

# Oil Market Report: February 2022

At the end of last year, we predicted a speedy resolution to the issues surrounding the Gazprom (ie, Russian) owned Nord Stream 2 gas pipeline (<https://stabilityfromvolatility.co.uk/market-reports/energy-market-report-10-21/>). As gas prices spiralled out of control, we figured that no European Government would sit on their hands and do nothing to increase gas flows into Europe. However, we now know that the line will not be going ahead (for the foreseeable future at least), as newly appointed German Chancellor Olaf Scholz has vetoed its operation on the back of the exploding Ukrainian situation.

One imagines that privately, plenty of European leaders would love to have given Nord Stream 2 the green light. Then the increased supply of gas might bring prices down and end the billions of pounds of energy bill subsidisation that is now taking place across the continent. It would also give breathing space to ragged energy departments who are stuck in a crisis whereby energy growth is booming, whilst supply is faltering – be that fossil fuel based or renewable.

There were however two rather large objects that stood in the way of a green light for Nord Stream 2. One was the USA, who whilst facing a certain element of domestic turmoil in their own energy markets, are far more energy self-sufficient (when it comes to gas) than Europe. This gives them a certain sang-froid in their dealings with the Nord Stream issue and their opposition to the pipeline is absolute. They believe its opening will give Russia even more power over Europe. Plus, there is a healthy dose of self-interest thrown into the mix, because even green leaning Democrats are well aware of the economic value of US liquified natural gas exports to Europe. These would be displaced by any new pipeline bringing extra Russian gas into the continent's heartlands.

The second object standing in the way of Nord Stream 2 was as implacable as the first, but considerably more surprising. It would now seem that Russia began to pull back from the new pipeline in the final quarter of last year, sensing greater value in a catastrophic European energy crisis, than in the commercial benefit that the line presented. Remember that current gas prices are now so high that Russia is earning more income through existing pipelines, than was forecast as a result of the extra volume to be transited via Nord Stream 2. Furthermore, such is Russia's enviable geographic position, that it has gas options to the East (China) and South (India / Pakistan), which means it can effectively starve (European) markets of gas as it sees fit. With China and India's boundless gas demand, compared to a Europe of awkward questions, tiresome politics and an obsession with the environment, the options East and South would seem considerably more attractive to Putin's Russia, than moving gas westward via Nord Stream 2.

Sadly this provides more than enough context for the current Ukrainian crisis. Conventional wisdom had always been that for as long as Russia wanted Nord Stream 2 operational, any incursion into the Ukraine would not be forthcoming. But if it has now been decided in Moscow that Nord Stream 2 isn't quite as important as it once was, then the immediate geopolitical outlook looks disconcertingly different. Putin has responded to the global energy crisis, sensing no better opportunity to take control of the Ukraine, whilst Europe prioritises covid recovery and domestic cost of living issues. Arch Machiavellianism for sure, but the Russian leader did cut his teeth in the KGB...

History is made up of missed opportunities and there are many when it comes to European energy policy. One example was when the proposed Trans-Caspian "Nabucco" line was confined to history in 2014. The proposed pipeline was to source gas from Azerbaijan, Turkmenistan and Iraq (travelling into Europe via Turkey) and was specifically designed to avoid over-reliance on Russian gas. For reasons that seemed important at the time (amongst them strong environmental opposition), the line was killed and Europe continues to rely on Russia for over 50% of its gas supply. Put quite simply, we are at the mercy of Russian energy, because we have no other viable supplies to rely on. Politicians of different persuasions differ on many things, but they normally agree that relying so completely on a foreign power for energy supply is not a good thing. Yet, that is the current situation.

Which begs the question whether it has been wise to treat gas in the same way as oil and coal, when it comes to the decarbonisation agenda? The former has considerably better CO2 credentials and yet has been blocked and opposed in the same way as oil and coal projects. The result has been limited gas supply, rising prices, the slowing of CO2 emission reduction, the current state of complete energy insecurity and now, an invasion. Those Ukrainians facing a rather uncertain future, may now choose to disagree with the current European viewpoint that "climate change threatens lives and livelihoods". So do wars and so does a lack of cheap and constant energy! Furthermore, there is clearly no point in cutting back on domestic energy production, if we are simply going to replace the same product (gas) with supplies produced elsewhere. It's too late to ask the question, but if we had taken as much care of our short-term energy needs – on an equal basis to the long-term – would the current Ukrainian crisis have been avoided?