BLOG

New oil price cap adds to Russia's economic distress

Today – Russian economy

AUTHOR

Laura Solanko

Senior Adviser

In mid-July, European Union countries adopted their 18th sanctions package of economic and individual measures against Russia. The latest batch of sanctions seek to further degrade Russia's ability to pursue its war of aggression in Ukraine and support EU efforts to end the war.

Importantly, the hard-hitting sanctions package signals the EU's ability and determination to take action on its own. Despite differing views, all 27 EU members unanimously voted to keep existing restrictions in place and adopt the extensive new sanctions package. Thus, anti-Russian sanctions remain in place with no easing in sight. Sanctions make it more costly and difficult for Russia to wage war.

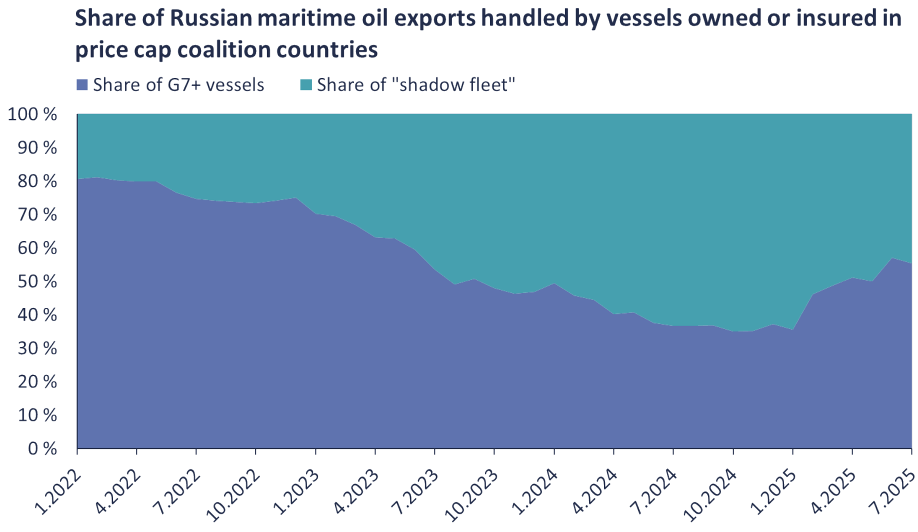
Sanctions measures against Russia fall into three categories: a) restrictions of exports of Russian commodities, b) restrictions on Russian imports of goods and services, and c) sanctions against specific individuals and corporations, including the freezing of Russian assets abroad.

The newest sanctions package contains measures from all three categories, hitting energy, banking, military industries and individuals. The most significant measures in the package relate to restrictions on Russian energy exports, further specification of the oil price cap and compliance monitoring. With some minor exceptions, maritime imports of Russian crude and petroleum products to the EU have been banned from February 2023. In addition, the imports of Russian crude oil via the Druzhba pipeline were reduced to a small fraction of its earlier flow. The pipeline currently only supplies oil to Slovakian and Hungarian energy companies. In the European Commission's view, these imports must also cease no later than 2027.

The EU import ban has forced Russia oil companies to find new buyers for their oil elsewhere in the world. Over the past two years, the geography of Russian oil exports has changed completely. Instead of EU countries, the largest purchasers are now China, India and Turkey. The new buyers have been enticed with substantial price discounts.

Western firms and financing arrangements have, however, retained significant roles in Russia's oil trade. Thus, on top of the EU import ban, Western countries retain the possibility of limiting Russia's export earnings via the oil price cap set by the G7 countries. Under the arrangement, firms based in countries of the price cap coalition are forbidden to participate in any way in the financing, transport or insurance of Russian oil exports if the oil is sold at a price above the per-barrel price cap.[1] This arrangement assures that Russia must continue to sell its oil at a discount.

Chart 1.



Source: CREA Russia Sanctions Tracker. The figure is based on the volumes of crude oil and oil products exported from Russian ports. In crude oil shipments only, the share of the shadow fleet is significantly higher.

A new price cap

Up until mid-July, the initial price cap of $60 a barrel for Russian crude, set in December 2022, remained untouched. EU has now decided at its own initiative to switch to a floating cap, so that the cap is always 15 % lower than the average price of Russian Urals blend over the previous six months. The EU's new price cap enters into force on September 3, lowering the cap price to $47.60 a barrel.[2] The United Kingdom has also announced that it is moving to a similar floating cap. Even if the decisions of other coalition member countries have yet to be taken, European companies alone play a significant role in global oil trade.

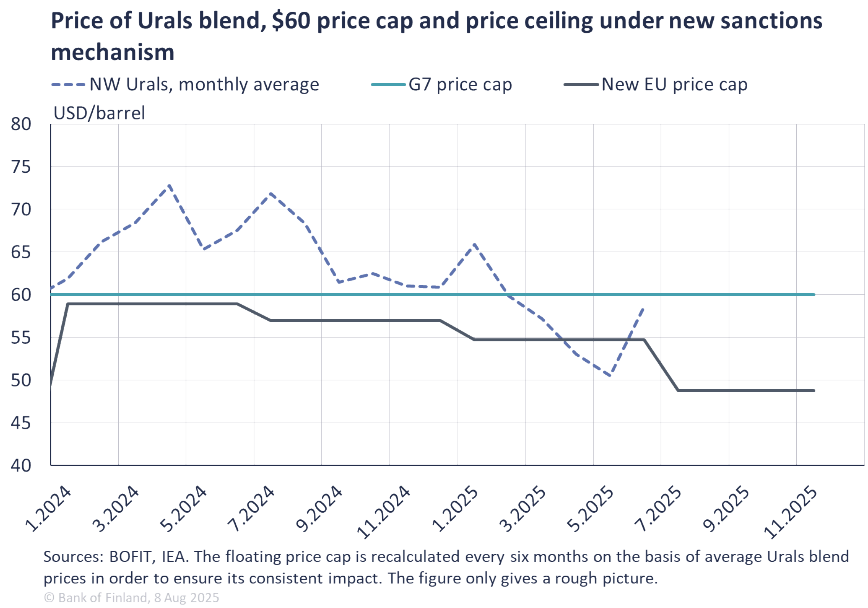
The introduction of the new price cap mechanism has significant implications, since it leads to a sizable decrease in the price cap. Due to recent declines in global oil prices, the $60 price cap was no longer binding. For this reason, the share of European tankers involved in Russian oil exports rose to about 50 % in the spring of 2025. The decrease in the price cap forces Russian oil companies to again seek other carriers for their export routes.

---

1. The coalition comprises the G7, EU and Australia. While Norway is not an official member of the coalition, it has implemented parallel legislation to the same effect. In addition, South Korea and New Zealand have announced they will uphold the G7 price cap.
2. If the cap price again changes, existing contracts are protected by a 90-day transition period.

Over the longer term, the change in the mechanism itself is significant. The price cap now will be adjusted every six months with the aim of keeping the price of Russian oil at least 15 % below prevailing market prices. This should give buyers greater bargaining power in seeking discounts from Russian sellers. Additionally, it forces all trading parties to be constantly vigilant and adds to uncertainty in dealing with Russian energy products. These complications reduce the lure of Russian oil and petroleum products to buyers on the world market.

Chart 2.



Sanctions list hits shadow fleet from multiple directions

The effectiveness of the price cap leverages the significant role of Western firms in global trade. For this reason, Russian actors have actively built complex, opaque and quasi-legal arrangements for maritime transport of fossil fuels, involving all aspects from crew selection and shipping companies to vessel insurance and payment arrangements. The vessels involved in these schemes are usually referred to as Russia's shadow fleet. Many of the vessels in the shadow fleet are in good shape, often acquired from Greek shipping companies in 2022 and 2023. But increasingly the fleet includes rust-bucket tankers approaching their final decommissioning. These tankers may have an unknown flag state, or they may sail with fabricated documentation.[3]

So far, Russia has been able to use the shadow fleet with partial success in circumventing the price cap. Indeed, from the summer of 2023 to the end of last year the average price of Urals blend generally exceeded the price cap. Of course, Russia never managed to garner prevailing global oil prices for its exports since the invasion of Ukraine, and the price of Russia oil has been running on average about $15 below the price of benchmark

3. For more on Russia's shadow fleet in Finnish, see BOFIT Blog post from February 11, 2025 Ruuhkaa Itämerellä – Euro ja talous.

Brent crude. Prior to the invasion, the price gap between Urals and Brent was typically one or two dollars a barrel.

Placement on the sanctions list excludes the cap-violating shadow vessel from all coalition country services – and violators are being placed on the sanctions list at an increasing pace. The EU's 18th sanctions package lists another 105 vessels, bringing the number of vessels on the sanctions list to almost 500. Over 200 Aframax-class short- and medium-haul tankers, which are key to Russia's maritime oil export trade, have been placed on the sanctions list. This effectively forces these vessels to concentrate exclusively on the oil trade activities of Russia, Iran and Venezuela.

In conjunction with the new price cap policy, the EU's decision to sanction additional shadow fleet vessels could be highly significant as it forces Russia to once again find a new (likely more expensive) export arrangements for circumventing the price cap. For shadow vessel traders, it seems to be a seller's market these days. The burden of additional troubles directly depresses Russian oil export revenues and tax revenues to the federal budget. The rising budget deficit compels Russia's current government to make hard choices, as the funds used to finance the war are ever more clearly diverted away from other core public sector functions.

Sanctions wall built one brick at a time

The latest sanctions package includes further decisions that are important in principle. One of these is the ban on importing into the EU petroleum products refined from Russian oil in third countries. Oil refineries, particularly in India and Turkey, have managed to exploit the cheap Russian crude oil and exported refined products to EU countries. This has been an important business activity, particularly in the case of the Vadinar refinery in Gujarat, India. Russia's state oil company Rosneft holds a 49 % stake in the refinery.[4] The ban only goes into force in January 2026, but oil buyers are already feeling cautious.

The EU sanctions package demonstrates that the EU can impose restrictions on third-country firms that assist Russia in circumventing sanctions. As a result, the latest package of sanctions extends not just to Russian firms, but e.g. Chinese and Turkish actors as well. The access of companies choosing to violate sanctions limits their access to services and goods produced in EU countries in one fell swoop.

Each new restriction presents new challenges to Russian entities and potential disruptions to supply chains. Each time sanctions are tightened and updated, Russian companies must adapt and seek costly workarounds. With a sanctions regime that now steadily shovels sand into the gears of the Russian economy, the drafting and approval of the next sanctions package should be done sooner rather than later.

---

4. Herrala and Solanko (2025), Öljyn matka venäjältä Intiaan ja sieltä Euroopan markkinoille. BOFIT Policy Brief 7/2025.

Tags

price cap, Russia, oil, sanctions