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RUSSIA AND SANCTIONS: IMPACTS ON ENERGY MARKETS AND GEOPOLITICS
ROUNDTABLE REPORT

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On March 15, 2022, Columbia University's Center on Global Energy Policy (CGEP) hosted a private, virtual roundtable focusing on the consequences of the Russian invasion of Ukraine on energy markets and geopolitics, as well as possible future actions of the United States, the European Union, and allied countries.

The roundtable took place three weeks after the start of the invasion of Ukraine by Russia on February 24, 2022. The United States, the European Union, and other countries reacted very rapidly by imposing sanctions on Russia. Mid-March was also a moment of extreme volatility in global energy markets, with commodity prices at record high levels amid growing fears of Russian energy supply disruptions. Concerns about markets' responses to a more severe disruption of Russian oil and gas supplies, whether initiated by Russia or by an embargo on Russian oil and gas, remain.

This document summarizes the March 15 roundtable, which was conducted on a not-for-attribution basis. Participants in this roundtable included senior corporate executives, civil society representatives, energy analysts, academic and think tank experts, and government officials from Canada, the European Union, and the United States. Roundtable participants discussed the potential evolution of the conflict in different timeframes and how sanctions and relationships between key geopolitical actors could develop. Given Russia's prominent role as a major exporter of oil, gas, and coal, speakers devoted special attention to the war's potential impact on energy markets.

Potential Sanctions Developments and Geopolitical Implications

The United States, the European Union, and allied countries reacted swiftly to the Russian invasion by applying sanctions to different parts of the Russian economy. The evolution of the war and the imposition of sanctions in the coming months will have implications for Russia and its economy. The keynote speaker acknowledged the difficulty of foretelling the precise course of the war but offered thoughts about scenarios in two-week, two-month, and two-year timeframes.

A Two-Week Scenario

In a two-week scenario, the keynote speaker hypothesized that if Russia seized control of major cities and supply routes in Ukraine (without inflicting too many atrocities), it could have cemented a victory of sorts without engaging in diplomacy with North Atlantic Treaty Organization (NATO) countries. At that point, Russia could be in a position to install a puppet government in Ukraine or dismember Ukraine into a multiplicity of smaller "People's Republics."

Some participants mentioned that this two-week projection would only happen if the Russian assault on Ukraine resulted in an overwhelming loss of life and territory for President Zelensky. Other participants countered this hypothesis, arguing that the unexpected stalemate would not allow for Russia's swift takeover of Ukraine.

The speed and escalation of the US and its allies' targeted sanctions campaign against key Russian individuals and institutions, designed to match the expected tempo of the Russian military's progress, was remarkable. The united front on sanctions appeared to have caught Moscow by surprise, resulting in the rapid isolation of Russia's economy and financial system, the plunging ruble, the closure of the Russian stock market, $640 billion of Russian central bank reserves frozen in G7 currencies, and the contraction of Russia's GDP by 15 percent by the time of the event. Moreover, the departures of major multinationals and financial giants were also largely unexpected.

However, one participant suggested that Putin may have in fact sought the social and financial isolation of Russia by instigating the conflict with Ukraine and inviting sanctions, which would allow him to revert the country back to what one speaker termed a "Soviet style of mobilization" that would be hierarchical and isolated from the rest of the world. This speaker also hypothesized that the invasion and its consequences may have been a calculated move to provoke anti-West sentiments among the Russian population.

Participants agreed that the next set of elevated sanctions ought to target Russian oil sales and revenues. However, they cautioned that Russia may have preemptively identified secondary markets for its oil.

Roundtable members discussed the United States' strategic and policy goals for escalating or relieving sanctions moving forward. Some speakers opined that if Russia was able to secure success within two weeks, Putin would insist upon full and unconditional sanctions relief in any peace talks.

However, the stalemate did not suggest to members of the roundtable that a cessation of hostilities was imminent. In fact, participants noted that signs pointed to the conflict becoming more entrenched and offering several possible adverse outcomes for Russia in the long run.

A Two-Month Scenario: Stalemate Persists, Outcome Unpredictable

The keynote speaker also presented a two-month outlook in which the West's sanctions and arms assistance to Ukraine would further entrench the current stalemate, with an escalating human toll. In this phase, the speaker argued, it would be in Putin's interest to establish dominance as quickly as possible in order to dictate the terms of any preliminary ceasefire and diplomatic negotiations.

However, other participants countered that the current stalemate is likely to persist as Ukraine is bordered by four NATO countries, Russian military gains appear to have plateaued, with attrition warfare taking a toll on its forces, and the West is contemplating increasingly aggressive sanctions. They observed that the plucky resistance mounted by besieged eastern Ukrainian cities has denied Putin a speedy and assured victory. In this scenario, argued these speakers, a significantly weaker Russia would be forced to the negotiating table without receiving any major concessions from the West or from Ukraine.

If, however, Russia deploys chemical or biological warfare against Ukraine, many speakers anticipated those actions would trigger a full financial embargo with (largely) unknown outcomes for Russia and global energy prices.

Participants noted that the US Congress could consider imposing Iran-style (gradual ramp-up) sanctions and the G7 countries could increase arms assistance to Ukraine. They likewise predicted that large multinational companies that exited Russia are also unlikely to return in this short-term period, so the country's financial isolation will likely persist.

In this two-month timeframe, participants also suggested that the US and its allies may choose to withhold sanctions relief until Russia fulfills its commitments (unlike the Minsk Agreements) or contributes significantly to rebuilding and rehabilitating Ukraine via reparations.

One respondent also questioned the feasibility of reducing global dependence on Russian oil and petroleum exports in the short run, given that Russian oil has already found secondary markets at deep discounts. They also wondered whether Putin would consider the direct sanctioning of Russia's energy revenues (about 40 percent of Moscow's budget at the time of the event) akin to the US establishing a no-fly zone or delivering MiGs to Ukraine.

Many participants suggested that China will be strategic in its response in this standoff, particularly if it perceives opportunities to take over select Russian assets or backfill markets lost by Russia. Some speakers proposed that China may still choose to provide support to Russia via its financial institutions that do not have Western exposure.

A Two-Year Scenario: Bleak Outlook for Russia

In this last scenario, two years into the invasion of Ukraine, the keynote speaker outlined a grim geopolitical and financial outlook for Putin and Russia. The speaker noted that, similar to the Iran sanctions regime, the US and its allies may actually find it easier to escalate energy sanctions. By this logic, the US and G7 escalation of an Iran-style sanctions regime would be twofold: First, the threat of secondary sanctions on countries purchasing Russian oil (exempting jurisdictions that significantly reduced their purchases of Russian oil in the preceding three to six months) could phase reductions of Russian oil exports over time, and second, purchasing countries could be required to hold payments for Russian oil sales in their own banks, and those funds could be restricted to bilateral trade in goods and services, thereby hurting Moscow's war chest.

According to the speaker, the combined impact of the prolonged stalemate and Western sanctions could sour Putin-ism, potentially to the point of precipitating regime change. It may be hard to evaluate whether the united front of the United States, the European Union, and allied countries can remain intact throughout a two-year period as sanctions are not an "on/off" switch. Speakers pointed out that group cohesion may be tested if oil and gas prices continue to skyrocket and a negotiated ceasefire is delayed by Ukraine's resistance.

Participants noted that while there is still room to escalate sanctions, it is equally important to think about deescalation: Only a limited number of sanctions will be considered for removal, but Russia will likely want to maintain control of Crimea and the separatists' republics and insist on demilitarization. Possibilities for sanctions relief will depend on Ukraine's veto power as the aggrieved party that has suffered billions of dollars of damage and civilian casualties. Ukraine may also require stronger US security guarantees, especially if it loses what Putin considers "Novorossiya" (i.e., Donbass, eastern, and southern Ukraine), some speakers argued.

Conversations also addressed that a negotiated outcome will also likely be subject to the United States' position on export controls and EU countries' insistence on assurances of territorial integrity. Even if sanctions are relieved by a negotiated settlement, some discussants noted, the self-sanctioning larger multinationals would be unlikely to return to Russia given the high risk premium, which could complicate the ability of the United States and other governments to negotiate away sanctions and guarantee relief in a future deal.

Russia versus the World

Participants discussed that two years post-invasion, the world may be dealing with an isolated, increasingly nationalistic, rogue, nuclear-armed Russia that poses a real threat to the international community. Similar to Iran, Venezuela, and other sanctioned countries, some speakers argued, Russia will likely have gamed out multiple contingency plans to weather increasingly dire scenarios by way of what one speaker called an "economy of resistance" (i.e., indigenizing key industries), but unlike the self-imposed isolation of North Korea, the Russian population may not be willing to fully cede their former way of life.

It is unclear how effective continued sanctions or foreign policy tools may be in the face of this more isolated, dangerous Russia. Sanctions relief may be a very tough negotiation given that speakers noted a broad perception that many sanctions on Russia, like those targeting corruption, were well deserved. They also argued that it may be hard for the US to threaten secondary sanctions against allies, despite previous success in enacting strict sanctions against Iran (for example, the SWIFT ban cut off nearly all Iranian banks).

One participant hypothesized that more binary geoeconomics may push Russia and China beyond their current transactional partnership toward a partnership of convenience, with a financially weakened Russia increasingly dependent on China to sustain itself in the global economy. However, others countered, China may not wish to taint its reputation by propping up a politically isolated Russia with pariah status. Some noted that Russia may also find some allies among non-G7 countries that remained on the fence in the early days of the conflict, and at some point "sanctions fatigue" may set in.

Developments more than two years in the future are even harder to predict: participants acknowledged that Russia has reemerged as an immediate threat to global security but wondered if in three to five years, the United States would shift its attention back to China. However, in the meantime, China and Russia may grow closer, albeit in an unequal relationship, with China continuing to prioritize its self-interest and agenda in an increasingly polarized world.

Ramifications for Energy Markets

Global oil, gas, and coal markets were already tight before the war started. Given Russia's key role as an exporter of oil, gas, and coal, a disruption of those export flows would further exacerbate the tightness and increase the level and volatility of commodity prices. The discussion focused primarily on the repercussions of high prices and volatility for Europe before moving on to discussing the impact on Russia and other countries and regions. The extent to which recent events shattered expectations and instigated an atmosphere of uncertainty stymied participants' attempts to predict future outcomes. Nonetheless, the difficulty of reducing Europe's energy dependence on Russia, the long timelines and heavy investments inherent to diversifying energy supplies, and the uncertainty regarding alliances in the future energy order were prominent themes throughout the discussion.

European Union

Conversations between energy executives and European officials underscored how unthinkable the current situation was. These discussants noted that the shock of Russia's invasion is pushing Europe to accelerate its efforts to reduce its reliance on Russian gas through emergency measures to meet energy needs, reduce demand, build-out alternative energy sources, and diversify away from Russian gas and oil.

First, speakers noted that Europe is pursuing emergency measures to protect energy security in the near future. Germany, France, and Italy have fired up hard coal, lignite, and oil units, with what one participant reported as 10 gigawatts that are ready to be ramped up. These emergency measures may temporarily increase emissions. Nonetheless, the plans to achieve net zero by 2050 are still in place as, if anything, the Russia-Ukraine war may yet accelerate Europe's energy transition. Additionally, several participants discussed Europe's efforts to reduce gas demand by replacing gas boilers with heat pumps or other technologies in countries like Italy, the Netherlands, Germany, and the United Kingdom; Italy's goal to take out household gas boilers by 2027 has been pulled forward to 2024 or 2025.

Next, Europe is further ramping up the build-out of low-carbon energy sources. Speakers identified numerous initiatives throughout the continent: The German government has pulled forward its target for achieving a 100 percent renewable power system to 2035, meaning it will have to invest even larger-than-planned sums in clean hydrogen and offshore wind. In Poland, this means the continuation of offshore wind and plans to build out small nuclear reactors. The British government will similarly expand offshore wind, solar, CCUS, and hydrogen projects. The French government has announced a massive rejuvenation of its nuclear program, while the British government may consider expanding its nuclear program as well.

The build-out of green hydrogen will likely accelerate with the crisis, speakers predicted, noting that the number of hydrogen facilities under construction is rising quickly. The coronavirus pandemic had already produced what participants perceived as a dramatic shift in the prospects for hydrogen, as governments poured substantial sums of recovery money into the industry. Roundtable attendees saw Belgium and the Netherlands as leading the development of hydrogen facilities, with participation from northern Germany, northern France, the United Kingdom, and Spain. Speakers also highlighted that green hydrogen is already price competitive with blue hydrogen.

Europe is seeking to diversify away from Russian gas and oil with renewed vigor. The European Commission laid out a proposal to lower imports of Russian gas by two-thirds (around 100 billion cubic meters [bcm]) by the end of 2022. Yet these plans are not the law, and member states are responsible for enforcement. But, according to several participants, achieving these targets this year or even in the next 36 months seems highly unlikely as the supply side is not adequate: Meeting this demand implies maximum output from all liquefied natural gas (LNG) export facilities in the world. One speaker observed that 100 bcm of LNG is the equivalent of China's annual LNG imports; another noted that an LNG cargo entering Europe cost buyers $100 million (at the time of the roundtable), a price that is not sustainable regardless of subsidies, meaning demand has to fall if Europe is to reduce its imports of Russian gas.

Attempts to ensure European gas supply in the short term have also sparked international outreach. Participants highlighted several announcements: The United States said it will provide LNG. The Qataris are planning to dramatically increase their LNG supply, although this increase is notably three years away. Meanwhile, Japan has attempted to shift LNG to Europe. The Algerians are trying to repurpose gas used for enhanced oil recovery to boost natural gas supply. Yet the acceleration to build new capacity and secure non-Russian gas and oil may take roughly three years, estimated one speaker. Furthermore, to increase LNG imports, Europe will have to sign long-term contracts as new LNG sellers will not start producing without some level of guaranteed offtake. Roundtable members pointed out that the focus on decreasing gas in the name of decarbonization leaves a weak incentive to deliver natural gas.

The cost of Europe's shift may exacerbate inflation, some attendees cautioned. The goal of raising LNG imports by 50 bcm is putting significant pressure on gas spot prices. Prices like \$30–40/mmBtu (observed in the two weeks preceding the roundtable) make LNG imports extremely expensive for Southeast Asian countries like Thailand and Vietnam. While Europe's decarbonization transition will continue, the war may derail efforts in other countries in the short term, a speaker suggested, noting that China's intention to take its coal gasification program offline has already become unaffordable.

Receiving these LNG imports also requires further developing Europe's LNG import capacity, and discussion turned to plans to address these infrastructure demands and the challenges they may face. The construction of several LNG terminals has been announced in Germany, Poland, the Netherlands, and Italy. Other projects, like the MidCat pipeline between Spain and France, would also address important infrastructure bottlenecks but will take years to complete. Participants surmised that operational costs would rise not only because of higher transport costs but also due to capital expenditure increases for new infrastructure, and these effects would be exacerbated by rising interest rates that increase the cost of debt finance.

In the end, a core question roundtable members examined is whether Europe will stop importing Russian natural gas. One speaker argued that the question is not on the Russian side but on the European side. Since the beginning of the invasion, they noted, the combined incremental LNG and gas from Russia entering Europe had only increased, as Russia actually began moving more gas through Ukraine.

Russia

As the discussion continued, one speaker focused on the implications of the war for Russia. The speaker argued that Russia made a conscious calculation that even without exports to Europe, where it currently exports about 48 percent of its oil and refined products, the regime could sustain itself on the cashflow from remaining revenues in the short term. Furthermore, the speaker continued, in 2021, Russian oil and gas revenues hit historic highs, suggesting they have some reserves. Nonetheless, the bet on the remaining revenues operated on the assumption that China, India, and other non-OECD countries, already struggling with high oil prices and the effects of the COVID-related recession, would buy oil at prices of \$20–40/bbl, the speaker argued, meaning these countries would likely buy cheap Russian gas and coal that finds no other market. This speaker anticipated that the global energy markets will increasingly split between those pursuing a climate agenda and those willing to profit off of Russian fossil fuels: in short, Russia anticipated diversification.

Regarding the nature of sanctions on Russian natural gas, another speaker described two models. In the first model, sanctions would focus on restricting flows. In the second, sanctions would restrict access to revenues. According to this participant, denial of revenues may be more effective in punishing Russia by limiting its ability to facilitate trade finance, but the danger of restricting revenues is that Russia could turn off the taps due to the perception that they are giving away gas for free. This conundrum makes the question of implementing sanctions on natural gas complicated. Speakers noted that China will likely heavily resist Iran-style sanctions on Russia because it imports both Russian pipeline gas and LNG.

Russian pipeline gas and LNG will increasingly flow to Asia, participants argued, citing Russian infrastructure projects as evidence for the pursuit of this diversification. Russia would like the flexibility to decide between moving gas to European or Asian markets. For example, one speaker highlighted Gazprom's announcement of a technical study for the Power of Siberia 2, which would travel through Mongolia to bring gas from the fields of Western Siberia to China. Construction projects like this one would face challenges as some technologies are not produced domestically, though speakers suggested that these obstacles will likely be solved by Asian suppliers. Roundtable members saw Russia's interest in China evidenced by the exceptionally low natural gas prices for gas flowing through the Power of Siberia Pipeline.

China

The discussion also shifted to China's point of view. One speaker argued that China had not signed up for Power of Siberia 2 nor for the Sakhalin Pipeline. This discussant noted that China would like Russia to pay for Power of Siberia 2, and there is currently no financing agreement. As Chinese banks have not provided money for Power of Siberia, the participant argued, they likely will not finance the Sakhalin Pipeline either, and instead, China may focus on Central Asian gas. The speakers disagreed on whether China's presence in Central Asia would decrease Russia's influence there.

Japan and Asia

Roundtable members considered that Europe's higher LNG import needs could have a strong effect on prices but expected Japan and Korea to manage, given that they are used to paying high prices. Yet participants debated the question of whether Japan will continue using Russian LNG. Speakers noted that Japan plays a significant role in financing LNG projects in Southeast Asia, in part due to regional hesitation to take Chinese financing, so Japan's stance will be significant for the future of LNG development in Asia. Furthermore, participants concluded, the extent to which Asian countries more broadly choose to invest in renewables and efficiency, meaning whether they follow a similar path to Europe, will be significant for LNG markets.

Middle East

One speaker framed the current developments as a reordering of the global energy order, focusing on OPEC states, whose relations with Russia remain an open question. They noted that the Gulf States have shown support for Russia by failing to condemn the war and by not joining in sanctions or taking advantage of Russian weakness. Participants viewed Saudi Arabia's decision to switch to the yuan as a significant gain for China, especially with the question of switching from the dollar to the yuan rising broadly in the Middle East.

Conclusion

The closing speaker noted that the shock of the invasion may create pressure to resolve some chronically difficult problems, such as siting and permitting for power transmission in Europe. The discussion highlighted the question of whether the current situation will fundamentally change the energy landscape moving forward. As the war unfolds, there will be more scope for discussion. The question of whether this crisis will accelerate or hinder the energy transition in Europe and in the rest of the world remains.

Notes

1. European Commission, "REPowerEU: Joint European Action for more affordable, secure and sustainable energy," March 8, 2022, https://eur-lex.europa.eu/resource.html?uri=cellar:71767319-9f0a-11ec-83e1-01aa75ed71a1.0001.02/DOC_1&format=PDF.

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She has served on the Board of the Young Women's Council of the High Water Women Foundation, was a mentor in Girls Write Now, Inc., an Amplifier for Girl Be Heard, and member of the Grants Advisory Committee of The New York Women's Foundation. She is currently a member of the Steering Committee of the Women's Foreign Policy Group (WFPG) Young Professionals Network.

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