

# **FEAR, PREDICTABILITY AND PROFIT: WHY NOTHING WILL CHANGE FOR A DIVIDED UKRAINE**

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Achieving ‘Harmony in the World’ through international cooperation or scourging those ‘Disrupting the Peace’ are simple enough themes for short media segments but for pragmatists these are neither explanatory nor accurate. Instead realists argue that harmony and peace are illusory ideals which never existed. In world affairs the analogy of ‘balancing’ or more commonly the ‘Balance of Power’ appears more apt. Such is the case of Russia’s relationship with the Ukraine. Not all that long ago Russia literally had its say in affairs in each of the regions it bordered. Whether it was Eurasia, the Caucasus or particularly in Eastern Europe, everyone looked to Moscow’s reaction first before deciding anything on their own. When the Soviet Union fell apart, the rest of the world believed that it was the end of “Russian Hegemony.”

Western countries were partly right. Russia became very weak. It was marked by internal political fragmentation if not outright anarchy. GDP fell by 52%, industrial production by 64.5% with agricultural volume by 60.4%. The weakened currency was punctuated by severe inflation. Whenever such things occur, any country in the same situation will resort to its strengths however few they may be, namely the turnaround of a weakened military and its abundance of natural resources of which oil plays a key role.<sup>1</sup> While it never achieved the status of exporter like China for example, the recentralization of authority has brought it back to a point where it demands to be reckoned with, for better or worse, by other countries.

The key problem with this return of power is that the Europeans do not remember the past as the Russians do. In the Russian mindset, Crimea was never meant to be part of the Ukraine. What the Tatar-Mongolian invasions taught the Russians as early as the 1600s was never to become landlocked even if it required invading and annexing to do so. Once you have ports, you can have fleets which was what Peter the Great did in the Baltic and

Black Seas.<sup>2</sup> The territory of the Ukraine was always admired for its tillable soil but it was still locked between Russia, Poland and Crimea. Access to the Black Sea, to include control over the neighboring Azov Sea was always key elements of Russia's external policy<sup>3</sup> thus solidifying their definition of what it meant to be powerful.

This is also what Lord Palmerston understood in 1853 during the First Crimean War. 'The caveat he attached to Russian invasion and encroachment was that it would only be allowed so long as other governments, namely European ones were apathetic to Russia's actions'. The remedy according to Lord Palmerston was for unification and powerful resistance. Once that occurred, Russia would back down. Apparently unification worked for it was this same war that Russia lost Sevastopol and their military presence in the Black Sea. At the Treaty of Paris, signed on March 30, 1856, Russia returned southern Bessarabia and the mouth of the Danube to Turkey. Moldavia, Wallachia and Serbia were placed under international observation rather than Russia so long as the Sultan promised to respect the rights of his Christian subjects.<sup>4</sup>

Nothing teaches or informs the affairs of countries more than its past humiliations. Fast forwarding to today it is no accident that Ukraine's fault lines coincide with the necessary logistical routes to access the Crimean port of Sevastopol. By annexing Crimea, Russia no doubt feels they have regained what is rightfully theirs.

As mentioned earlier, Russia has two strengths – natural resources, namely its oil and its military. With Venezuela having larger reserves than Russia, it has two choices – build pipelines or load oil tankers at a port. Looking at the former, Russia's state-owned oil company 'Gazprom' is a key player for the exports amounting to roughly 50% of Russian GDP. Gazprom's crusade against Ukraine started on January 1st, 2006 when it stopped the supply of gas to Ukraine. The reason for such a move was Ukraine's unwillingness to enter into a new contract with the revised prices increasing from \$50 to \$230 per thousand cubic meters of gas. In response, Kiev began the collection from the transit pipelines meant for Gazprom's European customers. While Gazprom reinstated shipment the very next day (January 2d), the damage was done. With the mediation of the Swiss company Rosukrenergo on January 4<sup>th</sup>, both sides agreed to a contract that settled on \$95 per thousand cubic meters.<sup>5</sup>

When this happened again on December 31, 2008, Gazprom's intention was to raise the price to the European level of \$450 per thousand cubic meters. Predictably on January 1, 2009, Gazprom shut off supply to Ukraine, and on January 7, supply to Europe was blocked. When Prime Ministers Vladimir Putin and Yulia Tymoshenko agreed on a price of \$ 450 per thousand cubic meters on January 19<sup>th</sup>, a 20 percent discount was given with conditions attached to Sevastopol. By 2010, Moscow agreed to sell Kiev gas at a discount of 30% under the guarantee that the Russian Black Sea Fleet could stay at Sevastopol until 2042. This last contract signed in 2011, was the main reason of Timoshenko's imprisonment and her prosecution.<sup>6</sup>

With the ouster of President Viktor Yanukovich in 2014, Russia could not lose its pipeline nor its port. The key question is whether the sanctions in effect today has the same sting

that Lord Palmerston envisioned 161 years later. The answer is an unequivocal no. Whenever world leaders talk about unification against Russia, what they are really signaling is apathy. Here's why. However punitive, the sanctions regime has not proven to necessarily stop whatever odious behavior state actors may be committing but instead create a counteraction. As a result, Russia's reaction was for Gazprom to sign agreements with Chinese company CNPC to supply oil for 30 years at \$400 billion.<sup>7</sup>

This oil, otherwise meant for Europeans was taken off the market with the stroke of a pen. The reason this is important is if supply never reaches the open market, what remains available becomes scarcer. When a commodity becomes scarcer, it becomes more expensive. What the European Union got for its trouble was instability, devaluation and inflation in Ukraine while its own citizens face a higher heating bill with its imposed taxes this coming winter. In return for its pariah status, Gazprom made a deal increased its stock price by \$2 the day it was announced.<sup>8</sup>

The lingering question that remains is if Gazprom is owned by Russia's most politically powerful, how can they have a stock going up at all if they are under sanctions? The answer is that Gazprom stock is still traded in the world's financial markets. What is also traded is Brent Sea Crude in London and West Texas Crude at New York's Mercantile Exchange (NYMEX). Oil speculation has nothing to do with what is actually available but the fear that supply may be disrupted. Neither does this have anything to do with collusion between the parties because with supply and demand there is nothing to discuss when it comes to buying low and selling high.<sup>9</sup>

That offers no assurance to the Ukrainians or the next group of people that try to assert their own nationalist ideals. Just ask the Georgians. With regards to speculation and the world's markets, the casino adage that the 'house always wins' still rings true. In this case, Moscow wins, London wins and New York wins regardless of whether sanctions have teeth or is in reality disguised apathy to the voters at home watching the evening news. Profit was hardly what Lord Palmerston had in mind when he introduced the first-ever economic sanctions against Russia back in 1855.<sup>10</sup>

### **Footnotes:**

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<sup>1</sup>Van Sjaoshi, 2013. "If China will fall apart as the USSR, the consequences will be even more pitiable" (translated from Russian), published at Xinhuanet, available at <http://inosmi.ru/world/20130814/211858034.html> [accessed August 26, 2014]

<sup>2</sup> V.S. Bobylev, 2008. "Russia's external policy in the era of Peter I" Published at Jelektronnaja biblioteka , available at <http://www.universalinternetlibrary.ru/book> [ accessed August 26, 2014]

<sup>3</sup> Zurab Chiaberashvili, 2014. "Москва слезам не верит" (translated from Russian), published at Gruzia online, available at <http://apsny.ge/articles/1408646241.php> [accessed August 26, 2014]

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<sup>4</sup> Andrew Lambert, 2011. “The Crimean War” Published at BBC History, available at [http://www.bbc.co.uk/history/british/victorians/crimea\\_01.shtml](http://www.bbc.co.uk/history/british/victorians/crimea_01.shtml) [accessed August 26, 2014]

<sup>5</sup> Aleksandr Gabuev, 2014. “Protection against Gazprom” (translated from Russian), published at Kommersant, available at: <http://www.kommersant.ru/doc/2492526> [accessed August 26, 2014]

<sup>6</sup> *ibid.*

<sup>7</sup> Forbes, 2014. “ Miller called the cost of the contract a commercial secret” (translated from Russian), published at Forbes, available at: <http://www.forbes.ru> [accessed August 26, 2014]

<sup>8</sup> *ibid.*

<sup>9</sup> Myra P. Saefong and William Watts, 2014. Nymex oil at six week high; Brent tops \$109” Marketwatch, available at: <http://www.marketwatch.com/story/oil-futures-mixed-brent-lifted-by-ukraine-tensions-2014-04-14> [accessed August 27, 2014]

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<sup>10</sup> Lambert, 2011.