Rodney's Take

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Another Ineffective Russian Ban and Higher Prices

The U.S., Britain, and the members of the European Union once again are taking a tough stand on Russian energy exports. On February 5, the group will ban Russian diesel and fuel oil, adding to their ban on Russian oil imports that went into effect in early December. Chances are that the impact will be the same, which is minimal.

While the Russian oil ban by some countries and price limits on trade by others curbed Russia oil sales, the nation still sells more than eight million barrels per day in the global market. Almost a year after Russia invaded Ukraine and western nations vowed to punish the Kremlin, Russia remains among the top three oil producers on the planet. Yes, Russia sells a chunk of its oil at a discount to prevailing world prices, but they still earn a hefty profit compared with their production costs, and the discount is enticing enterprising companies in other countries to take even more of the Russian crude.

India, which imported about 2% of its oil from Russia in 2021, secured 25% of its oil from Russia last year, growing the total from about 36K barrels per day to more than one million. But the Indian importers weren't just switching suppliers to take advantage of lower prices, they also were ramping up exports. India has few oil reserves but immense refining capacity. Indian refiners are importing more Russian oil, blending it with other supplies, refining it, and then selling it to the same Western countries that have banned Russian supplies. The blend, refine, and export move is perfectly legal, even though it obviates the point of the Russian import ban.

Now, the same thing is about to happen with diesel and fuel oil, and chances are that Indian refiners are giddy at the prospect of adding to their profits through some combination of blending, refining, and exporting such goods. Given that Russia is a major exporter of diesel and fuel oil, it's possible that enterprising companies in a number of countries won't have to worry about refining, they can just add Russian diesel to supply from other nations, call it a "blend," and resell it on the global market at the prevailing price.

The dance step in the energy markets might be taking a little cash out of the Kremlin's pocket, but the benefit doesn't go to consumers. Instead, middlemen are raking in fat profits. Don't expect this to change in the months ahead.

China is reopening its economy and the U.S., European, and Chinese economies appear to be ending a rough patch and establishing a base before moving higher, but oil is sitting at $80 instead of $40, as we might expect during less-robust times. OPEC+ has kept a tight lid on supply, which means oil and related energy prices likely are headed higher, not lower, no matter what the U.S. wants to have happen. As our economies improve, expect oil prices to settle around or just above $100 and for energy to cost more.

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