EU Stumbles Over Russian Oil Slick

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Global Research, May 12, 2022
Indian Punchline 11 May 2022

Region: Europe, Russia and FSU
Theme: Oil and Energy

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The European Union officials are insisting that oil sanctions against Russia are coming. On Sunday, France's Ecological Transition Minister Barbara Pompili was certain that "we will reach (an agreement) by the end of the week."

But the Organisation of Petroleum Exporting Countries (OPEC) has warned EU that it would be impossible to replace more than 7 million barrels per day (bpd) of Russian oil and other liquids exports potentially lost due to sanctions or voluntary actions.

The fine print here is that the Western entreaties on OPEC to increase oil production is falling on deaf ears not so much due to diplomatic recalcitrance as the group's genuine inability to implement higher hikes due to under-investment in oil and gas ventures that has left some Opec+ members with dwindling spare capacity (with the exception of Saudi Arabia and the UAE.) In fact, in March, OPEC+ production production recorded a decline for the first time in 13 months and is currently around 1.48mn b/d under the coalition's quota system.

OPEC+ members, including Russia, have agreed to raise output by about 432,000 barrels per day in May, as part of a gradual unwinding of output cuts made during the height of the COVID-19 pandemic. There is seething anger in Washington that Saudi Arabia and the UAE refrain from stepping up production. Hence the renewed talk of the 15-year old Damocles' sword in the form of a US legislation to punish these countries — NOPEC bill — which aims to modify the existing antitrust law to revoke the sovereign immunity that has long protected OPEC and its national oil companies from lawsuits in American federal courts.

If signed into law, the US attorney general would gain the ability to sue the oil cartel or its members Saudi Arabia or the UAE in federal court. (Other producers like Russia, which works with OPEC in wider group known as OPEC+ to withhold output, could also be sued.) But the energy superpowers know this threat is a load of baloney — that the US is in no position to dictate terms. In fact, when the US Congress passed a version of the bill in 2007, it died under veto threat from President George W. Bush who said it could lead to oil supply disruptions as well as "retaliatory action against American interests."

The “retaliatory action” that Bush feared, which President Biden should fear even more, could today include Saudi retaliation by way of terminating the use of the dollar for its oil trade, which would of course lethally undermine the dollar’s status as the world’s main reserve currency and significantly reduce the US influence in global trade.

Some recent reports suggest that Saudis are already in talks with Beijing on usage of local currencies for some portion of their oil trade, something that China also has been seeking lately. Interestingly, in a recent commentary, the well-known Chinese political thinker Zhang Weiwei argued strongly in favour of a new thinking in Beijing against the backdrop of the US’ harsh sanctions freezing the foreign exchange reserves of the Russian Central Bank and removing Russia from the the Swift international settlement system. Prof. Zhang wrote:

> “The current (Russian) decision to link natural gas and other raw materials to the ruble can be said to be a revolution against the hegemonic order of the US dollar. Very inspiring. As the world’s largest economy (based on purchasing power parity), the largest trader of goods, the largest consumer market and investment market, we (China) must boldly conceive and practice the construction of a financial system in the “post-American era”… We have a good hand, we have abundant natural resources, including a large amount of rare metals, we have the most complete industrial chain in the world, we are the only one in the world that can produce almost everything from the first industrial revolution to the fourth industrial revolution All product countries. Linking the renminbi to our special resources, to many products, is a new idea that we can consider.”

Be that as it may, Biden is highly unlikely to take the NOPEC path. The powerful American Petroleum Institute (which holds veto power on the Hill) thoroughly rejects the very idea of a lawsuit against OPEC for antitrust behaviour and market manipulation, which it fears could trigger “serious, unintended consequences” by giving Opec members an opportunity to reciprocate against US companies and even undermine their ability to sustain growing production.

Suffice to say, it is incredible that the EU is planning to commit harakiri this weekend by imposing oil sanctions against Russia. But then, it is one of those queer coincidences that at such a transformative period in world politics, the EU’s executive branch is headed by two arch-Atlanticists and hawkish Russophobes — Commission president Ursula von der Leyen and foreign policy chief Josep Borrell. When Biden is set to sign a $40 billion bill to defeat Russia in the proxy war in Ukraine, the least these two decision-makers can do to supplement the war effort is to cut Europe’s umbilical cord with Russia in oil trade — something that had survived even the high noon of the Cold War era (US diplomatic skulduggery notwithstanding.)

So, von der Leyen travelled to Budapest yesterday to persuade President Viktor Orban to join her chariot to storm the Russian citadel. Orban threatens to veto EU sanctions against Russia, since Hungary is critically dependent on Russian oil supplies, which come overland through the Druzhba pipeline at ridiculously low cost price. Orban visited Moscow on February 1 when he and President Putin agreed on a new long term gas contract at favourable price.

Hungary needs more time (and investments) to reduce its dependency on Russian gas. But Orban is a smart politician too. Von der Leyen crossed Orban’s path, irritated alike by his authoritarian tendencies at home and his warm ties with Kremlin, and in an itch to teach him a hard lesson decided in March to withhold EU funding for Hungary by invoking the "rule-of-law conditionality mechanism."

Perhaps, von der Leyen thought she could incentivise Orban. Of course, going slow on the EU's conditionality mechanism prescribing a "rules-based order" for Hungary is a counterfactual that is impossible to test. The word so far from Budapest is that no deal was struck. But the bottom line in the Hungarian saga is that EU member states can muster "smart power" within the group's treaties to frustrate the Commission using a mechanism outside of it to try and get to them. In systemic terms, this highlights the limits of European integration via the backdoor: what the EU can actually achieve institutionally without treaty change.

It is far too premature for the EU to talk about stabilising prices or reducing dependence on Russian energy resources because these processes will take time. On the other hand, these sanctions won't deter the Russian operation in Ukraine, while the ensuing turbulence in the world oil market will not spare European economies too.

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