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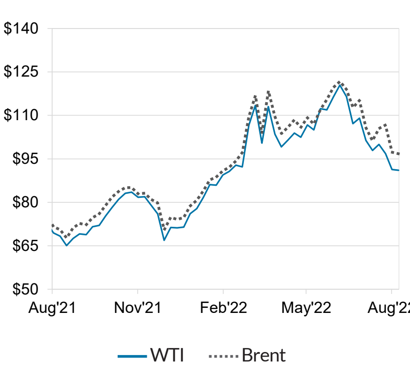
BRENT, WTI PRICES 2021-22 ($/bbl)



Source: CME, ICE

THE BIG PICTURE

Russia's Great Gas Rearrangement

- *Boosting domestic consumption and diversifying exports underpin Moscow's new energy strategy as the EU seeks to phase out Russian gas imports by 2027.*
- *Both will require major investments, and domestic sales will bring lower returns to Gazprom.*
- *Moscow may need to find a new home for roughly 130 billion cubic meters or more — assuming some EU slippage and continued Turkish purchases.*

Russia is minimizing gas exports to Europe as part of a pressure campaign on Brussels amid the war in Ukraine. A full cutoff right now brings revenue and leverage risks to Moscow. But longer term, Russia needs a plan to replace sales to the EU, even if its expectation is that Brussels will fail to reach its ambitious 2027 target.

It's speculation to predict precise volumes of exports to Europe in the long term, said Sergei Kapitonov, a gas analyst at Skoltech Project Center for Energy Transition and ESG in Moscow. But with that in mind, Turkey, the Balkan states and in the EU, Hungary and possibly Austria and Germany, could still be using Russian gas even after 2030 due to economic reasons — with Turkey probably the only less politically dependent market, he noted. And if and when the conflict resolves, Russia may use its short-term instruments to stay on the EU market as a supplier of last resort in times of gas deficit or price hikes.

The EU's 150 Bcm of imports last year accounted for 30% of Gazprom's and 20% of Russia's production — or nearly 70% of pipeline gas exports and some 60% of Russia's total gas exports, including LNG. Turkey separately imported some 25 Bcm of Russian gas in 2021, accounting for the bulk of Gazprom's roughly 30 Bcm in non-EU westward exports. Toward that end, according to the Russian oil and gas veteran, former Energy Minister Yuri Shafranik, Europe could still be taking 35 Bcm-45 Bcm annually in 2030. That could leave some 130 Bcm or more seeking alternative markets.

A new 2050 energy strategy is expected to be drafted by mid-September, centering on developing the domestic gas market and building out alternative export infrastructure. Replacing European exports is critical to filling state coffers: Gazprom revenues were at a record high of $10 billion per month in the first half of 2022. It is also critical to extending the lives of mature gas fields in West Siberia, around which cities were built in the region in the 1970s.

Domestic Potential

In the near term, domestic demand hardly offsets the drop in gas exports to Europe and will likely decline because of an expected economic slowdown amid Western sanctions. Metals, automotive and other industries are already feeling the pressure of restricted export and import opportunities, which will contribute to this year's expected 5% decrease in power generation, a large consumer of natural gas. That

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said, Moscow intends to spend 800 billion rubles ($13 billion) over 2021-25 on expanding the gas grid, including in frontier eastern regions with historically low gas penetration rates.

Based on Gazprom estimates last year, Russia had hoped to increase domestic consumption by at least 18.6 Bcm/yr by 2025 through the expansion of the gas grid. Moscow now seeks to accelerate the grid expansion project, Deputy Prime Minister Alexander Novak has said. With new industrial consumers, sparsely populated east Siberian and far eastern regions might consume up to 30 Bcm/yr in the long term, he said. The Murmansk region in northwestern Russia, which also lacks gas pipelines, might add 8 Bcm/yr to consumption if it switches from fuel oil to gas, according to participants at a recent meeting of the State Duma energy committee.

Iran's booming domestic gas consumption shows what's achievable under sanctions, but "Russia's domestic gas market is a well-balanced one with only a few potential points of growth," Kapitonov noted. These may include the expansion of LNG use for bunkering in the Arctic, gasification of coal-dependent cities and possibly more use of gas in steelmaking sector and petrochemicals, he said, although sanctions could constrain gas use in technology-dependent industries such as petrochemicals. Should that industry take off, it could potentially replace some $30 billion per year of petrochemicals imports, Shafranik said.

Revenue Pain in the Picture

New sales into the domestic market will hardly generate similar revenues to those in Europe, which has traditionally been a higher-margin market. Gazprom's exclusive right to export pipeline gas at higher prices has been widely seen as a reward for the socially oriented mission to ensure stable supply at regulated and relatively low prices at home. Indeed, with low gas prices for residential consumers having that social component in Russia, unpopular steps to raise prices at home are not expected in the short- to medium-term period, notes Kapitonov.

Taking that into account, Gazprom instead might get the right to set flexible prices for industrial consumers at home, the State Duma energy committee suggested. While this would help replenish the coffers of Gazprom, the Kremlin's cash cow, it could also result in higher costs for its clients and spur inflation.

China in the Driving Seat

Russia has two pipeline contracts with China for a total of 48 Bcm/yr — with exports this year to reach 15 Bcm/yr on the 38 Bcm/yr Power of Siberia line. Gazprom says it can supply up to 130 Bcm/yr in the future. But some experts believe that although Beijing might be interested in cheap Russian piped gas, it might be cautious about deepening ties with sanctions-hit Russia. Chinese investment in Russia under its Belt and Road scheme fell to zero in the first half of this year, while Chinese lenders could struggle to recoup their investments in Russia as planned.

China will also likely use Russia's growing isolation as leverage in gas price talks in any new contracts with Russia, further reducing margins on expensive export pipeline projects. February's 10 Bcm/yr supply deal, on which details are scant, was likely pushed through by politics and Russia's need to demonstrate it has friends outside the West.

Russia is meanwhile sticking to plans to expand LNG exports to up to 140 million tons/yr by 2035, up from 30 million tons/yr currently. But these look unrealistic amid EU sanctions banning the export and transit of key liquefaction equipment, while foreign engineering contractors, including Technip Energies and Linde, are withdrawing from Russian projects. Moscow has yet to develop its own LNG technology and competence at scale.

For now at least, revenue pain is a future worry. Gazprom is currently exporting at its lowest levels to Europe since the late 1970s-early 1980s but reeling in historically high earnings, Kapitonov pointed out. But longer term, Russia's gas will need to find non-EU markets at scale. In contrast to the rerouting of oil exports, these alternative gas markets will require significant investment to reach — and won't likely be as lucrative.

Staff Reports

MACRO TRENDS

Russia Accelerates Dollar/Euro Ditch, But Move Has Limits

- *Russia is now receiving payment for some of its oil in non-Western currencies, including the yuan, United Arab Emirates dirham and ruble.*
- *This is a central part of Russia's decoupling from the West and closer alignment with "friendly" countries from Asia and the Mideast.*
- *But Russian exporters fear they could be burdened with currencies that are not fully convertible, creating liquidity headaches and conversion costs; neither does the move fully insulate Russia from US sanctions' reach.*

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The Issue

Buyers of Russian oil are being asked to pay for their barrels in new currencies, as the "toxic" dollar and euro lose their luster for Moscow, while some customers' euro payments are being converted, at a punitive rate, into rubles. This is all part of Russia's strategy to "de-dollarize" its economy, and more broadly weaken the influence of the dollar. Analysts warn, however, that Russia's future dependence on currencies that are marginal in global trade could inflict long-term economic damage. It may also fail to offer full protection from US sanctions.

Friends vs. Enemies

The shift to alternative currencies like the yuan and dirham will accelerate in the run-up to Dec. 5, when the EU embargo on Russian crude imports comes into force, with a ban on product imports to follow two months later. Russia's Central Bank is currently mooting requiring state-controlled companies to transfer funds in currencies from "unfriendly" countries — i.e. the US and EU member states — into currencies from "friendly" jurisdictions, such as China and India, which have no interest in punishing Moscow for its war with Ukraine. Russia's thinking is that the negative impact of this currency switch will be minimal, as it will have much less need to pay for imports in dollars or euros because of sanctions.

This month, the Central Bank described de-dollarization as "inevitable" and stressed the need for all industries, not just oil and gas, to collaborate in the effort. All Russian exporters are now under pressure to start using other currencies, with an implicit threat that they will face repercussions if they don't play ball. "This is very serious, nobody is messing around here," a Russian industry source says. "It's a pain, but what can you do?" He points out that state-controlled Rosneft switched entirely to euro payments from dollars several years ago.

Return to the Ruble

In parallel with this currency switch, Russian oil exporters are starting to receive payment in rubles via a two-step procedure that involves initial payment in euros or dollars, at a designated Russian bank, after which they are converted into rubles. This system is already being used by European importers of Russian gas.

A longtime trader in Russia says he was told by a state-controlled company to pay for all his oil in euros at a European branch of Gazprombank, and then have the euros converted into rubles, at a hefty rate. "These were the instructions, we had no choice in the matter," he says, complaining that the cost of the conversion works out at around $8-$10 per ton. Gazprombank could not be reached for comment.

Other buyers of Russian oil are separately grappling with the inconsistencies with EU sanctions. "You can buy a cargo of Russian oil from Rosneft via a UAE company, and send it to Europe, but you can't charter a Russian ship. There are obstacles wherever you go and none of it makes any sense."

Currency Surplus, Sanctions Risk

If, as expected, Russia receives most of its oil payments in non-dollar/euro currencies, what will they do with all this money? Among Russian exporters, there is a fear that they will be left with a surplus of cash that they can't convert into dollars or euros. "What can we do with yuans?" asks one.

Russia may study the example of Iran, which was forced by US sanctions to phase out the dollar and euro and sell its oil to China and other countries in their own currencies. The problem for Iran is that this limits it to trade with those countries, while some is still stuck in overseas accounts. Russia could face similar trade constraints.

China is the one to watch "for providing currency liquidity at scale," says Rachel Ziemba at the Center for New American Security, while questioning China's willingness to extend that role to third parties. The UAE dirham has limitations, she says, as it is pegged to the US dollar and is not widely used outside the Mideast Gulf.

Ziemba also questions Russia's ability to cut itself off completely from the dollar. "There's still a limitation of cross-border, non-dollar, non-G10 payment systems at scale, which limits Russia's ability to completely insulate themselves." (Countries home to so-called G10 currencies are largely aligned on Russia sanctions.) Most currency trade touches the US system, even if briefly, today. "There are signs that's shifting," she said, but there's still not a "lot going from emerging market currency 'X' to emerging market currency 'Y' without touching the US system." That leaves Russia vulnerable to possible future US secondary sanctions.

De-Dollarization Limits

A longer-term and much more ambitious goal is to weaken the role of the dollar globally and encourage other countries, such as China, to de-dollarize. In June, President Vladimir Putin spoke of the need to have a new international reserve currency based on a basket of non-Western currencies at a meeting of the Brics countries — Brazil, Russia, India, China and South Africa.

The response to his proposal has been muted, and progress toward global de-dollarization or a new reserve currency is expected to be slow, given the dollar's considerable advantages — not least its dominance in forex and commercial trade, hedging opportunities and the US financial system's transparency.

And while the tensions following US House Speaker Nancy Pelosi's visit to Taiwan increase China's incentives to "reduce its exposure to US payment system," China at the same time "is not going to stop exporting to the US or be willing to put that in jeopardy short term," says Ziemba. Further, for Beijing, "having a more international currency means losing some control," she adds. Among other measures, China has controls on capital outflows in place.

Paul Sampson, London, and Emily Meredith, Washington

GEOPOLITICS

New Hopes, Old Fears Over Draft Iran Nuclear Deal

- *EU foreign policy chief Josep Borrell announced Monday that a new round of hastily convened talks in Vienna to revive the 2015 Iran nuclear deal had produced a final text, which leaders in Tehran and Washington are now deliberating.*
- *Whether they choose to accept the draft agreement in the coming days or weeks could have profound implications for oil markets and Mideast security.*
- *The EU's push to seal a new deal reflects the gravity of the energy crisis Europe is facing.*

The Issue

An apparent breakthrough in efforts to resurrect the nuclear deal is the latest peak in a 15-month roller coaster. It may be the last: Borrell says the space for additional significant compromises has been exhausted. Several key areas of disagreement remain, although they are understood to be narrow. But the decision-making endgame takes place in a particularly challenging geopolitical context.

Tehran's ties with Russia have visibly strengthened lately, while US-China relations are in the deep freeze over Taiwan, and in Washington, the Iran nuclear deal is a politically polarizing issue as midterm elections loom. All complicate the outcome.

'Whac-a-Mole'

Painstaking efforts by the EU mediation team have succeeded in closing the gaps, with Borrell saying the latest indirect negotiations between the US and Iran fine-tuned the text and addressed a handful of remaining issues. Iran seems to have eased off on its demand that the US remove the Revolutionary Guard's designation as a foreign terrorist organization — a key former stumbling block — although Iranian state media last week denied this. There has also reportedly been progress on guarantees that Iran will benefit economically from the lifting of sanctions, another thorny issue. The so-called safeguards probes by the International Atomic Energy Agency (IAEA) into Iran's undeclared nuclear activity dating back decades have instead emerged as the main obstacle to reaching an agreement, even if technically unrelated to the nuclear deal, or Joint Comprehensive Plan of Action (JCPOA). Also unclear is how the final text proposes to resolve the question of expiring "sunset" clauses — nuclear-related sanctions that are due to start coming off from 2023 under the original deal, even though Iran's nuclear program is far more advanced than it was.

Nothing is assured, and Borrell warned that "behind every technical issue and every paragraph lies a political decision that needs to be taken in the capitals." A State Department spokesman said the US is ready to quickly conclude a deal based on the EU's latest proposals. The administration of US President Joe Biden certainly has an interest in helping Europe with the oil price fallout from efforts to isolate Russia, although that doesn't necessarily translate into a willingness to agree on significant compromises. But the fragile consensus around the nuclear deal in Tehran means it is still unclear what Iran will decide.

Mohammad Marandi, a professor at Tehran University who has worked with Iran's negotiating team, underlined the safeguards issue. "One thing is certain," he told Energy Intelligence. "The IAEA board of governors' accusations against Iran must be closed before the implementation of a deal."

Western Pressures, Eastern Pivot

Russia's moves to tighten ties with Tehran in response to intense sanctions pressures from the West have strengthened Iran's hand in the negotiations. President Vladimir Putin's comments on his visit to the Iranian capital last month about closer cooperation on energy, industry and transport, and the memorandum of understanding between the National Iranian Oil Co. and Gazprom, potentially worth $40 billion, are proof for some that Iran can cope fine with US sanctions. Moscow is also interested in Iran for its so-called North-South transport corridor megaproject.

Others remain doubtful about the prospects for greater Russia-Iran cooperation absent US sanctions relief and are skeptical that Iran's defiance of the West is a sustainable strategy. "Iran has been hoping that a pivot towards the east would strengthen its political and economic position in the international community for over a decade now," Esfandiyar Batmanghelidj, founder of economic think tank Bourse & Bazaar, tells Energy Intelligence. "I think the Iranian experience of working with Russia and China has been one characterized by disappointment." State-owned energy firms from both countries froze or withdrew from upstream investment in Iran on the return of US sanctions.

Aligned Incentives, Differing Ideologies

Borrell has stepped up his efforts in recent months to get Iran back into compliance with the JCPOA, emphasizing his determination to see Iran reap the economic benefits of doing so. With Russian crude subject to an EU import ban (and Russian shipments to an insurance and financial services ban) from December, Europe would no doubt relish the chance to resume purchases of unsanctioned Iranian oil, seen as a good alternative to Russian Urals (p6). From Iran's perspective, the benefits windfall oil revenues would bring to its weakening economy are obvious, notwithstanding the risk that a Republican victory in 2024 US presidential elections means those revenues could be short-lived. Under a revived deal, Iran would also regain access to frozen foreign reserves worth around $100 billion.

"The problem, I think, is that although there is a degree of clarity among Iran's economic decision-makers, it is probably a smaller aspect of the decision-making for this administration than it was for the previous administration," says Batmanghelidj. "For this administration, I think what is of greater concern is essentially ... the political appearance of this deal and how it comes about."

Russia's direct interest in facilitating a revived JCPOA, as another important party in the negotiations, is less clear. Besides displacing Russian barrels, a deal promises to ease the energy price pain in Europe that benefits Russia. But sanctions removal could also allow for deeper Russia-Iran (and China-Iran) investment, with Western firms likely to exercise caution for fear of a US reversal. The deal also offers potentially huge security dividends in the Middle East region, where Iran has already initiated talks with Saudi Arabia. The alternative could see a return to the heightened tensions between Iran and its rivals and tit-for-tat strikes witnessed after 2018. That is hardly in Russia's interests either, given that it has become ever more involved in the region over the past decade.

Simon Martelli, London, Oliver Klaus, Dubai, and Emily Meredith, Washington

POLICY

The US' Fresh Climate Outlook, Credibility

- *US lawmakers are advancing legislation that will spend heavily to reduce greenhouse gas emissions by some estimated 40% over 2005 levels, driven by reductions from the power sector.*
- *After years of US climate policy swinging wildly, the congressional effort to subsidize deployment of clean technology puts US energy policy on firmer footing for the next decade.*
- *There is still a gap when it comes to what US President Joe Biden has pledged to do and what lawmakers are willing to agree to.*

The Issue

The US House of Representatives is on the cusp of passing landmark climate legislation alongside tax and health measures in the Inflation Reduction Act, a bill Biden is expected to sign once it reaches his desk. It's an about-face compared to the situation just weeks ago, when Democrat Sen. Joe Manchin's apparent dismissal of the bill left climate action essentially limited to executive actions vulnerable to reversals. US negotiators will have a stronger hand going into international climate talks this fall, although the provisions in the bill aren't expected to fully deliver on the Biden administration's pledge to reduce emissions by 50% by 2030.

Nuts and Bolts

Overall, the bill is structured around the idea that the electricity sector needs to be decarbonized while the economy is electrified. There are substantial incentives aimed at deploying additional renewables and clean energy, with most projected emissions cuts coming from the power sector, said Rhodium Group's John Larsen. In addition to credits for solar and wind, hydrogen gets new cash, on a sliding scale based on its life-cycle emissions. Credits for carbon capture increase, with a new cap for pricey direct air capture of $180 per ton. There are also new incentives for nuclear power. To try and widen the scope of the credits, nonprofits and other entities that typically don't pay federal tax can receive the renewables credits as direct pay. That could help some municipal and similar organizations deploy renewable energy.

To reduce consumption, there's money aimed at transportation, manufacturing and buildings. There are incentives for sustainable aviation fuel and electric vehicles (EVs), including for medium- and heavy-duty vehicles. A $4 billion program is aimed at deploying energy efficient appliances in homes, with thousands of dollars in rebates available for people to replace gas-fired heating, water heating and cooking appliances with electric versions. And there's money for the federal government to shift how it does procurement: appropriations for its own EV purchases and to procure low-carbon steel and cement for buildings — an effort at underpinning government programs aimed at helping to foster a market for those industries.

The Home Front

The bill — along with a semiconductor chip manufacturing bill that Biden signed this week — also functions as an industrial policy of sorts, with some of the credits tied to manufacturing in the US or free trade agreement countries, or using labor that meets certain pay and training requirements. The focus on homegrown innovation also serves to bolster competitiveness vis-a-vis China, a key Biden administration aim.

The tax credit for clean energy production, for example, increases by 10% for projects that meet a domestic content requirement. EV credits are very dependent on where the vehicle is manufactured. By 2028, 80% of the minerals in the EV battery must come from North America to qualify for half of the $7,500 credit. To qualify for the second half, 100% of the battery components must be manufactured and assembled in North America.

In a further nod to supporting domestic supply chains, the legislation gives the administration $500 million to spend over the next two years in areas where the Defense Production Act has been invoked — something the White House has done with respect to battery supply chains and heat pumps, although there aren't specific parameters in the bill.

Keeping (Some) Oil and Gas on Side

To reach a compromise with key swing lawmaker Manchin, Democrats included guarantees to lease federal land for oil and gas drilling and reinstated leases that were tied up in the courts. That might be aimed at assuaging vocal industry critiques that federal leasing and permitting is too restrictive, although the bill also increases royalty rates and introduces other changes that could make leasing more expensive.

Criticisms from green groups have been muted. That might be because the bill's overall greenhouse gas reductions are expected to far outweigh any increases from additional leasing. Robbie Orvis at Energy Innovation, which has done extensive modeling on federal energy policies, said his group's projections show that for every one additional ton of greenhouse gas emissions added by the leasing requirements, 24 tons are avoided by the other elements of the bill.

Significantly for industry, the bill's incentives for carbon capture and hydrogen align federal programs with the transition plans of big oil firms such as Occidental, Chevron and Exxon Mobil. Smaller firms have more to worry about with respect to a methane fee that serves as a backstop for forthcoming regulations and an increase in corporate taxes.

Making It Stick

Reassuring the world that this time climate policy is here to stay will be critical for the US to regain credibility on international climate talks. Going into Glasgow talks last year, legislation appeared to be in the offing, helping negotiators make their case. "Unless you can walk the talk, people look at you and say 'that's nice, let me know when you've done something,'" then-US climate negotiator Jonathan Pershing told Energy Intelligence last November. But the legislative efforts collapsed shortly after. Combined with Supreme Court decisions on the power sector and regulation that enhance the vulnerability of executive actions, Washington would have had a thin case to make on the international stage come COP27 in Egypt.

Lawmakers are now deploying some tactics to minimize the potential whiplash. For example, if a new administration were to roll back methane regulations, companies would no longer be able to get an exemption and would have to pay the methane fee outlined in the bill. And the massive spending package itself serves as reassurance. Not only is the US pledging to deploy low- and zero-carbon technologies at home, deployment could make those technologies more scalable elsewhere.

Emily Meredith, Washington

POLICY

EU Ban Puts Tankers on Collision Course

- *An EU ban on insurance and financing for tankers that carry Russian oil come winter will make it near impossible for many shippers to move this oil.*
- *Moscow and friends could try to assemble a fleet of non-Western tankers, which could perhaps handle much of Russia's crude, but not the refined products.*
- *The EU is discussing a possible loophole, in which tankers could carry Russian oil if bought at a discount under a potential US-backed "price cap" — but traders still see a supply crunch in the making.*

An EU shipping insurance ban is creating a huge obstacle to export Russian crude oil and refined products a couple months from now. This could create massive price spikes for oil worldwide, on top of expensive natural gas. Under the ban, Russia's total 5 million barrels per day of seaborne fuel exports — 3 million b/d of crude oil and 2 million b/d refined products — must be shipped on tankers without any ties to EU insurance and financing. But the bulk of the world's fleet has ties to the EU — and UK — banks, brokers and insurers. Brokers say there won't be enough tankers to handle Russia's oil.

That's not all. The world is facing a double conundrum. The shipping ruling accompanies another sanction that bans most of Russian crude and product imports into EU countries — impacting the 2 million b/d that still flows from Russia to the EU. Russia has already diverted some 1.5 million b/d of crude and products that no longer goes to the US, EU and UK and now mainly sails to India and China. But Russia must find a new market for the remainder. Even if new buyers appear, tankers are the bottleneck to get the oil to market.

Some assess that 80% of the global vessel fleet is connected directly or via reinsurance to Western companies that ultimately connect to Lloyd's in London. Sources say Lloyd's, even absent parallel UK sanctions as yet, will have to align with EU rules. Says one UK insurance official: “Obviously Lloyd’s has European partners. And we are subject to all the sanctions regimes there are and have to abide by all of them, of course. It gets very complicated.” The US Treasury Department reckons that 75% of Russian product exports via its European ports are still linked to the Western financial system.

Loop the Hole

Three scenarios can develop between now and December (for crude oil) and February (for refined products) when the two-step import and insurance bans take effect. Perhaps the most obvious but politically hard-to-stomach option is for the EU to abandon the insurance ban and avoid lower Russian exports that would tighten balances, especially for refined products. The EU’s whatever-it-takes approach to punish Russia for the war can cause price spikes or rationing for oil products, on top of historically high natural gas prices. Dropping the ban would be a massive crack in the alliance against Russia. But keeping it in place might destabilize EU governments, undermine support for the anti-war effort, and deepen inflation and an expected economic recession.

To keep oil flowing, the US is driving an effort to allow shippers the use of Western insurance and financing if traders buy Russian oil at a price set by members of the G7 and allies. The price cap — higher than cost but lower than market value — should limit Russia’s oil income. The US, UK, EU (with France and Germany G7 members), Canada, Japan and also South Korea are mulling a system with flat prices for oil and products. An EU official says that “ensuring the security of energy supply worldwide is a key priority.”

For now, the EU thinks a price cap is the way to go. Traders, however, don’t see it working and think it can be undermined with bogus paperwork — one paper showing the capped price, another paying the Russians extra money under the table. Russia has signaled it would make the plan fail and could limit supply.

A Darker Way

A third option is that Russia and other nations like China and Iran link up their fleets and get certification, insurance and finance outside Western financial networks. Western brokers call this a dark fleet, as tankers at times also conceal where they are. Such a fleet would divorce the trade from the direct impact of sanctions. Already, Russia’s state-controlled Sovcomflot (SCF) has been putting its substantial tanker fleet out of direct reach via intermediaries that register vessels outside Russia. It opened an office in Dubai in November. SCF said it’s a vital part of its “fleet management system.” Much of the Russian oil trade moved there as well. SCF was forced to sell and reflag a number of its ships from Russia to Liberia or Cyprus after US sanctions. Iran also has a large fleet that operates outside the Western system. China, among others, could join.

A London shipbroker thinks Russia, or others, could create new companies that buy old tankers and sail them with sovereign insurance and financing. By pooling non-Western vessels, Moscow might be able to get much of the crude to market via ship-to-ship transfers in Europe or off Morocco, but not the products, is the broker’s assessment. Efforts to go outside the Western system are growing. In recent months, India has started certifying SCF vessels for safety and seaworthiness. This is required by insurance companies (including non-Western insurers) to cover the risk of a cargo — which can be worth $200 million on board a very large crude carrier, and cause billions of dollars in damage in case of a spill.

Abandon Ship

The plethora of sanctions, from the US, EU and UK, makes it hard for Western shipping companies to decide if they can carry Russian cargoes — even now. Dozens of companies and individuals have been sanctioned and cannot be dealt with. They could be connected to a cargo of oil. The London broker says there are two camps of shipowners. One has stopped loading anything Russian. It doesn’t want to be caught in the net of sanctions as the smallest oversight can result in financial punishment. The other takes a more pragmatic approach: If the insurance company approves the cargo, the ship will carry it. “No legitimate company will sail a cargo without insurance,” the broker says.

John van Schaik, New York, and Rafiq Latta, Nicosia

CLOSING ARGUMENTS

China's Taiwan Gameplan, Turkey's Russia Tilt

China: Clear Statement on Taiwan

The Chinese reaction to US House Speaker Nancy Pelosi's visit to Taiwan continues to evolve, with the Chinese military announcing that it has "successfully completed" the tasks set out for a series of military exercises surrounding Taiwan. These drills had taken on the characteristics of a de facto air and naval blockade that appeared to be designed to pressure the Taiwanese government into capitulating to China's demands that it politically integrates itself with the mainland. While the major exercises have now ended, the Chinese military has declared that it will continue to monitor the situation — and to maintain its combat readiness.

Beijing has indicated that while it continues to seek "peaceful unification" with Taiwan, it "does not pledge to relinquish the use of military force and retains all necessary options" when it comes to fulfilling its one-China principle. Underscoring the seriousness of the situation, China has suspended contacts with the US over a wide range of issues, ranging from maritime security to climate change.

The Taiwanese government had countered the Chinese military exercises with military drills of its own. The US government has likewise indicated that it will not accept any infringement by China on Taiwanese sovereignty, and that the US will continue to seek passage through the Taiwan Strait, which China declared closed due to military exercises, in the coming weeks. The US has extended the deployment of an aircraft carrier battle group off the eastern coast of Taiwan. The administration of US President Joe Biden continues to believe that the Chinese are not serious about invading Taiwan at this time and has focused its response on garnering support for its diplomatic condemnation of China's actions. Neither the US nor Taiwan has backed down from publicly declared positions that Pelosi's visit was part and parcel of normal discourse, and not the provocative action China has declared it to be.

To what extent China has moved the Taiwan issue from political to military channels is unclear. If Taiwan remains in the political channel, and the US and Taiwanese takeaway is that China was bluffing or messaging, then the Taiwan issue could revert to the uneasy status quo that existed prior to the Pelosi visit. That could suit Chinese President Xi Jinping, who is expected to be approved for a third term in office at the upcoming Chinese Communist Party conference. However, if the Taiwan portfolio remains under the Chinese military, and the US and Taiwan pursue policies designed to push back against the Chinese military posture by challenging China in the Taiwan Strait, then the possibility of triggering a war is very real.

Turkey: Looking East, Not West

Turkish President Recep Tayyip Erdogan recently concluded his second meeting with his Russian counterpart, Vladimir Putin, inside of three weeks. More leap than drift, the Turkish embrace of Russia suggests that Ankara has found a seam in the strategic divorce that has occurred between Russia and the West — and which it is exploiting to its unilateral advantage.

While critically important regional security issues in Ukraine and Syria were on the agenda, the major takeaway from these two meetings is that Turkey has set its course on strengthening its economic and political ties with Russia in a manner that puts it at odds with its erstwhile Nato allies.

At a time when the US, Nato and the EU are pushing for the economic and political isolation of Russia, Erdogan has taken a different path. The meeting of the Turkish and Russian presidents, which took place in the Russian Black Sea resort of Sochi, produced a wide range of economic agreements, including a decision by Turkey to partly pay for Russian natural gas in rubles, a renewed commitment to complete a nuclear power plant currently under construction in Turkey, and a willingness on the part of Turkey to integrate the Russian Mir card payment scheme with the Turkish financial system. The two countries also re-upped a target to expand trade from the current $26 billion per year to $100 billion.

The Turkish-Russian economic cooperation comes on the heels of a series of strategic decisions by Turkey, such as seeking to join Brics and possibly the Shanghai Cooperation Organization, that point to a growing Eurasian emphasis in Turkey's geopolitical posture. Issues such as Syria and Ukraine, where Turkey is at odds with Russian policy, remain sensitive topics. But both Ankara and Moscow appear to have found a way to avoid direct military conflict while expanding economic and political ties.

Turkey's actions underscore the reality that Europe is far from united in its response to Russia's ongoing invasion of Ukraine. Growing economic pressures and political tensions within Europe as governments there deal with the fallout of their collective policy of sanctioning Russia have prompted Turkey to believe it can act with near impunity when it comes to expanding ties with Russia. While the US and several of its European allies have expressed reservations about Turkey's Russia policies, any punitive response — if at all — is expected to be measured, out of a desire to avoid further alienating Turkey from the West.