European Division over Russian Energy

Sarika Rahman[#1], Kendall Carll[#2], Eli Pearl[#3], Michelle Liou[#4] , Joy Park [#5]

[#]*Foreign Policy, Institute for Youth in Policy*
1700 Van Ness Ave #1143, San Francisco, CA 94109

[1]sarikarahman@yipinstitute.com, [2]kendallcarll@yipinstitute.com, [3]elipearl@yipinstitute.com, [4]michelleliou@yipinstitute.com, [5]joypark@yipinstitute.com, mairelle@yipinstitute.com

***Abstract*— This brief explains the economic beginnings of European and Russian energy transactions in relation to the EU's proposed ban on Russian oil, which comes as a response to the Russian invasion of Ukraine. It details obstacles that the European Union will have to overcome for the proposal to pass, as well the next steps Europe must take to counter an absence of Russian energy in Europe.**

***Keywords*— EU, Russia, Ukraine, Oil Ban, and Dependency**

I. Executive Summary

As Russian forces continue to violently push through eastern Ukraine, the EU, in an effort to place greater pressure on Russia, proposes a ban on all Russian oil imports. However, while the ban holds the possibility of severely damaging the Russian economy, European nations will have to contend with Russian retaliatory response, as well as the impacts of losing its largest supplier of energy. This brief traces the history of European dependency on Russian energy and connects it to the current debate on banning Russian oil in all member states of the EU. Furthermore, it considers the possible means by which Europe will adjust to the loss of Russian energy, both before and after the enforcement of the oil ban.

II. Overview

On May 4, 2022, European Commission President Ursula von der Leyen announced a proposal to ban all Russian oil in Europe.[8] The plan aims to phase out the import of Russian crude oil in six months and stop the flow of refined oil by the end of 2022. The move to ban Russian oil is the latest in EU efforts to economically punish Russia for its invasion of Ukraine, which has persisted and escalated since the initial attacks in late February, 2022.

A. Pointed Summary

- ➢ Increasing economic pressure against Russia
- ➢ Developing energy independence from Russia

B. Relevance

Before the proposal of the ban, the EU joined other Western nations in implementing and enforcing crippling sanctions against Russia. Of the measures taken so far by the EU, restrictions on Russia's financial and capital markets, economic sanctions against Russia's financial, energy, and technology sectors, and removal from SWIFT have been most influential among other measures. More recently, on April 8, 2022, the EU adopted its fifth package of sanctions against Russia, which notably included a ban on Russian solid fuels, an indication of the next steps the EU plans to take to remove itself from Russian energy.[14]

III. History

The fifth package of sanctions comes directly in response to the worsening condition of the eastern Ukraine. Following intense shelling in various northern and eastern Ukrainian cities for over a month, Russia announced on March 30 that it had agreed to withdraw from the capital city of Kyiv, which it had failed to take over after several attempts.[10] However, as predicted, the move was largely a regrouping of Russian forces in order focus more on the Donbas region.[19] Furthermore, shortly after the announcement of withdrawal, Ukrainian President Zelinsky accused Russia of war crimes after at least 278 dead bodies were found in Bucha, a city northwest of the capital.[20] Furthermore, with Russian refocus on the Donbas region, the conflict grows even worse in the southeast of Ukraine, namely in cities such as Mariupol and Odessa.[26] As a result of increased Russian aggression in the region, the EU, along with other Western nations, are compelled to take drastic actions to halt Russian

funds that would allow the war persist. However, such actions are inextricably tied to Europe's history with Russian energy.

A. Tried Policy

Current ties between Russian oil and Europe began during the Soviet Union. Post-World War II, the Soviet Union concentrated its economy into oil production, occupying second place in global oil production by the 1950s. By 1955, the USSR, through oil exports, managed to form close ties with Germany. By the 1960s, the USSR and Germany had signed several trade agreements, and, in 1964, formed the world's longest oil pipeline Druzhba, commonly referred to as the "Friendship Pipeline."[27] However, by the 1980s, due to its growing dependence on oil, the USSR failed to develop other sectors of the economy, which made it vulnerable to regular shifts in global oil prices and forced the country to trade for critical raw resources. Nevertheless, in 1989, the total energy production of the Soviet Union was equal to "21% of the world's population," surpassing the 20 percent that U.S. was responsible for at the time.[11]

The growth of Europe's energy dependence from Russia grew continuously from then on, eventually leading to the creation of the gas pipeline Nord Stream in 2011. Specifically, Germany's energy dependence on Russia grew significantly, as the country relied on Russia for an estimated 50% to 75% for its natural gas.[18] Currently, the pipeline is responsible for one-third of all Russian gas exports, reaching record levels in 2021. Plans were also made for the construction of Nord Stream 2 prior to Russian invasion of Ukraine but were halted shortly after the invasion.[18] Furthermore, in 2021, the EU imported more than 40% of its gas consumption from Russia, leading to current concerns regarding European dependence on Russian energy.[13]

B. Current Stances

Despite its dependency, the European Union, in response to the invasion of Ukraine, has and is attempting to cut ties with Russian energy. As stated previously, almost immediately after the invasion, Germany halted the development of Nord Stream 2, a gas pipeline that would double the output of the Nord Stream 1 pipeline.[4] The Nord Stream 1 pipeline directly connects Germany and Russia, and sends Russian gas straight to Germany. The EU has attempted to create a gradual embargo on Russian crude oil in six months.[7] The goal is to put the most strain on the Russian economy while also not putting mass strain on EU countries. However, the proposal has not received unanimous support. The EU is also installing a ban on Russian coal, but the full effect of the ban was pushed back to mid-August.[16] The EU has been unable to fully ban Russian energy due to mass dependence, and fully cutting Russia out of oil and gas trade will be a tall task for the EU.[28]

As for Russia, it has responded to EU sanctions by installing sanctions of their own. Gazprom, a Russian Government-owned gas company, announced that it would stop transporting natural gas through Poland.[3] This ban is one step by Russia to cut off Europe from Russian gas. The Poland ban follows sanctions by Russia to more than 30 European energy companies. Bulgaria has also been cut off of Russian gas, which has resulted in gas prices in Europe surging by 28%.[22] In response, European Union President Ursula Von Der Leyen called the cutting off of Russian oil an "Instrument of Blackmail."[15] To stimulate the Russian economy, the Russian government has forced buyers to secure Russian gas via the use of Rubles. In response, European states have accepted Russia's proposal and opened ruble accounts. The usage of Rubles has been seen as a loophole, as Italian Prime Minister Mario Draghi stated that using rubles to do business with Russia does not betray sanctions against the Russian state. Russia will likely continue to react to European sanctions with sanctions of their own.[6] The prime effect of these sanctions and counter sanctions is that it will become harder and harder for the average European citizen to cheaply acquire oil and gas.

IV. Policy Problem

A. Stakeholders

As a result of concern regarding prices and resource allocation, following the announcement of the proposed ban, Hungary, the Czech Republic, and Slovakia reported that transition to another alternative wouldn't be viable due to the lack of

time and existing infrastructure. Even with an extended one-year deadline, Hungary diplomats have pushed for an all-out exemption from the ban.[23] Without compromise, Hungary's veto would halt the whole proposal as EU proposals require unanimity to enact. Meanwhile, Greece, Malta, and Cyprus have expressed concerns about their shipping industry, as they host large ship-management centers and together harbor the largest shipping fleets in the EU.[12] With Greece shipping half of all Russian exports following the invasion, a ban on Russian exports would cut transport revenue in these countries. On the other hand, Germany has agreed to support the ban despite its heavy reliance on Russian natural gas. Already, German Foreign Minister Annalena Baerbock said that Germany will stop importing Russian oil and will gradually halt natural gas imports by the end of 2022.[25] However, Financial Times reports that the cut would cost 12% of Germany's GDP, bringing concerns of high prices of basic necessities.[2] Ultimately for Europe as a whole, the plan to ban Russian oil faces significant obstacles before being conceivable.

B. Nonpartisan Reasoning

As the ban on Russian oil continues to be debated, questions arise on if the ban will be successful to begin with, specifically on if Russia will be able to weather the ban even with pre-existing sanctions. Though Russia may be able to hold on short-term with current high prices, Russia will likely not be able to redirect the entire European allotment to other nations. In fact, an EU ban would result in a loss of 2 million barrels a day from Russia.[9] However, Asian buyers have already increased their consumption of discounted Russian oil, namely in India and, to a lesser extent, Turkey.[30] Either way, gas prices are expected to increase worldwide, but especially for Europeans, who will have to swiftly find energy alternatives under the ban.

V. Policy Options

Even with the best public cooperation, a full ban on Russian oil would leave a substantial gap in consumer demand throughout Europe. Importantly, this gap would not be evenly distributed, with countries in the East considerably more reliant on Russian oil than those in the West. The obvious question of fill-in is then both pre- and post-proposal: a persuasive, minimally inflationary supply replacement is necessary to get Eastern approval on the ban and will be essential in ensuring the efficacy of the policy.

Currently, two methods of supply-replacement have arisen – the diversification of imports and investments in European oil and gas infrastructure – while another, the potential restarting of European nuclear energy supply.

Diversification of Imports

Diversification is the most obvious course of action. Compared to other policy options, diversification has the unique benefit of providing an immediate influx to help fill the gap of Russian energy, while other options often rely on promises of investments into energy sectors to increase long-term, domestic production. The constraints of diversification are nevertheless substantial, even if they are more political in nature.

As a strong supporter of the ban, the U.S. has offered to increase its exports to the continent. President Biden said, with specific reference to Germany's aims of halving Russian energy, the U.S.[21] is poised to increase its role as an energy supplier to Europe, particularly by replacing the punishing restrictions Russia has placed on European natural gas purchases. What isn't clear, however, is exactly how President Biden would enforce such a measure, as demanding private companies to increase their sales to a group of countries is hardly in the list of enumerated presidential powers. And, as many executives in the oil and gas field are concerned with, the U.S. has a shortage of port and shipping capabilities, having effectively already met its export capacity.

The other partnership that Europe is likely to pursue would be with various OPEC countries. With few of those countries having allegiance to the West, Europe will be met with hesitant resistance in asking neutral countries to indirectly intervene in the Russia-Ukraine conflict on the part of the West. Even then, OPEC has made explicitly clear to Europe that: 1) it won't be, as a bloc, pumping more

oil to the continent; and 2) even if it did, replacing the lost volumes is certainly impossiable.[1]

Despite these challenges, the EU estimates being able to replace roughly half of the lost imports. According to Ben McWilliams, analyst at Bruegel, the avoiding of severe inflationary pressures will come down to reducing consumer demand as European governments will just have to "'ask households to cooperate'" with the reduction in supply.[9]

Upgrading European Oil and Gas Infrastructure

The purpose of waning Europe off of Russian energy supplies is two-fold – to punish Russia economically and to push Europe toward self-resiliency. To achieve this energy independence, Europe must upgrade its own oil and gas infrastructure in order to operate independent from Russia. These energy investments also act as a critical leverage point in negotiations with eastern European nations hesitant to support the ban.

The European Commission is now "considering offering landlocked eastern European Union states more money to upgrade oil infrastructure in a bid to convince them to agree to an embargo on Russian oil." Upgrades to existing infrastructure will then be a certain reality post-ban, being a necessary precondition to its passing.[17]

Even with current investments and future promises, however, the most clear problem with relying on upgraded infrastructure as a solution to the lost Russian supply is that it takes time to build. This delay puts the EU in a unique spot whereby they either have to pass the ban now and ensure a larger shortage or wait to pass the ban, potentially reducing its efficacy.

Restarting of European Nuclear Energy Supply

Diversification and infrastructure investments, while their effectiveness in filling in the supply shortage that would be created by the ban may be argued, are essentially guaranteed. What isn't a guarantee is the serious consideration of revitalizing Europe's waning nuclear energy supply in order to fill the gap.

Currently, a combination of intentional phasing out of plants and the allowing of infrastructure to become outdated has led to the rapid decrease in European nuclear plants.[24] As Europe faces a worsening the energy crisis, the slow loss of nuclear energy for the European continent comes at a particularly bad time.[24]

The problem with the nuclear energy supply is both practical and political. As another form of energy infrastructure investments, there will be a delay between policies that work to promote nuclear energy and the increase in energy supply as a result. Politically, though less toxic than in the U.S., policies to increase nuclear energy supply face challenges unique from oil and gas – concerns over radiation pollution, waste storage, etc.

VI. Conclusions

As the Western nations face increasing confrontation, it certainly seems to be in Europe's long-term interest to achieve energy independence from Russia. More immediately, a full ban on oil imports would increase the economic pressure the West is putting on Russia for its violence in Ukraine.

Such an energy transition may also provide the opportunity for clean, renewable sources to proliferate. An E3G study indicates that Europe would be able to transition away from Russian energy by 2025 without the extension of coal power or building of oil/gas infrastructure.[29] While some fossil fuel investments will likely be necessary in order to get the ban over the diplomatic finish line, Europe would do well to use the push for independence to invest heavily in clean energy sources.

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