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WORLD

Ukraine's State Energy Company Keeps Russian Gas Flowing as War Rages

An uneasy alliance between Ukraine's Naftogaz and its Russian counterpart sustains gas supply to Europe and fills government coffers on both sides of the fighting

By *Jenny Strasburg* [Follow](#) and *Joe Wallace* [Follow](#) / *Photographs by Serhii Korovayny for The Wall Street Journal*

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Even as Russian rockets have peppered its facilities, Ukraine's biggest state company has done hundreds of millions of dollars in energy business with Moscow. But the uneasy commercial truce is showing signs of collapse, threatening to sever an influx of money into Ukraine's coffers and a primary conduit of Russian natural gas into Europe.

Ukraine's NJSC Naftogaz has carried on its business of routing Russian gas to Europe since Russia invaded. Its longstanding but rocky partnership with Russian government-controlled energy giant Gazprom PJSC is so politically and financially important to both sides that neither has been willing to shut the spigot.

Yet the alliance is unlikely to survive long-term no matter what the outcome of the fighting, analysts and insiders say. The European Union has pledged to stop using Russian oil and gas by 2027.

The war has already stretched the relationship to breaking point. Naftogaz has moved to bring a legal case against Gazprom alleging underpayment by Russia as a result of its sending less gas through Ukraine in recent weeks. A Gazprom spokesperson didn't respond to a request for comment.

Naftogaz CEO Yuriy Vitrenko is racing to bolster the state energy giant so that any end to its partnership with Moscow, combined with lower production and the costs of wartime subsidies to its customers, doesn't sink the company or further drain Ukraine's public finances.

“Historically we were in the middle of Russia and Europe, transporting Russian oil and gas to Europe,” Mr. Vitrenko said. “That’s still a big part of our business despite the war.”



Mr. Vitrenko faces pressure to find billions in new financing while showing that Naftogaz is making progress on lower-carbon energy and diversification. He traveled to last month’s gathering of the world’s elite in Davos, Switzerland, and was in Washington last week asking U.S. officials to help provide as much as \$8 billion to supply Ukraine with natural gas this winter.

“That is the immediate and highest priority,” Mr. Vitrenko said of the fundraising. “We are future-proofing.”

A White House spokesman said, “We remain committed to Ukraine’s energy security and will continue to work closely with the government to identify effective solutions.”

Naftogaz is one of Ukraine's largest energy companies, with a future deeply intertwined with the country's economy. Its subsidiaries include Ukraine's largest domestic gas producer and its biggest oil producer. The company also distributes gas for heating and electric power.

In 2021, Naftogaz contributed almost 11% of Ukraine's state budget through taxes, dividends and other payments, according to Fitch Ratings. Russia paid about \$1.2 billion in transit fees for the routing of 42 billion cubic meters of gas into Europe through Naftogaz and Ukraine's state-owned transmission operator, according to the company's 2021 financials.

Moscow has sought to bypass Ukraine for years with the subsea Nord Stream pipeline, which sends Russian gas under the Baltic Sea to Germany. Germany suspended certification of a second pipeline, called Nord Stream 2, before Russia's invasion.



Ukraine funneled almost a third of the European Union's gas-pipeline imports from Russia in the final quarter of 2021, according to EU data. Since Russia invaded Ukraine in late February, the interchange has taken on a dark irony, with Russia deploying Europe's gas money to fund the war, and the transit fees Russia sends monthly to Naftogaz accounts via correspondent banks helping bolster Ukraine's defense.

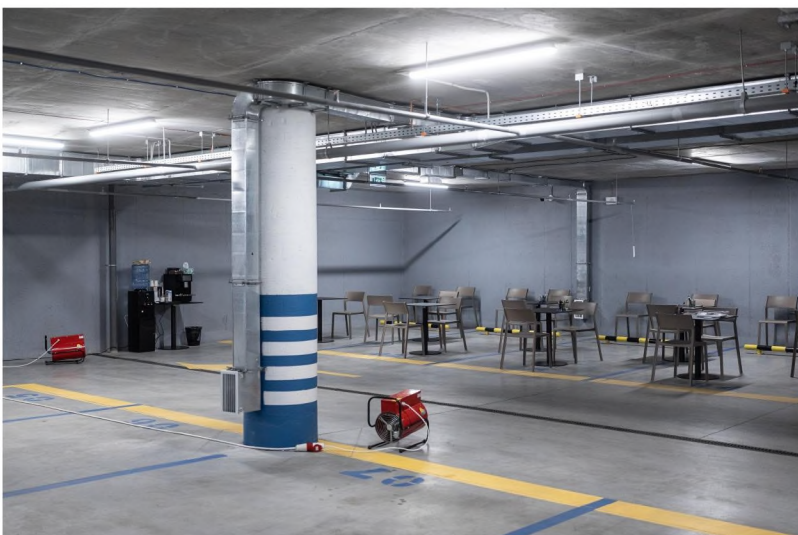
In late February, with Kyiv under attack, Mr. Vitrenko worked deep underground in a Soviet-era bunker outside the city. Over two weeks, he stepped in occasionally as cook, making pasta with vegetables for refuge-seekers including soldiers and a government minister. They worked on an electric stove, he says. The deepest bunkers don't have natural gas.

"We could not even prepare for this kind of bunker life," Mr. Vitrenko said. "Everything you had in your fridges...people would bring what they had."

Mr. Vitrenko first worked for Naftogaz two decades ago as an outside consultant. After working as an investment banker in London, he returned to Naftogaz in roles including finance and adviser to the chairman before leaving in 2007. He acted as energy minister of Ukraine for a few months before returning to Naftogaz as CEO last year.

Naftogaz employs roughly 60,000 people and says it has lost 25 employees to fighting, about half of them while on the job. Mr. Vitrenko and some colleagues are back in their Kyiv offices, with quick access to an underground parking garage that doubles as an air-raid shelter.

For much of the war, more Russian gas has flowed through Ukraine to Europe than in the run-up to the invasion. Mr. Vitrenko and other Ukrainian officials say Moscow should send even more. They have accused Russia of siphoning off supply, of failing to make up for shortfalls from cutoffs at one border crossing in Russian-occupied Ukrainian territory and of seizing control of a compressor station in the Donbas area in Ukraine's east.



If Russia were to cut flows through Ukraine to the EU, it would dry supplies and boost prices inside Ukraine, which uses some Russian gas for domestic consumption. Some analysts, industry officials and lawmakers say Naftogaz will need to produce more natural gas from Ukraine's domestic reserves to survive in a postwar future.

Damage from fighting depressed domestic production—which covered two-thirds of Ukraine's gas needs before the invasion—by about 12% in April compared with the eve of the invasion, said Iryna Sereda, an analyst at Energy Exemplar. Mr. Vitrenko has projected a full-year decline in gas production of 3% to 6% stemming from the war.

Boosting domestic gas production will depend heavily on foreign financial and technical support, Mr. Vitrenko said. But a long history of corruption in Ukraine and underinvestment in the country's gas fields present difficulties, investors and analysts say.

Mr. Vitrenko was named CEO in April 2021 when Ukrainian officials fired his predecessor. That led to the resignation of Naftogaz's supervisory board, which had been part of governance reforms required as a condition of foreign support from the International Monetary Fund and others. The board's dismantling has left the government playing that role instead.

“There's a lot of potential in Ukraine for future gas production, but a wide array of risks, even outside of wartime,” said Ashley Sherman, an oil and gas research director with energy consulting firm Wood Mackenzie.

The drop in demand and supply has made it difficult for Naftogaz to calculate how much gas it needs to import to meet Ukraine's cold-season needs. The company might need to import four billion cubic meters, which could cost about \$4 billion, likely supplied by overseas lenders, said Andrii Zhupanyyn, head of the parliament's subcommittee on gas policy.

Even as Mr. Vitrenko urges the world to shut off Russian gas, he isn't sure where or how it will be replaced. He has been working to secure Ukrainian access to liquefied natural gas shipped into Europe, but says there are no easy answers.