside from the US sanctions that Pakistan needs to be aware of. Pakistan should make sure that the price of gas continues to remain economically viable to the country. Although the price of gas that Iran is offering is fairly high, the IPI pipeline is still beneficial for Pakistan as it will save the energy-deprived country \$652 million and \$1.17 billion annually.<sup>53</sup> Pakistan should consider its self interest and act in a way that will be beneficial to the country in the long run.

If Pakistan continues to go ahead with the deal, it will improve its bilateral ties with Iran, a neighboring country. Enhancing economic ties will help the two countries to overcome their differences over the Balochistan province, the situation in Afghanistan and the sectarian issue of Shias and Sunnis. It will also help develop a relationship of mutual trust fostered by a common goal.

## **Conclusion**

The IPI pipeline is of great regional importance, which is why decisions made regarding it have implications on countries other than just Iran, Pakistan and India. Russia and China, for instance, will also be affected. Sanctions on Iran by the US, especially on its Central Bank, are of utmost concern. The European Union is supportive of the new sanctions, while countries such as Russia, China and India feel that having negotiations and meaningful dialogue with Iran would be a better option.<sup>54</sup> It is believed that if the US does not impose such sanctions on Pakistan, its ally in the 'War on Terror,' it will be a great confidence building measure (CBM).<sup>55</sup>

Whether Pakistan will actually go ahead with the project or not is something that lacks certainty in itself. The new sanctions have scared off some countries, while others seem to be confused about their decisions. India, having backed out

of the IPI pipeline project after securing nuclear energy assurances from the US, is now reconsidering its decision again due to its ever increasing energy needs. This may compel it to look at the IPI pipeline especially considering President Asif Ali Zardari's recent visit to India that was highlighted due to the increased goodwill it brought.

Termed as a "win-win proposition for Iran, Pakistan and India" by Pakistan's former Prime Minister Shaukat Aziz,<sup>56</sup> the IPI pipeline would be a great way for Pakistan and India to deal with their acute shortage of natural gas. There are economic and development gains for all three countries involved.

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