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# THE RUSSIAN ENERGY MARKET

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Russia, as we are all aware, is the second-largest producer of gas and third-largest oil producer in the world. It is also one of the world's top exporters of coal and wheat, along with being a leading producer of other important resources, such as palladium and ammonium nitrate.<sup>1</sup> The largest known natural gas reserves of any state on earth, the second-largest coal reserves, eighth-largest oil reserves and one of the largest exporters of hydrocarbons indeed, makes Russia mighty rich in energy resources.<sup>2</sup>

In totality, it comes to 32% of the world's natural gas reserves, 12% of oil reserves, 10% of the coal reserves and 8% of uranium reserves.<sup>3</sup> This brief statistical data makes it clear that the energy reserves market is of key strategic significance for Russia in multi-fold ways and means. Russia holds a very large share of natural gas reserves as a primary source of energy, much higher than the rest of the world. These reserves are mainly owned and operated by the well-known Russian monopoly company, Gazprom, which alone produces 94% of Russia's natural gas reserves. Gazprom alone carries 25% of the world's well-known gas reserves over its shoulders and exports 16% of global production.<sup>4</sup> If we study the European region specifically, then a major amount of gas consumption takes place through the Ukraine gas transmission system, which is Soyuz, Brotherhood and the Belarus gas pipeline which follows the trail of Yamal to Europe. The main importers of the Russian natural gas are the European Union member states, the Commonwealth of Independent States (CIS), Germany, Ukraine, Belarus, Italy, Turkey, France and Hungary.

Now coming down to the oil business, Russia produces the largest amount of oil in all forms to the non-OPEC states, and the second-largest globally after Saudi Arabia, which too is overtaken at times. The Russian oil produce in all its forms is also mainly exported primarily to the European states only. As per reports, Russia is also the main transit country of Kazakhstan when it comes to oil. Some of the largest and most well-known Russian oil companies are Rosneft, Lukoil, TNK-BP, Surgutneftegaz, Gazprom Neft and Tatneft to name a few. Though all the companies mentioned hold a major share in the Russian oil market, most of the oil trunk pipelines are owned and operated by the state-owned monopoly company,

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<sup>1</sup> Lu, C., Gramer, R. and Hagos, S. (2022). "What would a Russian Invasion mean for Energy Markets", *Foreign policy*, February 23.

<sup>2</sup> Neely, J. and Blair, E. (2022). "Sanctions on Russian Oil and Gas will Hammer Global Market", *Reuters*, March 23.

<sup>3</sup> Malik, H. F. (2022). "The world's biggest oil trader says the energy market reflects less concern about a supply crunch from the Russia/Ukraine war", *Insider*, April 4.

<sup>4</sup> Neely, J. and Blair, E. (2022). "Sanctions on Russian Oil and Gas will Hammer Global Market", *Reuters*, March 23.

Transneft. And the oil products pipelines are owned and operated by its subsidiary Transnefteproduct. At present, the East Siberian-Pacific Ocean oil pipeline is being built by Transneft. This in turn would make the Russian oil in all its form available and accessible to the Asian-Pacific markets, namely China, Japan and Korea to name a few.<sup>5</sup>

Changes have been unanticipated in the global energy market ever since the Soviet Union collapsed in the early twentieth century. The hydrocarbon reserves in Russia that were hushed behind the walls, became accessible to the world since then. Russia then became a well-founded energy supplier to the world and also, the world's largest natural gas exporter. A piece of statistical evidence states that of the 98 million barrels of crude oil that moves globally, 7.5 of it belongs to Russia. But this was before the giant land attacked Ukraine.<sup>6</sup> Now, the global energy market is rigid and stiff.

## Present Impact

Globally, the states that have been less dependent on the Russian energy market like the US, Japan and South Korea have either stopped or cut Russian oil deals. The United Kingdom, meets 8% of its total demand from Russian oil, but ever since the invasion took place, it has decided to end all its energy needs with Russia.<sup>7</sup> Eurozone has been demanding a complete ban on Russian energy for a long time. The effects of the sanctions have started to gain notice, it is getting hard to find buyers for Russian oil shiploads and as per data, the oil loading at Russian docks too had fallen by 2 million barrels per day.

The Russian Deputy Prime Minister, Alexander Novak made a statement saying that the global energy markets are sure to collapse in case sanctions are imposed on Russian oil and gas.<sup>8</sup> Ever since the conflict began in East Europe, the European Union wishes to expand sanctions on Putin's land, which has started to include hydrocarbons. He even mentioned that a ban on the Nord Stream 2 gas pipeline from Russia to Germany would fuel up inflation. The Nord Stream 2 gas pipeline that was designed to double the flow of Russian gas heading directly to Germany.

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<sup>5</sup> Ibid.

<sup>6</sup> Lu, C., Gramer, R. and Hagos, S. (2022). "What would a Russian Invasion mean for Energy Markets", *Foreign policy*, February 23.

<sup>7</sup> Malik, H. F. (2022). "The world's biggest oil trader says the energy market reflects less concern about a supply crunch from the Russia/Ukraine war", *Insider*, April 4.

<sup>8</sup> Neely, J. and Blair, E. (2022). "Sanctions on Russian Oil and Gas will Hammer Global Market", *Reuters*, March 23.

Matthias Warnig happens to be the CEO of the Nord Stream 2 gas pipeline company, although registered in Switzerland, it is a wholly-owned subsidiary of Russian state gas giant Gazprom. Talking of Warnig, he is a German citizen, a former agent of the East German secret police and is said to maintain close contacts with the Kremlin. Meanwhile, Biden has decided to look for Russian alternatives already. This decision come days after the German Chancellor Olaf Scholz announced freezing the certification of the pipeline. Halting the certification of the pipeline has been a major hit for Russia, especially financially, because of the heavy investments made by the country. Reportedly, the Dutch front-month gas agreement has also hit a record high ever since the invasion began towards the end of February this year.<sup>9</sup>

In an article for *The Economist*, the American energy expert Daniel Yergin predicted that Russia is likely to become a “reduced energy power” after the invasion. “Although it remains a necessary supplier for now, its role is certain to diminish.”<sup>10</sup> The world has been fighting inflation for over two years now. It wouldn’t be a sound decision to ban supplies from a state that produces more than half of the global oil and related products. The oil prices have already skyrocketed to an eight-year high and gas prices too are at a 40% high. The International Energy Agency (IEA) had also once called it impossible to replace the raw materials and goods Russia provides in such a short period without shortages or inflation.<sup>11</sup>

There is also a dilemma that the stock markets have started to experience, which is whether to invest in the Russian energy market or not. Things are even worse for traders and investors who have already invested in the market and have started to run into a loss.

## US Response to the Crisis

Moscow “could make the decision to try to change calculations in the West, use commodities as a form of hybrid warfare by essentially curtailing exports, making sure Ukraine cannot export, and then you have a big inflationary spiral coming,” said a government official of Russia. Europe has always had a heavy dependence on its eastern neighbour, with Russia supplying 40% of natural gas to the whole of Europe. American and East European leaders

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<sup>9</sup> Malik, H. F. (2022). “The world’s biggest oil trader says the energy market reflects less concern about a supply crunch from the Russia/Ukraine war”, *Insider*, April 4.

<sup>10</sup> *Ibid*.

<sup>11</sup> Neely, J. and Blair, E. (2022). “Sanctions on Russian Oil and Gas will Hammer Global Market”, *Reuters*, March 23.

have stated it clearly that the Kremlin won't think twice before wielding its gas supplies as a geo-strategic tool in order to fuel the economic warfare. This is because Russia has a history of cutting its supply chains to Ukraine due to price feuds by way of reducing or removing exports. "Europeans are worried that military action in Ukraine could impact supply flows," Chausovsky said. "We're at a stage where that could happen at any moment."<sup>12</sup>

The announcement of various sanctions on Russia imposed by the US President, Joe Biden has indeed added more salt to the wound. This is because many company officials and trade and finance professionals have been blocked from being a part of, or from even participating in, any kind of US-related trade in one of the financial institutions.

The Nord 2 pipeline system as we know, already has been halted by the German government due to the invasion, but experts suggest that the decision may not affect the current gas supply chain of Russia but will be a hard hit for all the traders and investors who contributed in it.

Coming to oil, European energy companies are presently embroiled in the Russian energy market. European companies such as BP, Royal Dutch Shell, and Total Energies have for long been a part of the multibillion-dollar oil exploration and production projects in collaboration with Russia. "Second- and third-order sanctions could make it really complicated for international oil companies to operate in Russia," Croft said.<sup>13</sup>

The Russian invasion and the following sanctions have started to see consequences even in the banking industry. Some major Russian banks like Sberbank, VTB Bank, and Gazprombank etc., that invested in the Russian energy market have come to be on the target list of Western sanctions.

Recently, officials from the Biden administration have started exploring alternatives to the Russian energy market in order to reduce the shock on Europe. A few suggestions are to start shipping U.S. liquefied natural gas (LNG) to Europe. If not, then push Qatar, which is also one of the top gas exporters globally, to shift its gas pipelines and start supplying more gas to Europe. But even then, experts have suggested it on various platforms that it won't be possible for just one state to replace the Russian energy market, and that too all of a sudden. In one of the press conferences, the Qatari government said "it would be 'almost impossible' for any

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<sup>12</sup> Ibid.

<sup>13</sup> Lu, C., Gramer, R. and Hagos, S. (2022). "What would a Russian Invasion mean for Energy Markets", *Foreign policy*, February 23.

country to fully substitute Russian gas to Europe, with most LNG already tied down in existing contracts.”<sup>14</sup> According to Saad al-Kaabi, the Qatari energy minister, “only 10 to 15 percent of the Qatari supply could feasibly be diverted to Europe.” As long as this dependence on Russian gas continues and the conflict escalates, experts warn that Europe will bear the brunt of the supply crunch, even as it affects commodities globally. “The Europeans have more to lose than we do from either sanctions on the energy sector or Russia’s retaliation to sanctions,” said Samantha Gross, director of the Energy Security and Climate Initiative at the Brookings Institution. “Over the shorter term, it’s really painful for Europe.”<sup>15</sup>

## India’s Stand in the New War

*NewsOnAir* reports that as the Russia-Ukraine crisis ensues, India had sharply hit back at its critics for ‘campaigning’ against India on Russian oil imports.<sup>16</sup>

Addressing the ‘First India-UK Strategic Future Forum’ along with visiting UK Foreign Secretary Liz Truss, EAM Dr. S Jaishankar quoted a report that said that it was Europe that was buying more oil from Russia.

“We have seen for some time, what looks like a campaign on this issue. I was reading a report. Europe has bought 15% of more oil and gas from Russia than it did a month before. If you look at the major buyers of oil and gas from Russia, I think you will find most of them are in Europe.”<sup>17</sup>

This statement was perhaps a response by the External Affairs Minister, Dr. S Jaishankar to the US Deputy National Security Advisor, Daleep Singh, who during his visit to India stated that Washington didn’t want to see any kind of rapid acceleration in Russian imports to India.

Dr. S Jaishankar had further pointed out that, India got the bulk of its energy supplies from the middle east, about 8% of it from the United States and in the past perhaps less than 1% from Russia. He said, “when the oil prices are high it is natural for countries to go out in the market and look for what are ‘good deals’ for their people.”

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<sup>14</sup> Ibid.

<sup>15</sup> Ibid.

<sup>16</sup> News On Air, (2022), “The Present and Future of Russian Oil”, *PBNS*, March 4.

<sup>17</sup> Ibid.

“But I am pretty sure if we wait two or three months and actually look at who are the big buyers of Russian oil and gas, I suspect the list would not be too different from what it used to be and I suspect we won’t be in top 10 on that list,” the EAM added.

When asked about the UK’s response to the scenario, the UK Foreign Secretary said that: “

*Europe prioritizes cheap gas, cheap goods while overlooking long term security. We didn’t do enough when Putin invaded Crimea. We did not do enough to involve ourselves in the Minsk agreements and we are now seeing the results of that. Necessarily dependence on energy on technology takes time to address, but the UK is now removing China’s Huawei from its telecom’s networks and also reducing and eliminating our dependence on Russian oil and gas”.*<sup>18</sup>

## Future Implications

The most pragmatic approach right now would be to shift focus to Europe. Before the winters set in, the European states need to pile up oil and natural gas. But the drawback here is that, most of the refineries in Europe are owned and operated by the Druzhba oil pipeline system. If this pipeline also shuts down due to the sanctions, then its highly likely that the refineries might have to be got by the sea. But the oil import terminals may not have the ability to manage the supplementary shipments all of a sudden. The alternative to this could be to import it from the middle East or the US which will turn out to be even more expensive.

According to Daniel Yergin, the Russian energy supply will come down on its own in a few years.<sup>19</sup> In the meantime, the European states will start building on renewable energy capacity, France specifically will start building on nuclear plants. The sale of electric vehicles will shoot up. But demand for coal and its prices may shoot up. With these changes happening, Russia might decide to shift its pipelines to Asia towards China and India demand 20% and 3% of Russian energy share respectively.<sup>20</sup> We even see these Asian superpower states have started to pile up Russian energy at the best prices available these days. Even after banning the Russian crude oil, there are chances that Japan might import Russian oil from the Sakhalin-I project

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<sup>18</sup> Ibid.

<sup>19</sup> Ibid.

<sup>20</sup> Gravitas, (2022), “Why Europe’s energy supply depends on Russia?” How Russia can cripple Europe? March 23.

where Sodeco, a Japanese company has a stake. This doesn't end here, shifting petroleum exports from Europe to Asia would also make Russia face its own challenges. Transport and communication arrangements, deliberations and negotiations over deals involving the USD won't be less of a burden. Indeed, in the near future, the global oil streams are likely to change direction. However, if the Ukraine conflict continues for long then, the Western investors could withdraw their investments from the Russian energy market and sanctions would prevent new investors from investing and taking over the business due to the fear of further sanctions, loss or collapse. Realistically, until and unless Iranian and Venezuelan barrels don't start to flow through their respective pipelines which will take time, effort, planning and most importantly, investors for funding, the oil will continue to be on a boil. So, expect oil to remain on the boil, unless Iranian and Venezuelan barrels start flowing, but that does not look imminent either. Until then, Russia will rule the roost in the energy sector for a few years. The severity of the crisis has not been taken seriously according to some experts, that is, prices aren't as high as they should have been given the immediate risk of war.

## Conclusion

If we were to discuss the impact of the Russian invasion on Ukraine in its entirety and not just the Russian energy market, it won't be wrong to state that the real issues are yet to come especially for developing countries like India and many more. The financial, logistics trade, transport and communication spheres have been severely damaged & the markets too, are in turmoil. All these things will have issues for the rest of the world in multi-fold ways. Whether further sanctions will be placed does not determine in any way if the entire world will actually suffer or not but, a period of energy crisis is bound to occur in a few months from now.

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