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# The oil cap price works, and so will its extended version



Enough time has passed since the introduction of the oil price cap on Russian oil almost two months ago, for the most important effects to be visible. The oil price cap imposed on Russian oil by members of the G7 and the EU has been working.

If it were different, the same group of the most developed economies would probably have abandoned this mechanism, or would have modified it.

However, the same model that has been applied to Russian crude oil will be extended to Russian oil derivatives, diesel, kerosene, and fuel oil, from February 5.

"I am encouraged we will be able to come to agreement by Feb. 5", said US Treasury secretary Janet Yellen in South Africa, during one of the stops on her African tour.

An important part of her talks with African partners, whom the US had been neglecting for a long time, concerned the implementation of sanctions against Russia. In the eyes of Moscow, many African countries are ideal partners for circumventing Western sanctions, particularly when it comes to oil.

The agreement between the G7 and the EU, which Yellen has been talking about, could be reached on February 5, when the implementation of the European package of sanctions against Russia, which prohibits the import of oil into Europe by sea, will begin.

If the already existing oil price cap on Russian crude oil is extended to oil products with the new agreement, it will be a very strong additional blow to Russian finances, and thus to its ability to wage an aggressive war against Ukraine.

The previous oil price cap on crude oil limited the price of a barrel to 60 US dollars and introduced restrictions on services accompanying Russian exports, primarily on transport insurance.

## The Russian budget is bleeding

Finland's Centre for Research on Energy and Clean Air has calculated the amount of "bleeding" from the Russian budget due to the current oil price cap after two months of implementation.

Their assessment says that the Kremlin loses as much as 172 million dollars a day because of the oil price cap.

If Western governments extend restrictions on Russian oil derivatives from February 5, the daily deficit of the Russian budget will increase to as much as 280 million US dollars per day.

The political Kremlin, understandably, does not recognise the colossal shortage of cash, so Putin's spokesman Dmitry Peskov said that "as far as the losses are concerned, no one has especially seen the caps yet".

However, the economic Kremlin cannot hide the obvious, so Finance Minister Anton Siluanov admitted that the country's budget deficit in 2023 might exceed the expected 2% of GDP as the oil price cap takes a hit on export income.

The Governor of the Russian Central Bank, Elvira Nabiullina, expects that Russia's cash flows will probably weaken considerably in 2023 as oil and gas sales to Europe plunge.

## There is no profit in alternative markets

Under the blows of Western sanctions, and the oil price cap, Russia has been frantically looking for a solution to the collapse of its main resources for filling the budget, primarily oil and gas.

Due to the embargo on oil exports, and then the cessation of gas imports from almost all European consumers, as well as the oil price cap, the drop in Russian profits on energy products could be even greater than 50%, as estimated by the Ukrainian Ministry of Finance.

Turning to large Eastern markets, after the blockade and restrictions in the West, is the only way out for Russia, but will not bring the desired compensation.

Precisely because of the oil price cap, the sale of its oil has been growing in the large markets of Asia, primarily China and India, but the financial effect is getting worse. Big buyers in the east are getting big discounts - more than 30 dollars per barrel - cheaper than Brent crude.

Russia simply cannot find an alternative in Asia for its lost European market, to which it exported more than 3 million barrels per day before the aggression against Ukraine.

The costs of transportation to distant Asian markets have been much higher, and the selling price has also been reduced by Western restrictions on transport insurance, because companies from G7 members provide as much as 90% of services in international maritime oil trade, including insurance and reinsurance.

## An unreliable, dangerous and illegal supplier

This forces Russia to reach for the "shadow fleet" of oil tankers. In the last year alone, Russia bought more than 100 tankers, through unknown companies: probably Russian-owned shell companies, says the study by Ben Cahill from the Centre for Strategic and International Studies (CSIS).

Considering that most of these ships are near the end of their lives, it is only a matter of time before some of them cause an environmental disaster.

In addition to the fact that international transport is carried out without the usual insurance, all these factors make Russia an unreliable and dangerous supplier, operating on the edge of legality.

If "Oil price cap 2" is agreed by February 5, as expected according to announcements of

Western governments, the space for Russian manoeuvring on the global oil market would be drastically narrowed; possibly even closed.

The previous model meets the goal of painfully reducing the Russian budget, as the source of its aggression against Ukraine, while simultaneously not harming the global supply.

"As oil prices have come down, there's no doubt that the price cap has, so far, and there's a long way to go, achieved our interest, which was to have continued supply of oil on the market to support economic growth while limiting the value that oil makes for Putin", said Amos Hochstein, special presidential coordinator to the US President Joe Biden, for CNBC.