CREA

Why Russia has strong incentives to keep supplying oil with a $30 price cap

Key messages for the EU

Initial signs of the crude oil price cap demonstrate that the policy is robust and effective. Estimates suggest the EU oil ban and the price cap are costing Russia an estimated EUR 160 mln/day. In the most recent 30 days, Russian fossil fuel exports to the EU were down 86% from a peak of EUR 700 mln per day in March 2022. Yet the EU is still sending EUR 100 mln per day to Russia for fossil fuels, made up of EUR 30 mln from pipeline gas, EUR 30 mln from crude oil, EUR 30 mln from oil products, and EUR 10 mln from LNG.

As the oil price cap review approaches in March, CREA's analysis builds the rationale for the EU to encourage a lower price level, based on 2 main reasons:

1. **Russia benefits from low oil production costs averaging less than $15 per barrel**, therefore with the current price cap set at $60 per barrel, Russia is making lofty profits which provides high tax revenues used by Putin to fund the war against Ukraine. CREA analysts suggest setting a lower oil price cap level of around $30 per barrel, in which Russia would still have incentives to supply oil closer to its low production costs whilst reducing its tax revenues.
2. **Russia's flexible and rent extracting tax structure on oil sales** is designed to extract maximum tax revenues whilst maintaining oil supply. As Russia's tax on fossil fuel exports is structured to syphon off the vast majority of the profit received, lower oil prices enabled through reducing the price cap level, would significantly damage Russian tax revenues whilst still encouraging oil production.

The EU & Norway play a key role in the maritime transportation of Russian crude oil, responsible for EUR 110 Billion or 29% of the maritime insurance of Russian crude oil throughout 2022. **EU & Norwegian owned ships played an even larger role in**

transporting Russian crude oil in 2022, responsible for EUR 177 Billion or 47% of all Russian crude oil exports.

European-owned and insured ships have carried EUR 310 mln per day of Russian fossil fuels in 2023, representing 65% of the total value of Russia's seaborne fossil fuel trade. This illustrates that the price cap coalition has a strong leverage to ratchet down the price cap level. Lowering Russia's export revenues from fossil fuels would significantly hinder Russia's ability to fund the war, especially important as it deals with large fiscal deficits in 2023.

Key asks for the EU to enhance the impact of the price cap and hinder Putin's ability to fund the war

The upcoming review of the level of the oil price cap in March is a prime opportunity for Ukraine's allies to starve Putin's regime of remaining fossil fuel revenues. We recommend lowering the price cap from its current level of $ 60 per barrel for crude oil down to a price level much closer to Russia's low production costs which average an estimated $ 15 or less per barrel. Lowering the price Russia receives for their oil exports would deny the Kremlin of taxable revenues, while still incentivising continued supply. We recommend:

- Revise the oil price cap down to $ 25–35 per barrel for crude oil and $ 5 per barrel higher for premium refined products. This level substantially reduces Russian mineral tax revenues while keeping Russian oil production economically viable. Use the EU's leverage as the largest owner of vessels transporting Russian oil and a key maritime insurer to emphasise that a lower price cap would significantly cut Russia's tax revenues while ensuring oil supply.
- Enhance monitoring and enforcement:
    - Permanently ban tankers that violate the price caps from entering EU and G7 ports or territorial waters.
    - Require copies of the underlying sales contracts rather than relying on attestations. Alternatively, require payments to be processed through an authorised intermediary, or that attestations can be allowed only from trading and financial entities on a pre-approved list established by the

EU/price cap coalition countries' sanctions authorities.
    - Establish a dedicated Russian oil sanctions monitoring & enforcement authority that conducts regular monthly and extraordinary audits on attestations and other required paperwork across coalition countries. Collaboration between EU and G7 monitoring and enforcement agencies to prevent, identify and address violations.
- Introduce additional sanctions to limit Russian seaborne oil trade. These include:
    - Restrictions on the sales of tankers, to prevent old tankers being used to circumvent the cap.
    - Prohibit transhipment of Russian oil through EU territorial waters and exclusive economic zones; collaborating with price cap coalition countries to identify and address transshipments elsewhere.
    - Require enhanced P&I insurance disclosure and review for any vessels not insured by the International Group when passing through the Danish Straits and other EU/G7 territorial waters or exclusive economic zones in order to ensure the enforcement of environmental norms.
- Institute price caps and/or import restrictions on pipeline oil coming to the EU from Russia.
- Address oil blending to ensure traded oil is not partly Russian - including through technical audits to check its origin.

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