

Russia's Significance for International Energy Landscape

Ken Koyama, PhD
Chief Economist, Senior Managing Director
The Institute of Energy Economics, Japan

On July 9, the Institute of Energy Economics, Japan, held a webinar titled “COVID-19 and Russia: The Present Status and Outlook of the Energy Situation and Putin Regime.” In the first half of this webinar on Russia suffering from the huge negative impact of COVID-19, an IEEJ expert made a presentation on the present status and problems of oil and gas production and exports. In the second half, another IEEJ expert gave a presentation on policy challenges for President Vladimir Putin who seems to have gained public confidence through the recent national referendum. These presentations were followed by question-and-answer sessions. In the following, I would like to summarize key points of Russia's significance for the international energy landscape that I felt anew through the webinar.

Russia is a leading energy producer and exporter. Regarding oil, the most important good in international energy trade, Russia produced 11.54 million barrels per day in 2019, ranking third in the world. As for natural gas, the second most important internationally traded energy commodity, Russian production in the year came to 679 billion cubic meters (BCM), ranking second. The United States was the world's largest oil and gas producer. The second largest oil producer was Saudi Arabia. Russia exported 9.19 million bpd in oil (gross exports) and 256.6 BCM in gas in 2019, being the largest oil and gas exporter in the world. Russia is thus an oil and gas giant rivalling the United States and Saudi Arabia. The three countries are competing against each other in the entire international energy market.

The oil and gas production and export policies of Russia, as the energy giant, are one of the most important matters of concern to the United States, Saudi Arabia and other energy stakeholders in the world. Given that the three countries are natural competitors against each other, whether the United States or Saudi Arabia could strategically cooperate with Russia would be the key to international energy market stabilization.

A typical case is Russia's participation in joint oil production cuts by the Organization of the Petroleum Exporting Countries and non-OPEC oil-producing countries. Whether Russia participates in OPEC-plus cooperation in production cuts has been the most important matter for OPEC and its leader Saudi Arabia over the past years. Russia has held the key to the joint production cuts for the stabilization of the global oil supply-demand balance. This is the reason Russia's refusal to enhance the production cuts in March this year led the OPEC-plus cooperation framework to collapse, plunging the international oil market into a price war. Russia's strategic conclusion that the enhancement would only benefit the United States to the disadvantage of Russia thus triggered an oil price crash.

Amid the COVID-19 disaster, however, the price war cost all stakeholders too much. In an interesting development, U.S. President Donald Trump served as a mediator to stop the price war. As a result, Russia came back to OPEC-plus to rebuild the OPEC-plus cooperation framework, leading the group to launch record production cuts in May. Russia has thus played a role in leading oil prices to turn up from record lows. Recently, however, the fate of the OPEC-plus production cut policy

including Russia's policy has been attracting attention from oil market players again.

Whether and how long Russia would cooperate with OPEC is becoming a matter of interest to oil market players. Russia for its part has implemented production cuts mainly at relatively inefficient run-down oil fields, according to analysts. Russia could switch from the production cuts. However, it is uncertain how much Russia could increase oil production or how much the Russian oil industry hit hard by the oil price crash and an oil demand plunge under the COVID-19 disaster could recover investment. Although the Russian oil industry has requested various rescue measures from the government, we will have to closely watch how such rescue measures would be implemented or how they would be effective. It is important to assess investment recovery in anticipating Russian oil and gas production over a short to medium term.

Russia's presence in the international natural gas market is also very great. Russian natural gas exports account for more than a quarter of global trade and mostly go to Europe linked to Russia through pipelines. Russia is also trying to expand gas exports to China. Russian gas exports have thus become a key factor exerting great influence on the Eurasian energy landscape and energy geopolitics. Russia has also increased its presence in the liquefied natural gas market in recent years thanks to emerging Russian energy company Novatek's growing LNG exports. As LNG has become a global good, Russia's presence has been rising not only in Eurasia but also in the global natural gas and LNG market.

However, Russia's gas sector has faced serious difficulties this year. Its pipeline gas exports to Europe, the most important market for Russia, in the first quarter of this year plunged some 30%. Factors behind the plunge include a warmer winter in Europe, a European gas reserve expansion prepared for a breakdown in negotiations on Russian gas exports via Ukraine, the successful conclusion of the negotiations late last year, European economic deterioration and lockdowns under the COVID-19 disaster, and Europe's LNG import expansion. European LNG imports expanded despite an overall natural gas consumption plunge as Europe became the last-resort buyer of LNG amid oversupply and weak prices. Russia has thus been affected by all such supply and demand changes. Whether Russia would remain the gas market supply-demand adjuster or change its course to restore its market share would have great influence on the European natural gas market and the international LNG market and should be closely watched.

Russia has recognized energy's strategic importance for itself. President Putin might have been well aware of the importance and been strategically considering how to use energy in the best interest of Russia. While Saudi Arabia's oil sector is monopolized by state-run Saudi Aramco, Russia's oil and gas sector has multiple leading companies. Russia thus differs from Saudi Arabia in terms of conditions regarding the government and the energy industry. In Russia, energy giants, including Rosneft in the oil sector and Gazprom and Novatek in the gas sector, have close relations with the Putin regime. When analyzing the Russian energy situation, we must consider and check these energy giants' behaviors and business strategies as well as their relationship with Russia's national strategies.

Energy policies and strategies of Russia, which is strongly conscious of viewing energy as a strategic good, will remain a key factor exerting great influence on the international energy landscape and energy geopolitics. However, we must take note of the fact that Russia and its energy sector face various challenges. The most important among the latest challenges are a sharp fall in export revenue and a remarkably negative impact on the national economy, which have resulted from an energy export decline and weak energy prices under the COVID-19 disaster. Other challenges include constraints on energy development under the prolonged and enhanced Western economic sanctions, growing

dependence on China amid Western sanctions and soured relations with Western countries, Russia's relatively weaker position against China, the need for addressing the global low-carbonization or decarbonization trend mainly seen in Europe as Russia's key market, and the diversification and advancement of Russia's economic structure depending heavily on oil and gas exports. How Russia would tackle these challenges will be a key point for analyzing the future international energy landscape. It is important for Japan to consider Russian policies and strategies in formulating national strategies.

Contact: report@tky.ieej.or.jp

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