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Russia Put All of Its Eggs in Chavez's Basket

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The death of Venezuelan President Hugo Chavez has forced Russian leaders to worry about the fate of billions of dollars in contracts it holds there, primarily in the oil and weapons sectors.

Moscow's trade and economic relations with Caracas were typical of those it has established with similar, autocratic regimes elsewhere, that is, they hinged almost completely on relations with one person at the top. The problem, of course, is that relations are highly vulnerable when the leader is disposed or dies.

During Chavez's reign, he nationalized hundreds of private companies, including foreign firms. He kicked U.S. oil companies out of Venezuela overnight after he concluded that Washington was plotting against him. He expelled them without any compensation and in violation of contractual obligations. But Chavez was above the law.

Chavez was personally behind all the major projects with Russia in energy, transportation,

weapons purchases and banking. For example, military and technical cooperation with Russia to rearm the Venezuelan army took off in full force in 2005-06 after the U.S. refused to supply the country's military with spare parts. Moscow signed military and technical contracts with Caracas totaling $11 billion, of which $4 billion is financed with Russian credit. As of today, $6 billion in contracts have been fulfilled.

Now that Chavez is gone, the one factor that has always worked against Russia — its lack of technological innovation — will play an even larger role in Venezuela turning to China instead of Russia for military and technical cooperation. What's more, with deepening economic difficulties and a resultant currency shortage, Venezuela might have trouble paying off its large debt to Russia.

Russian oil companies should expect even more serious problems. State-owned Rosneft has already signed a contract with the Venezuelan state-owned PDVSA oil company to develop the Carabobo-2 heavy oil field in the Orinoco River basin as part of a joint venture in which Rosneft holds a 40 percent stake. Rosneft is also part of a consortium with LUKoil, TNK-BP and Gazprom Neft that is working on the Khunin-6 project, also in the Orinoco River basin. Those companies were required to pay the Venezuelan government $1 billion each just for the right to join the projects, and according to various estimates, their additional combined investment over many years will reach $40 billion.

It seems that there is more politics than profit behind these projects for two reasons. First, it is strange for Russian oil companies to invest tens of billions of dollars in a country with an unpredictable future, especially when similar projects at home are terribly underfunded. Second, it has always been extremely difficult to work in Venezuela, and all the more so now that Chavez, Moscow's loyal friend and ally, has died. Chavez did not leave the country in the best condition. He doubled the size of the bureaucracy, which brought corruption and inefficiency to such high levels that the country was on the brink of collapse. The country's infrastructure is in ruins, and foreign companies might be forced one way or another to finance expensive infrastructure programs from their profits.

Notably, Rosneft head Igor Sechin, who attended Chavez's funeral last week, spoke with acting President Nicolas Maduro regarding the delicate issue of that country's unfulfilled contractual obligations to other Russian companies, including RusHydro. Russia might not have enough political and economic leverage to influence the behavior of the new Venezuelan leadership, whichever happens to emerge. Of course, Moscow prefers Chavez's hand-picked successor, Maduro, who is favored to win the election. But under the pressure of mounting economic problems, Maduro might take a more balanced and pragmatic approach, including subduing anti-U.S. rhetoric and turning to the U.S. and China for investment and large contracts.

Russian-Venezuelan relations could be complicated even further if opposition leader Henrique Capriles Radonski wins the presidential election on April 14. Even if Maduro wins, relations with Moscow will probably deteriorate as well. Russian-Venezuelan relations are fundamentally fragile. Compare them to the long and well-developed relationship between Cuba and Venezuela. Cuba has sent about 40,000 workers to Venezuela, including more than 5,000 specialists in sports, health care and education, and has acted as the initiator and co-participant in many important social projects. Simply expelling such a partner like Cuba

would be difficult, even if a right-wing leader were to come to power, because that relationship is deeply woven into the fabric of Venezuela's economic and political life. But since the collapse of the Soviet Union, Russia has showed little enthusiasm for large-scale programs designed to build a broad base in other countries.

Notably, China has taken this broad approach toward building relations with developing states like Venezuela, and as a result, Beijing enjoys a steadily growing economic presence in those countries, even when ruling regimes change. In contrast, Moscow continues to focus its bilateral relations on top leaders and their small inner circles in these countries. This might be fine as long as they remains in power, but as soon as they are gone, Russia risks losing political capital and billions of dollars in contracts.

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