

Russia's response to Western oil sanctions

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On 27 December, Vladimir Putin signed a decree on measures to respond to price cap imposed by Western countries on Russian oil and petroleum products (see '[Price cap on Russian oil: EU eases sanctions on Russia](#)'). The document prohibits the supply of these products to foreign legal and natural persons if the supplies were to be made on the basis of contracts providing for the use – directly or indirectly – of the price ceiling. The prohibition applies to all stages of delivery, not excluding delivery to the final customer. For crude oil, the provision will enter into force on 1 February 2023 and will apply until 1 July 2023. As for petroleum products, on the other hand, the implementation date is to be set by the government. At the same time, the document stipulates that the president may authorise the supply of crude oil and petroleum products despite the fact that they meet the conditions for prohibition stipulated in the act.

Commentary

- Putin's decree is an expected reaction to the restrictions imposed by Western countries on trade in Russian oil and petroleum products. The document was previously announced by Kremlin spokesman Dmitry Peskov and Deputy Prime Minister Aleksandr Novak. Neither its content nor the substance of Moscow's response are surprising. Even before the West's final decisions on the price cap issue, Putin had repeatedly announced that Russia would not supply energy resources to countries that would impose price restrictions related to oil and gas imports from Russia.
- The wording of the document indicates that Moscow's intention was to draft it in such a way that the Kremlin could have a great deal of flexibility in implementing the regulations introduced. Firstly, the president was given the right to arbitrarily decide on the application of exemptions to the supply ban. There are many indications that Moscow may be interested in exercising such an option in the case of countries which, although they supported the price cap decisions, at the same time pursue a policy aimed at strengthening energy cooperation with Russia (Hungary). Secondly, the decree grants the Ministry of Energy, after agreement with the Ministry of Finance, the right to provide explanations on the application of the regulation, which also creates room for interpretative changes depending on Russia's political needs. Thirdly, the relatively distant date of entry into force of the decree with regard to oil supplies (1 February 2023) and the lack of a specific date concerning petroleum products may indicate that the Kremlin intends to closely monitor developments in the oil markets in the coming weeks and make final decisions on the implementation of the adopted bans dependent on the observed results. This is also confirmed by the relatively short duration of the document

(until 1 July 2023).

- It is difficult to predict to what extent the decree may prove to be an effective – from Moscow's perspective – response to the oil restrictions implemented by Western states. This is influenced by the aforementioned lack of clarity regarding the process of implementing its provisions and, above all, by the changing situation on the global oil market. Firstly, the document will have little practical relevance if Russian oil prices remain as low as they were in the final weeks of 2022. On 21 December, a barrel of Urals crude cost less than \$42 (Primorsk and Ust-Luga) and \$40 (Novorossiysk) at European ports, well below the price cap set by the G7 countries, the EU and Australia (\$60 per barrel). Moreover, for EU members, the significance of the adopted decree will be limited by the embargo on the seaborne imports of crude oil from Russia, in force since 5 December. Secondly, it is unclear what attitude towards Russia will be adopted by trading partners from countries that have not joined the restrictions introduced by Western countries. Although Beijing or New Delhi, which significantly increased Russian oil supplies in 2022, did not support the decision of the G7, the EU and Australia, it is possible that they will be eager to use the established price cap to negotiate even greater discounts from Moscow. Thirdly, the global oil market is significantly influenced by supply and demand factors, such as the size of oil reserves in the US or changing forecasts for oil demand in the coming months in countries such as China.
- Although it cannot be ruled out that Moscow will use the decree as a legal justification for cutting off oil supplies to EU countries importing crude via the Druzhba pipeline, such a scenario seems less likely at this stage. On the one hand, such a decision would be part of the logic of energy escalation, an element of which has been the reduction and suspension of gas supplies to many European customers since spring this year. Moreover, the countries receiving the oil transported through this pipeline (Poland, Germany, the Czech Republic, Slovakia and Hungary) have formally supported the introduction of a price cap. On the other hand, however, supplies to these countries via the Druzhba pipeline have been formally exempted from the EU embargo and thus from the price cap mechanism. Thus, there are many indications that Russian companies will be able to supply oil to customers from the indicated countries under legally unchanged conditions (including pricing formula).