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## The 2020 Oil Crash: Is Russia Still An Energy Superpower?

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This month saw the dramatic outbreak of an oil price war launched by Saudi Arabia that caused the price of oil to plunge from \$55 to \$25 a barrel. While Russia's \$570 billion reserves mean that it can ride out the crisis in the near future, the episode calls into question the argument that Russia is an "energy superpower" whose oil and gas exports boost its international influence. Russia's policymakers have always wanted to turn its energy wealth into geopolitical influence, but it continues to wrestle with the state's "resource curse" involving domestic corruption and developments in global energy market related to fracking, climate change, and China's rise as the main customer for Russia's oil and gas exports.

### **Oil Price and Production**

On March 6, talks in Vienna between OPEC ministers and Russia broke up without agreement. Saudi Arabia announced that it would be increasing its oil output by 25 percent and offered extra discounts to European buyers. Global demand for oil had fallen by 3 percent since the start of 2020 due to the spread of the COVID-19 virus. The Saudis asked all members of the "OPEC+" group to cut output by 4 percent, but Russia refused, arguing that the price should be allowed to fall below \$50 a barrel, in order to drive U.S. shale oil producers out of business.

It was widely [reported](#) that Rosneft chief Igor Sechin was behind the decision to break with the Saudis, motivated by his desire to retaliate against the United States, whose post-Crimea sanctions have caused severe problems for Russia's oil and gas industry. Already a year ago, a [letter](#) from Sechin to President Vladimir Putin was leaked that protested the arrangement with OPEC+.

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Personnel changes also played a role. In January, Mikhail Mishustin replaced Dmitry Medvedev as Prime Minister—and Medvedev was seen as limiting Sechin’s influence. Russian energy minister Aleksandr Novak reportedly had good relations with his Saudi counterpart Khalid al-Falih, but he was replaced in September 2019 by Prince Abdulaziz bin Salman Al-Saud, the king’s eldest son.

Since 2008, U.S. producers have invested over \$400 billion in shale oil and gas, boosting U.S. oil output from 8.5 million barrels per day (mbd) in 2016 to over 13 mbd today. A price war will indeed damage U.S. oil producers—half of the shale exploration companies may go bankrupt. But U.S. consumers will benefit from falling oil prices. Oil and gas extraction accounts for [only 1 percent](#) of the U.S. economy, and the United States is still a [net importer](#) of oil. Russia is much more dependent on oil than is the United States, so the impact on Russian GDP growth and government revenues will be much more severe. It is not just U.S. shale oil that is uneconomic at \$30—the cost of developing Russia’s new fields in the far north and offshore in the Arctic means those projects will also be put on hold.

In light of these facts (well known to Russian leaders), correspondent Maksim Averbukh [makes](#) the provocative argument that the real motive of the Russians (and the Saudis) is to keep the oil price low this year to help President Trump win re-election.

### **Russia as an Energy Superpower**

In the 2000s, the biggest fear in the West regarding Russia was, it seems, the energy weapon. However, over the past decade, Russia’s rebuilding of its armed forces and its willingness to use them beyond its borders has shifted the perceived threat toward military power. This began with Russia’s invasion of Georgia in 2008 and continued with the annexation of Crimea in March 2014 and the military intervention in Syria in September 2015. At the same time, developments in global energy markets (the fracking revolution and the rise of China) have changed the equation of risks and rewards in Russian energy exports. Increasing global economic integration left Moscow more vulnerable to fluctuations in world markets, and post-Crimea sanctions revealed its exposure to Western interruption of key technologies and financial services. Russia’s capacity to wield the energy “weapon” to advance its interests looks much more questionable today than it did ten years ago.

Oil and gas were key to Russia’s return to prominence on the international stage in the 2000s. The term “energy superpower” took off after Russia’s interruption of natural gas supplies to Ukraine in January 2006. Many an *Economist* [cartoon](#) showed the Russian bear alongside oil and gas valves and pipelines. Russia was seen as using energy dependency to pressure neighboring states to accede to its political or economic demands. Swedish analyst Robert Larsson [identified](#) 55 instances between 1992 and 2006 when Russia cut, or threatened to cut, energy supplies. For the Russian elite, too, the term “energy

superpower” was a useful rhetorical device justifying their rule, with the geopolitical utility of energy being expressed in the 2003 Energy Strategy.

The data undoubtedly indicate that Russia is a major player on global energy markets. Russia is the second largest producer of natural gas and third largest producer of oil in the [world](#) (after the United States and Saudi Arabia). Until December 2018 the United States was a net oil importer, so Russia is the world’s second largest oil exporter and supplies about 20 percent of European oil consumption. Due to the shale gas boom, the United States is now the world’s top [gas producer](#), but Russia remains the #1 exporter, and it supplies 40 percent of the EU’s gas. Russia is the world’s #3 [coal exporter](#), with exports tripling over the past decade.

After the Soviet collapse, Russia found itself dependent on pipelines transiting Belarus, Lithuania, and Ukraine to access Western markets. So Moscow set about building new pipelines across the Baltic and Black Seas. Russia’s success in building these new export pipelines was a major strategic accomplishment. However, over the years, Russian efforts to wield the “energy weapon” often served to alienate countries and make them seek alternatives. Trade is a relationship of mutual benefit and dependence between buyer and seller, and the use of trade as a “weapon” can hurt the supplier just as much as the customer. Using energy as a carrot rather than a stick has not proved any more effective. Twenty years of subsidized energy prices for Belarus, for example, has not produced a loyal and subservient ally for Russia, a striking example of how hard it is for Moscow to turn energy sales into political leverage.

### **Russia as a Petrostate**

There is a curious imbalance between Russia’s resurgence as a power on the world stage and its anemic economic performance. This is largely explained by the decisive role that energy plays in structuring Russia’s domestic political economy. Russia remains very much a “petrostate,” in which the energy rent-seekers, in alliance with the security forces, have the upper hand over the profit-seekers. So the main geopolitical importance of energy when it comes to understanding Russia is not its role as a tool of power projection abroad but its role in shaping the behavior of the Russian power-elite at home.

For decades, hydrocarbons have [accounted](#) for 25 percent of Russia’s GDP, 75 percent of exports, and 50 percent of government revenue. At least until 2014, the Russian business cycle was closely tied to fluctuations of the international price of oil. Oil export revenues are three times larger than those for gas, but inside Russia, gas accounts for three times as much energy consumption as oil, being used to heat homes and generate 50 percent of Russia’s electricity.

Putin’s renationalization campaign concentrated ownership and control of Russian energy in the hands of a small circle of individuals close to himself. Much of the rents from

the energy trade are siphoned off by offshore intermediary companies such as Gunvor, which became the world's largest oil trader just five years after it was founded in 1999 by Gennady Timchenko, a friend of Putin. Timchenko and Putin "crony" Arkady Rotenberg also profited handsomely from the pipeline contracts they won for their construction companies.

Writing back in 2008, I was [cautiously optimistic](#) that Russia could beat the "resource curse." The Russian economy had doubled in size in the previous seven years, Russia had paid down its foreign sovereign debts, and its monetary and fiscal policies protected the economy from the gyrations of global oil markets. In 2020, the economic picture is far less rosy. The 2008 financial crash hit Russia very hard, and the economy never regained a sustainable growth path. While Russia avoided a complete collapse of the banking system in 2008, investment never returned to its pre-2008 levels, [GDP growth](#) has averaged less than 2 percent per year, and living standards have stagnated.

Russia's poor economic performance illustrates one of the central contradictions of the "energy superpower" model. The "resource curse" means that Russia's petrostate finds itself facing economic and political instability at home that erodes its ability to act confidently on the international stage.

### **Russia's Evolution Over the Past Decade**

Several important changes over the past decade have impacted our perception of Russia as an energy superpower.

#### *The Putin factor*

The consolidation of an authoritarian regime under Putin has defied sceptics who initially saw him as a weak, transitional leader—and has defied optimists who posited that Russia's growing middle class and rising young generation would demand an open and accountable government. Russia's authoritarian shift has consolidated its hydrocarbon dependency. Kremlin "cronies" continue to engage in asset seizure and even the jailing of rivals, so there is little incentive for independent capitalists, both foreign and Russian, to invest in Russia. The post-Crimea sanctions have furthered diminished Russia as a destination for investors.

#### *Russia's shift to hard power*

Russia has shown a new willingness to use military force beyond its borders. Its military interventions in Georgia, Ukraine, and Syria caught Western observers by surprise. Each operation was a success: enemy forces were defeated (without a fight, in the case of Crimea) and Russia's strategic goals were realized.

Putin had used some of Russia's energy export rents to [triple spending](#) on the Russian military in real terms 2000-2010. The armed forces underwent limited modernization but

were protected from radical reforms, and were rewarded with a prominent place in the regime's patriotic propaganda binge. This use of conventional hard power was accompanied by a panoply of techniques of "hybrid war" – some old, some new. Given that Russia was so actively using hard power, the question of Russia's energy diplomacy slipped out of view.

#### *Changes in global energy markets*

There have been some revolutionary changes in global energy markets over the past decade that together further undercut Russia's putative role as an energy superpower.

#### *The fracking revolution*

Developments in seismology and horizontal drilling – [the shale revolution](#) – led to an explosion of oil and gas production in the United States. Thanks to booming demand from China, which overtook the United States as the world's largest oil importer in 2013, the global oil price held up, at least until this past month. But the price of natural gas in the United States toppled from \$13/million British thermal units (MMBtu) in 2008 to below \$5 since 2010. Lower U.S. demand for LNG led to a fall in the price of gas on international markets. Gazprom had to cut prices and faced lawsuits challenging its long-term take-or-pay contracts, obliging it to pay \$3.2 billion in rebates to European customers for 2012. That year, Gazprom earned \$64 billion from exporting 217 bcm to Europe: in 2016 it earned only \$37 billion even though export volume grew to 262 bcm. Russia missed out on the seismology revolution, and has fallen behind in turbines, refining technology, and offshore drilling. It urgently needs to import technology, now barred by the post-Crimea sanctions.

#### *The rise of China*

Cooperation between Russia and China deepened after the 2008 crisis exposed the inadequacy of the Western-led system of global governance, and forced Russia to borrow from China to fund the completion of its new oil export pipeline. China overtook Germany as Russia's largest trading partner in 2011. For many years Russia did not allow China equity access in oil and minerals projects, but that started to change in 2013 when CNPC bought a 20 percent of Novatek's Yamal LNG project. Other deals followed. In 2014, Russia signed a \$400 billion deal to supply China with 38 bcm of gas for 30 years, though the price that Beijing will pay is not known. Putin's "pivot to Asia" decreases Russia's leverage as an energy superpower, since the country will not account for more than 10 percent of China's oil and gas needs in the foreseeable future. China's economy is five times as big as Russia's, so Moscow will always be the junior partner.

#### *Climate Change*

Russia signed on to the Kyoto and Paris accords, aware that they would not have to cut emissions to stay below the 1990 target level, given the collapse of Russian manufacturing in the 1990s. (As of 2014, [Russian emissions](#) were 30 percent below their 1990 level.) Rather than invest in conservation or renewable energy, Russia is building more atomic power

plants – and selling them overseas. The generous subsidies for Rosatom’s export program are a way to keep the military-industry complex happy and share with them some of the spoils from Russia’s hydrocarbon economy. Russian leaders have been complacent about climate change, and some prominent Russian scientists are climate change deniers. However, climate change will have a severe impact on Russia’s ecology and economy – as evidenced by the wave of droughts and forest fires and future thawing of permafrost. Finnish analyst Veli Pekka Tynkkynen [argues](#) that with its vast forest reserves, Russia has the potential to be a “green superpower,” but Moscow’s policy is held hostage by the hydrocarbon elite who try to maximize short-run profits.

## Conclusion

The concept of an “energy superpower” is somewhat contradictory, lumping together two quite distinct logics: that of the energy market and that of military superpowers. Russia wants to convert its energy wealth into geopolitical influence. But energy rents come with all the drawbacks of the “resource curse,” from corruption at home to market volatility abroad. As a relatively high cost producer, Russia cannot win in its “oil war” with Saudi Arabia. Yet despite its vast wealth, Saudi Arabia is not thought of as a superpower (it is even unable to prevail in the war in neighboring Yemen). It is unusual to see a resource-rich country taking on the attributes of a world power. It was resource-poor countries like Britain or Japan that created empires to acquire more resources. The United States itself has a rich resource base, but it began to import oil in the 1940s, and the search for oil contributed to the U.S. willingness to shoulder a superpower role.

Russia, of course, is the grand exception: Tsarist Russia was rich in resources but created the world’s largest empire. The expansionism of the tsars was driven by a concern for security and prestige rather than a search for resources. Likewise, the USSR’s quest for empire was not primarily driven by a need for more resources, but by a combination of security fears and ideological fervor. Putin’s Russia seems to be reverting to a similar pattern. Unfortunately, it ended badly both for the tsars and the Soviets.

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