
The prospects and challenges for Euro-Russia energy conflicts after the military invasion to Ukraine

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Half a year: what are the first results of the sanctions?

KEY SANCTIONS:

- Financial restrictions on loans and payments. Frozen financial reserves.
- Export controls for new technologies needed for the future development (long-term access for new equipment and services)

OIL:

- Oil embargo to come into force in December. It's already getting much harder for Russia to transport oil (more sophisticated logistics, increasing margins of intermediaries)
- Planned G7 "price cap" introduction

GAS:

- No sanctions for pipeline gas
- Technological sanctions for liquefaction equipment

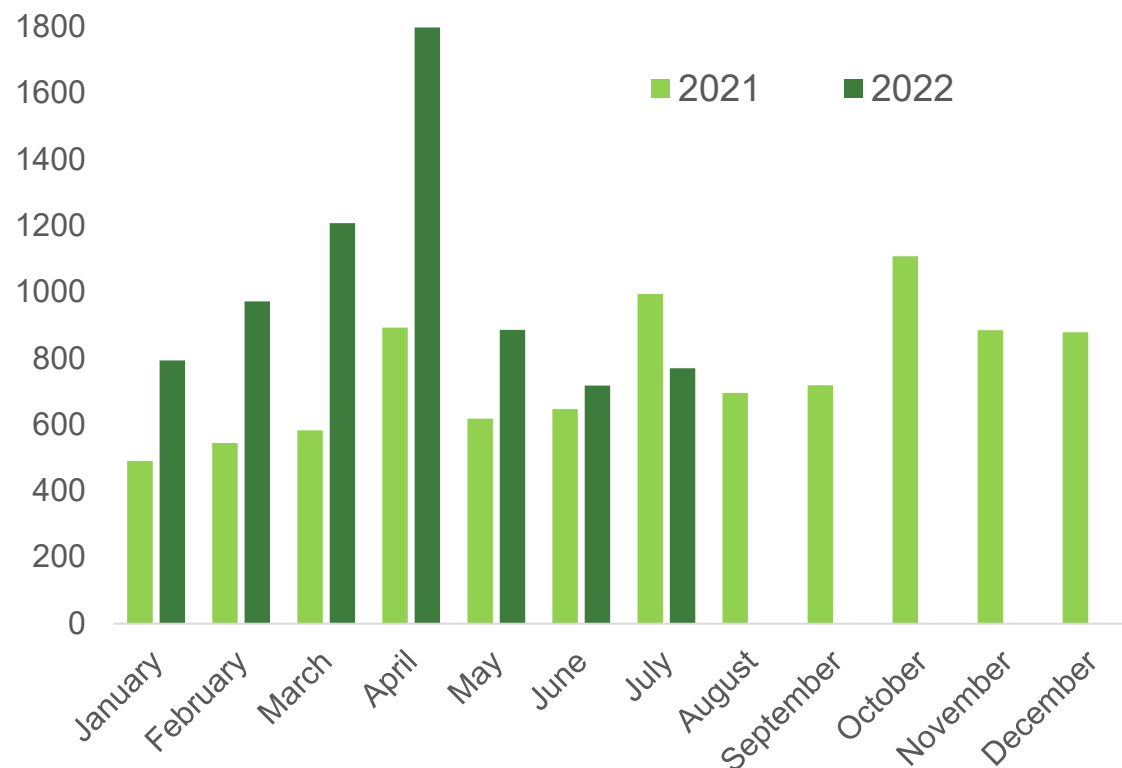
COAL:

Coal embargo starting from 10th August

Main impact surprisingly came from self-sanctioning on oil purchases and on the new investments as well as Russia's own supply cuts to Europe

Russian oil&gas revenues: Russia has record energy earnings, but budget revenues started already to slip

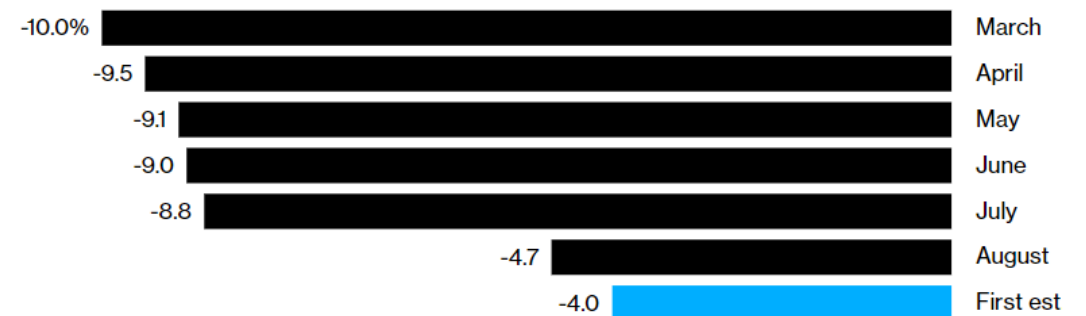
Russian budget oil&gas revenues, bln rubles



Source: Russian Ministry of Finance

- Russian economy slump is far more shallow than initially expected.
- Oil-and-gas earnings are still higher than planned, but are likely to decline later in the year as falling export volumes and ruble strength hit the result.
- These revenues are to a certain extent “virtual” as they cannot actually be properly used.

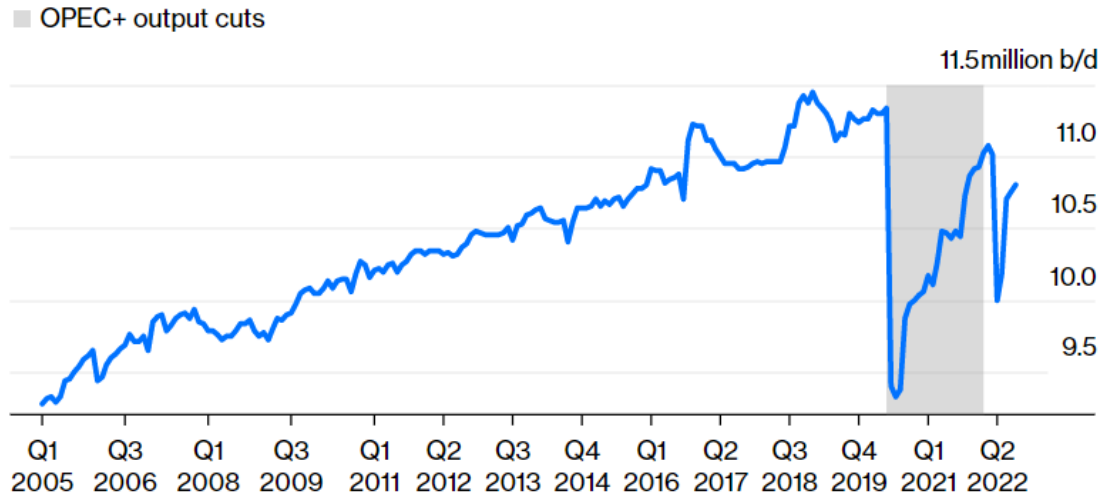
Monthly forecasts for 2Q Russian economic performance vs actual data



Source: Bloomberg surveys of analysts in March-August 2022, Federal Statistics Service for official report on 2Q

Russian oil industry: rebound in summer to the pre-war level after falling sharply in March-April

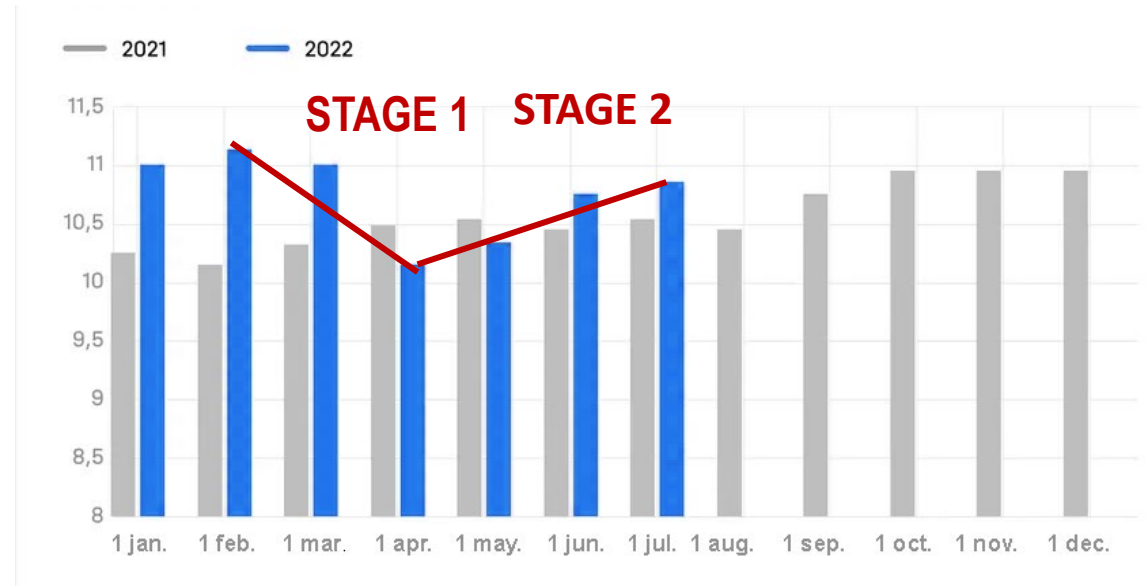
Historical crude oil production in Russia
(2005-2022, million bpd)



Source: Bloomberg and industry estimates

Note: August data is for early days of the month, based on industry estimates

Crude oil production in Russia
(monthly, 2021 and 2022, million bpd)

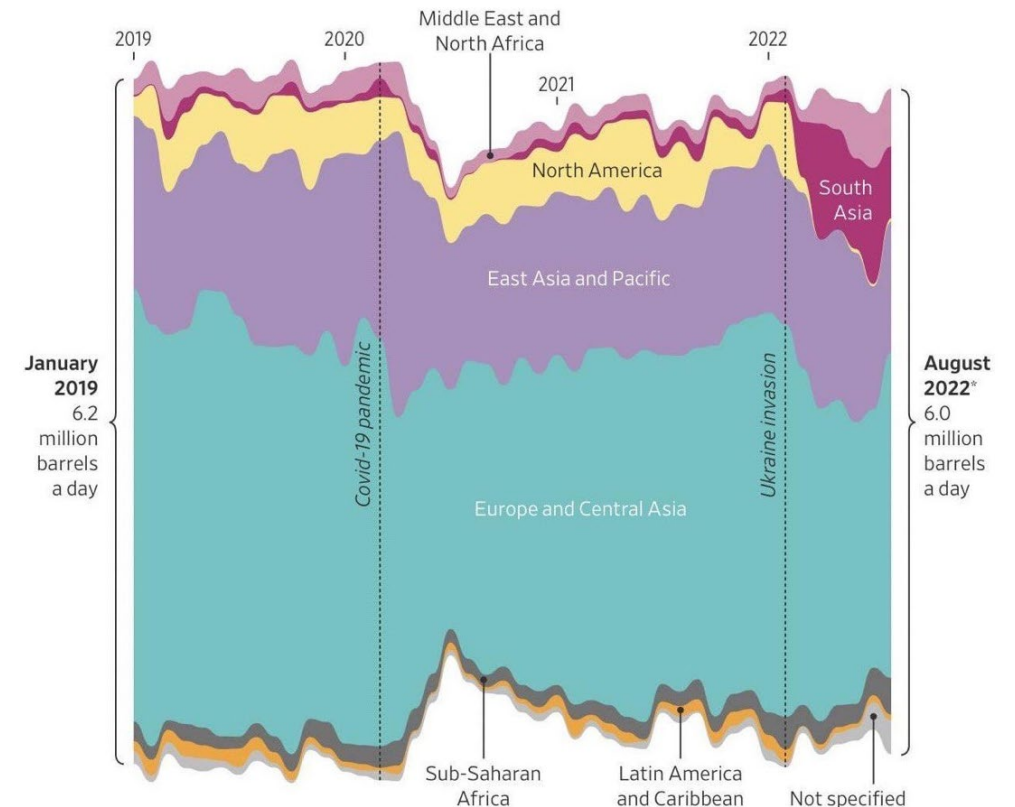


Source: IEF, The Bell

Russian oil exports: although the US and the EU reduced their imports, Asia and Middle East are buying more

- After that initial struggle, Russia has found new customers for the million barrels a day or so that European oil refiners have stopped purchasing due to self-sanctioning.
- Most of that crude is ending up in Asia — notably India — but also in Turkey and elsewhere in the Middle East. And some is still showing up in Europe, with buyers still purchasing Russian crude ahead of the planned introduction of official sanctions in early November.
- The second indicator is the price of Russian oil. Initially, Moscow was forced to sell its flavors of crude at huge discounts to other varieties to entice buyers. In recent weeks, however, Russia has regained pricing power, taking advantage of a tight market.
- Despite a trip by US President Joseph Biden to Riyadh, Putin has retained his influence inside the OPEC+ alliance.
- G7 decision to introduce "price cap" on Russian oil might have very severe consequences.

Russian shipments of crude oil and products



* As of 20th August 2022

Source: Vortexa, Andrew Barnett / The Wall street Journal

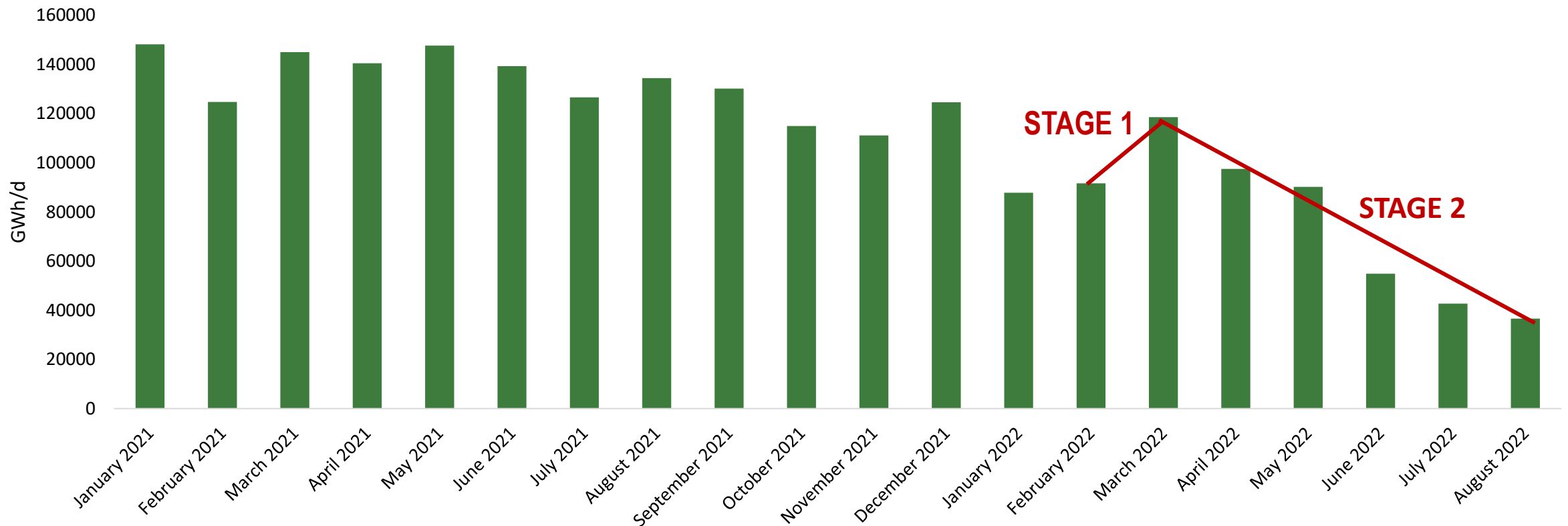
Russia`s reaction was predictable

- "As far as price restrictions are concerned, if they impose restrictions on prices, we will simply not supply oil and petroleum products to such companies or states that impose restrictions as we will not work non-competitively. Interference in the market mechanisms of such an important industry as the oil industry, which is the most important in terms of ensuring the energy security of the whole world, such attempts will only destabilize the oil industry, the oil market,"
- *Deputy Prime Minister Alexander Novak*



Russian gas exports to Europe are now at ~25% of average 2021 level

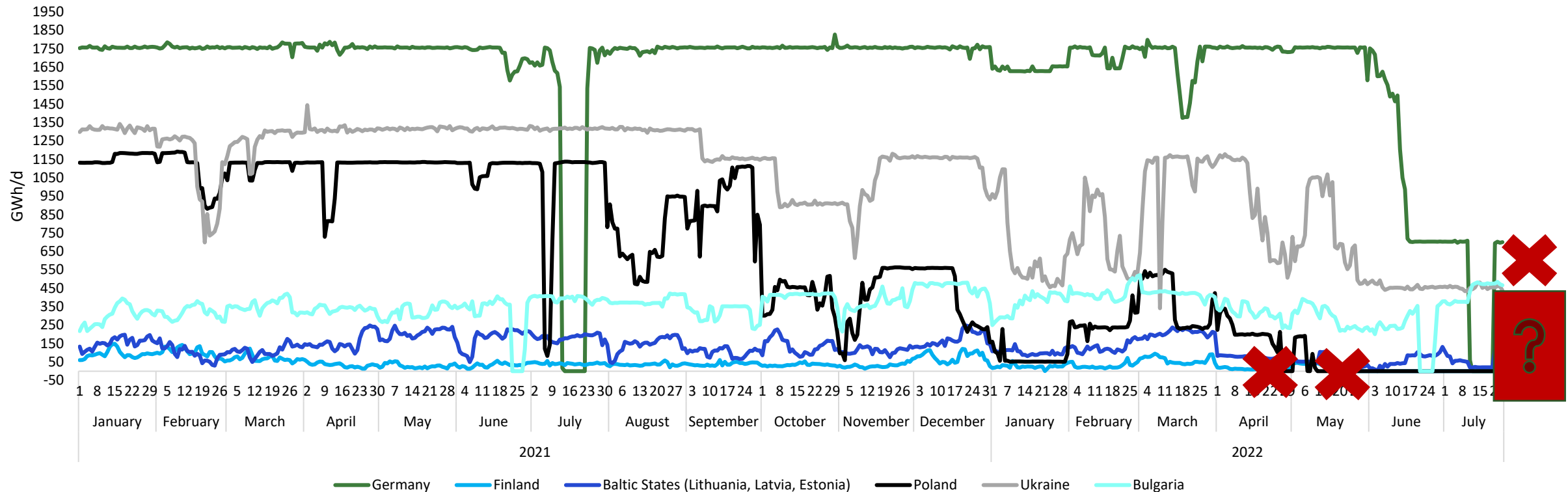
Total physical gas flows from Russia to Europe (excluding Turkey)



Source: ENTSOG

Russian gas exports to Europe are now at ~20% of historical level with high probability of further decline

Physical gas flows from Russia to Europe by direction (excluding Turkey)

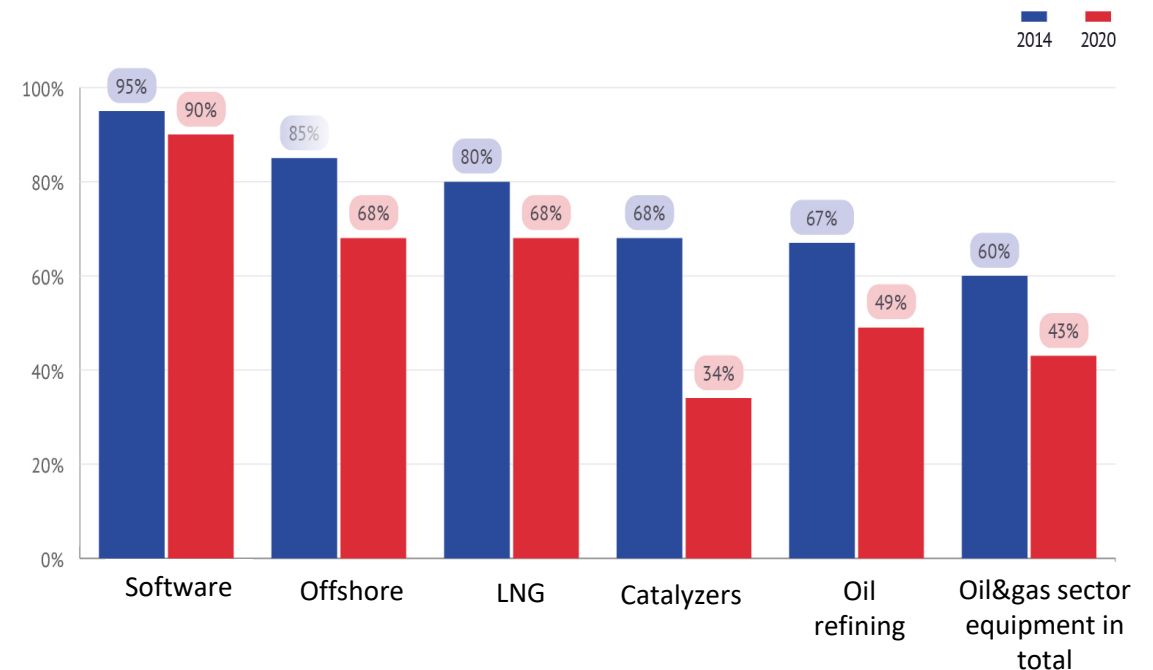


Source: ENTSOG

Main impact surprisingly came from self-sanctioning on oil purchases and on the new investments

- The share of foreign companies in oil and gas production in Russia was approximately 2.5 million BOE/d, equivalent to 11% of the total production volume in 2021.
- International oilfield service companies play key roles in the supply of software for oil and gas production, equipment for the LNG industry and trunk transportation, as well as in the implementation of multi-stage hydraulic fracturing.
- The departure of international oil and gas companies will greatly affect LNG and offshore projects, but in general it will not be critical. The departure of oilfield service companies may have a more serious impact.
- Western companies are withdrawing from the Russian energy sector, but the new decree put in place in August – Western companies will be banned from selling their stakes in the strategic sectors, including the energy.

Changing share of foreign equipment in the Russian oil&gas industry



Source: Russian Energy Ministry, Ministry of Industry and Trade, CDU TEK

Key unknowns

- High oil sales allow Russian to restrict natural gas sales to Europe, putting pressure on the EU leaders, which are bracing for massive retail energy price increases and potential shortages that may lead to rationing this winter. A combination of cold weather, surging demand for electricity and soaring prices later this year risks undermining Western support for Ukraine.
- Reaction of China, India and OPEC on the “price cap” introduction and generally their dissatisfaction with the West.
- Weather this winter.
- Degree of solidarity and success of anti-crises management in the EU.