

## Russia's gas discount for Ukraine is in Gazprom's interests

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On 8 October, President Vladimir Putin announced that Russia has provided economic assistance to Ukraine in the form of gas sales at a significant discount to make up the winter stock in Ukraine's underground gas storage reservoirs (UGS). The gas price after the discount was US\$260, compared to the current price of about US\$400 per 1000 m<sup>3</sup>. The Russian president stressed that Russia has once again offered Kyiv help in the past few weeks (in late September Moscow made a US\$750 million loan), despite 'heated debates' over Ukraine's possible signing of an Association Agreement with the EU. According to Russian media reports, the transaction relates to the supply of 5 bcm to the Ostchem gas company, owned by the Ukrainian oligarch Dmytro Firtash, which will be deducted from the company's planned amount for import from Russia next year (8 bcm). Ostchem is the largest private importer of gas into Ukraine; in September Firtash announced that he plans to increase its gas stocks in the Ukrainian UGS from nearly 1.5 million bcm to 6-6.5 bcm by the end of November. A delivery of 5 bcm of gas, with a discount of more than 30% off the price given in the original contract, would cost Gazprom approximately US\$700 million. According to the Russian media, the company has guaranteed itself the right to purchase the gas allotted to Ostchem at a preferential price in future, for example, if it is not used during the winter.

### Commentary

- Ukraine's gas reservoirs are an important part of the system of Russian gas transit to Europe; inter alia for example, they are used to bolster supplies if gas consumption in Europe rises. Russia has for months demanded that Ukraine increase its reserve holdings in the PMG to around 20 bcm. However, Kyiv has replied that about 16 bcm is enough to maintain current transit levels (the UGS held about 15 bcm at the end of September), and if Gazprom believes otherwise, it should itself finance the purchase of the difference (this contrasts with the practice of previous years, when Naftogaz financed the purchase of this amount of gas). The new deal with Ostchem will in practice allay concerns about the stability of gas supplies for European consumers in the event of a cold winter.
- The gas discount, which Russia has presented as 'assistance to Ukraine', primarily benefits Gazprom, as it can thus guarantee the stability of its contracts with its European customers, while also avoiding the high costs for storing gas in Ukraine's UGS (this summer, Kiev raised the charge for this service by 4.4 times). Ostchem, owned by Dmytro Firtash, a long-time business partner for Gazprom, will also benefit, as it can now make

big profits by selling the gas surplus after the winter season. Meanwhile, Ukraine will benefit by spending less foreign currency on importing Russian gas. However, the gas rebate will not improve Naftogaz's very difficult financial situation.

- Moscow has used the gas deal with Ostchem and its bank loan to demonstrate the benefits that Ukraine can obtain thanks to bilateral cooperation, and which contrast vividly with the losses which it will allegedly incur if it signs the Association Agreement. By changing its tactics and rhetoric towards Ukraine, Moscow is still trying to influence Kyiv's decision regarding its agreement with the EU, including by weakening the arguments of Ukrainian supporters of European integration.