

The Impact of Domestic Politics and Geopolitics on Energy Supplies from Russia

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Workshop: Economic Challenges for Energy

Madrid, 10 January 2013

Russia & the seller's gas market 2000-2008

- Long-term contracts linked to oil prices ensured reciprocal dependence between Russia and its European consumers;
- Sky-rocketing oil and oil-linked gas prices creates seller's market and boosts Russia's confidence and international standing;
- Russia promotes bilateral gas deals with European nations further undermining Europe's unified energy stance;
- Better gas price deals are offered to "friendly" nations and in exchange for access to downstream assets and control over the transit pipeline infrastructure;
- Offers higher prices for Central Asian gas to hinder the development of non-Russian energy routes;
- Construction of expensive transit-avoidance pipelines



The emerging buyer's market

- Shale gas development in the United States affects markets across the globe and strategies of LNG exporters
- Traditional oil-linked prices and long-term contracts come under pressure
- Russian gas become less competitive
- Buyers seek price re-negotiation
- Gazprom starts losing its market share
- China ends Russia's gas monopoly in Central Asia
- Gazprom comes under increased domestic pressure from politically-connected "independent" producers



North America holds the golden key and ...

- Can the US shale gas success be replicated elsewhere? China and Asia – possible. Europe – unlikely.
- Will the US choose to export its gas or use cheap gas domestically as a competitive economic advantage of its industries?
- This could hurt European manufacturing and chemical industries.
- The use of more gas + unconventional oil results in more North American oil available for export.
- Will the US need to retain its geopolitical presence if it no longer needs imported oil and gas?



... China as well.

- Can the US share its geopolitical role with China?
- China is the fast growing energy importer with an impressive track record of international energy projects.
- China as a premium market for LNG
- What about gas production?
- China's role in Central Asian energy has increased while Russia is a declining power there.
- China and the new Energy Silk Route – from Iran to the Far East.



Will a price war be good for European consumers and Russia?

- Russia is likely to choose gas volumes over prices;
- Russia can afford low gas prices in external markets;
- LNG & renewables will suffer if prices are low;
- Low gas prices will change the EU energy mix in favour of gas, promoting economic recovery and undermining renewables and LNG.
- Russia-backed pipelines (Nord Stream & South Stream) could become an important leverage in terms of volumes.



What about other players?

- Central Asia and TAPI – will it promote greater stability?
- LNG battles between Qatar and Australia?
- East African gas
- East Mediterranean gas
- Iran? Russia benefits from international sanctions against Iran and together objects Caspian submarine pipeline.
- Iraq
- Arctic gas?



Geopolitics

- Big factor:
 - Increased number of suppliers; increased diversity of sources
- Gas producers are made responsible by new competition
- Producer/Consumer relations are relations of mutual dependency and are therefore stabilising
- Transnational projects are stabilising forces – eg TAPI
- Battles will move from being military to being about markets, routes, regulation, technology, competitive advantage and environment

DOMESTIC POLITICS, TECHNOLOGY AND ENVIRONMENTAL CONCERNS
WILL DEFINE INVESTMENT DECISIONS.



Domestic politics in Russia

- Liberals vs. conservatives: ideology and struggle for assets
- Gazprom's decline and Rosneft's rise
- External pressures from markets and EU regulation on Gazprom
- Need to make a jump from Soviet-era brown fields to green fields
- Pressures from Rosneft and "independent" producers to change its price model
- Rosneft becomes an active player in the domestic gas market
- Rosneft as a gatekeeper for IOC involvement in Russia
- Rosneft as the national champion responsible for green field development
- Rosneft as Russia's energy envoy in Asia



Proposed privatisation of the Russian oil sector in 2012-2016

Company	State share on 20 June 2012	Proposed state share on 31 December 2016
Rosneft	75.16%	0% (golden share)
Zarubezhneft	100%	0% (golden share)
Transneft	78.1%	75% + one share
Sovcomflot	100%	0%

Source: Russian Government order no. 1035-p, Moscow, 20 June 2012.



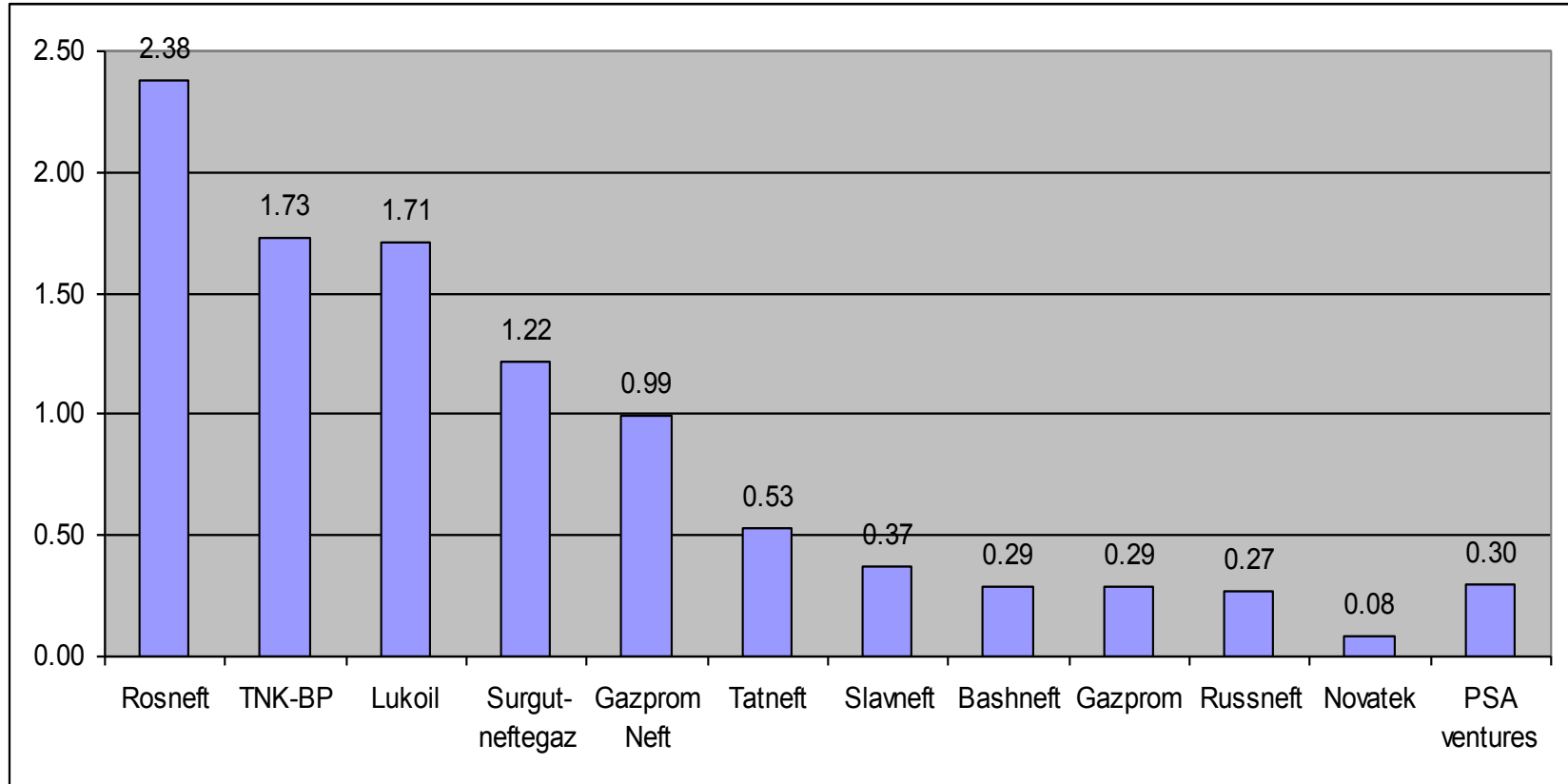
Rosneft' s enhanced role in the oil sector in 1995.

Conservative draft proposal	Yel' tsin' s final version – the decree of 1995
Commercial management of state shares in Russian oil companies	Management of non-core state assets remaining outside of the corporate structure of emerging oil companies
Managing state interests in relations with foreign companies operating under the PSA regime	Trading hydrocarbon volumes granted to the Russian state under production-sharing agreements (PSA).
Assessing projects aimed at new hydrocarbon development;	Becoming the main state contractor for research and development projects in the oil industry
Monitoring oil companies' adherence to the terms of geological and oil production licenses Involvement in state decisions on the transportation of crude oil volumes via the Transneft export pipeline network	None

Source: Ukaz presidenta Rossiiskoi Federatsii, "O pervoocherednykh merakh po sovershestvovaniyu deyatel' nosti neftyanykh kompanii", No. 327 of 1 April 1995; Shafranik' s interview



Russian liquids production in 2011, mmb/d



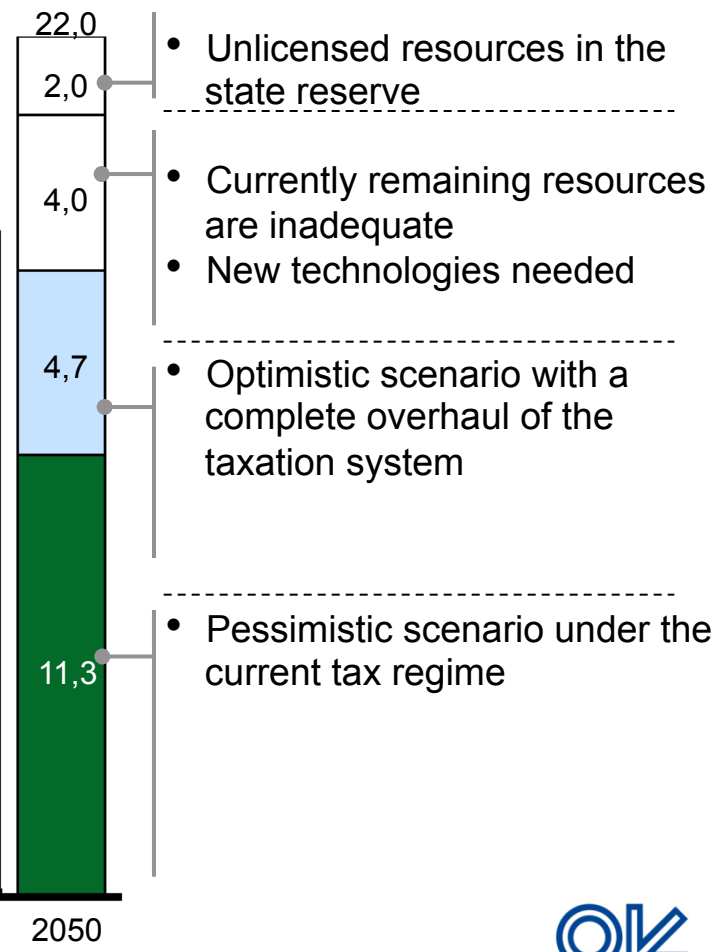
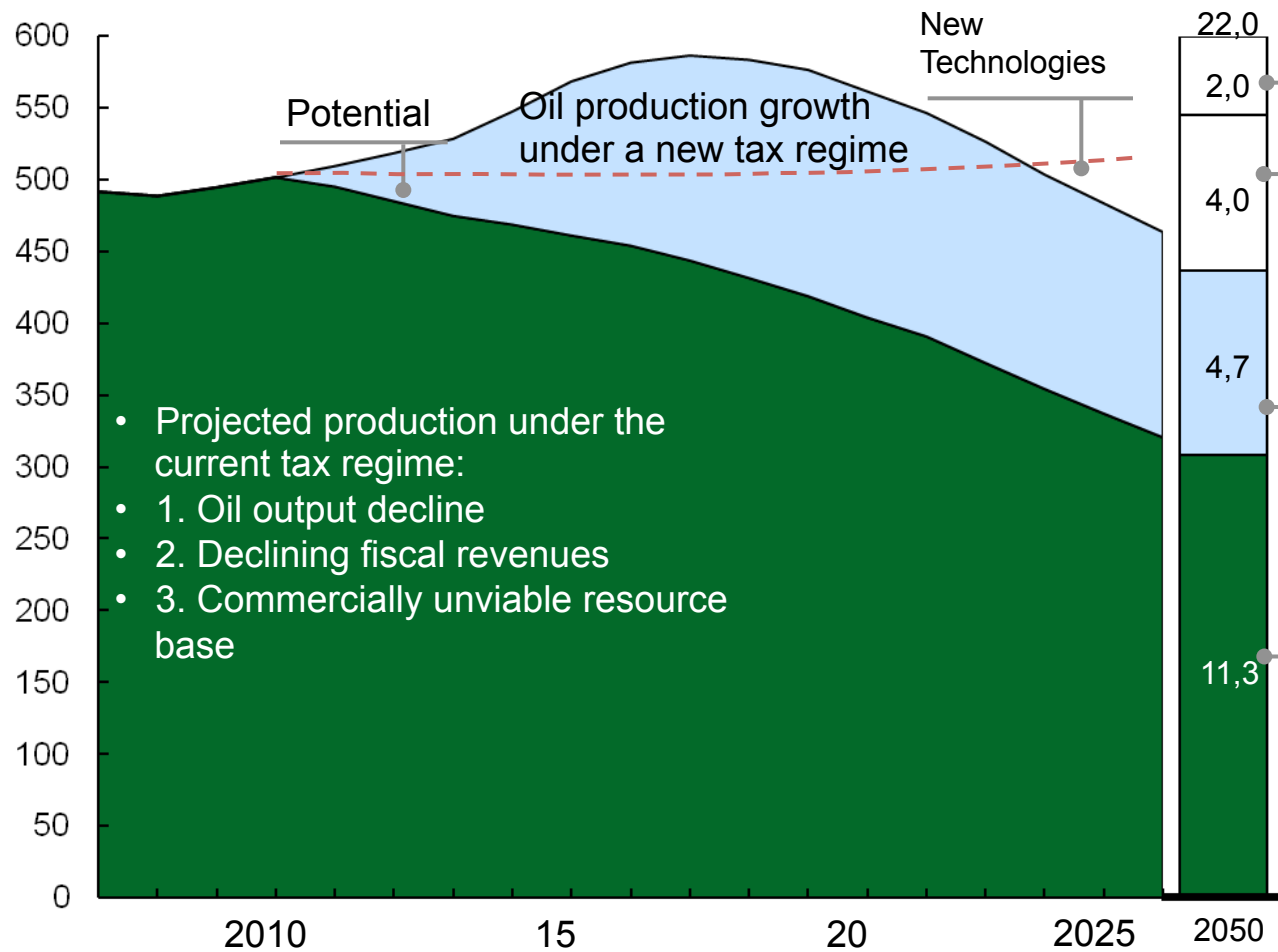
Source: Company reports. Note: Yuganskneftegaz, a former key asset of Yukos, is responsible for over 55% of Rosneft's production.



New tax system will boost oil output

Annual oil production
Million tonnes

Reserves (ABC₁, C₂)
Billion tonnes

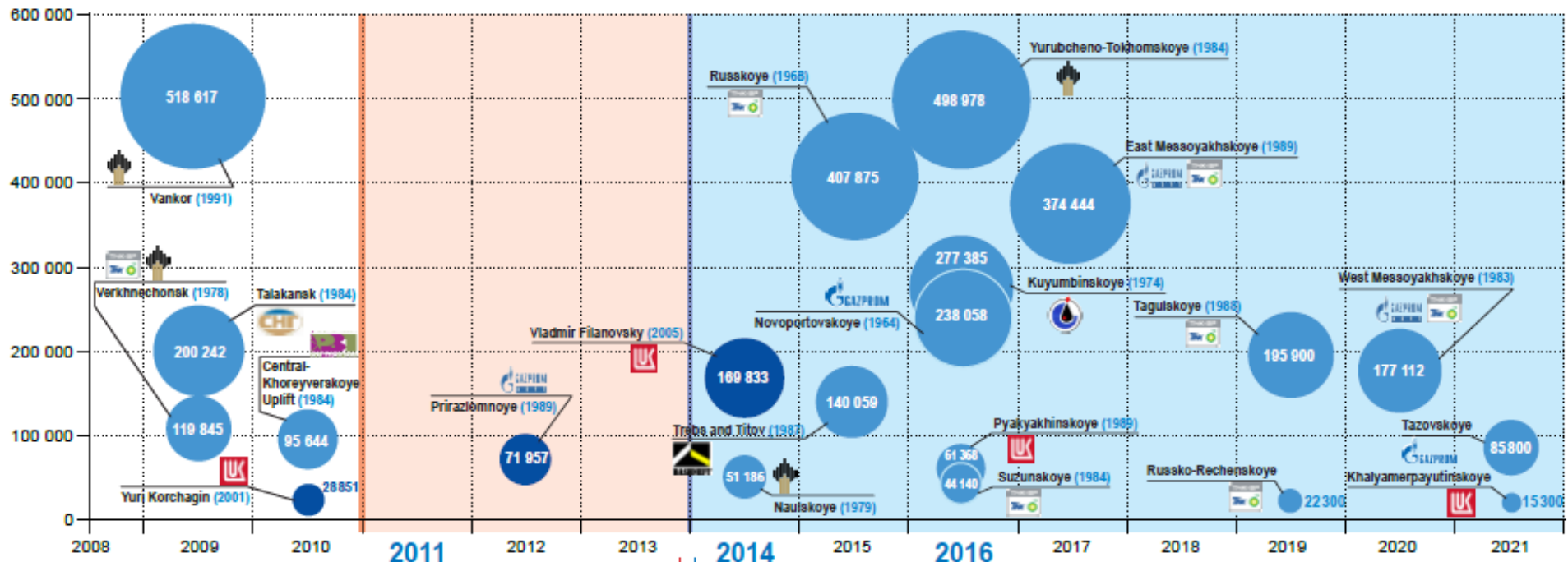


- Projected production under the current tax regime:
- 1. Oil output decline
- 2. Declining fiscal revenues
- 3. Commercially unviable resource base

- Unlicensed resources in the state reserve
- Currently remaining resources are inadequate
- New technologies needed
- Optimistic scenario with a complete overhaul of the taxation system
- Pessimistic scenario under the current tax regime



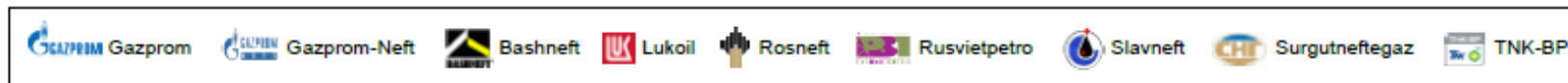
The “jack-pot” approach of Russian companies



In 2012-2013 Russia will not be developing any new fields which can maintain the current oil production level.

In 2014-16 Russia plans to start developing more hydrocarbon fields.

Licence holders



Rosneft + TNK-BP

	Rosneft	TNK-BP	Combined
1P hydrocarbon reserves (bn boe) ⁽¹⁾	23.4	14.9	38.3
2P hydrocarbon reserves (bn boe) ⁽¹⁾	35.1	30.0	65.1
Oil production 2011 (kbpd) ⁽²⁾	2,380	1,742	4,122
Gas production 2011 (kboepd) ⁽²⁾	206	245	451
# of refineries in CIS ⁽³⁾	7	5 ⁽⁴⁾	12
Total net capacity (kbpd) ⁽³⁾	1,048	772 ⁽⁵⁾	1,820



Rosneft Assets

- Greenfield Projects
- ◆ Gas Projects
- ▲ Brownfield
- Refining Assets

TNK-BP Assets

- Greenfield Projects
- ◆ Gas Projects
- ▲ Brownfield
- Refining Assets

Source: Company information

Note: (1) PRMS reserves as of 31-Dec-2011

(2) Including shares in affiliated companies, not including ITERA

(3) Including non-controlling stakes and Rosneft's four mini-refineries in Russia

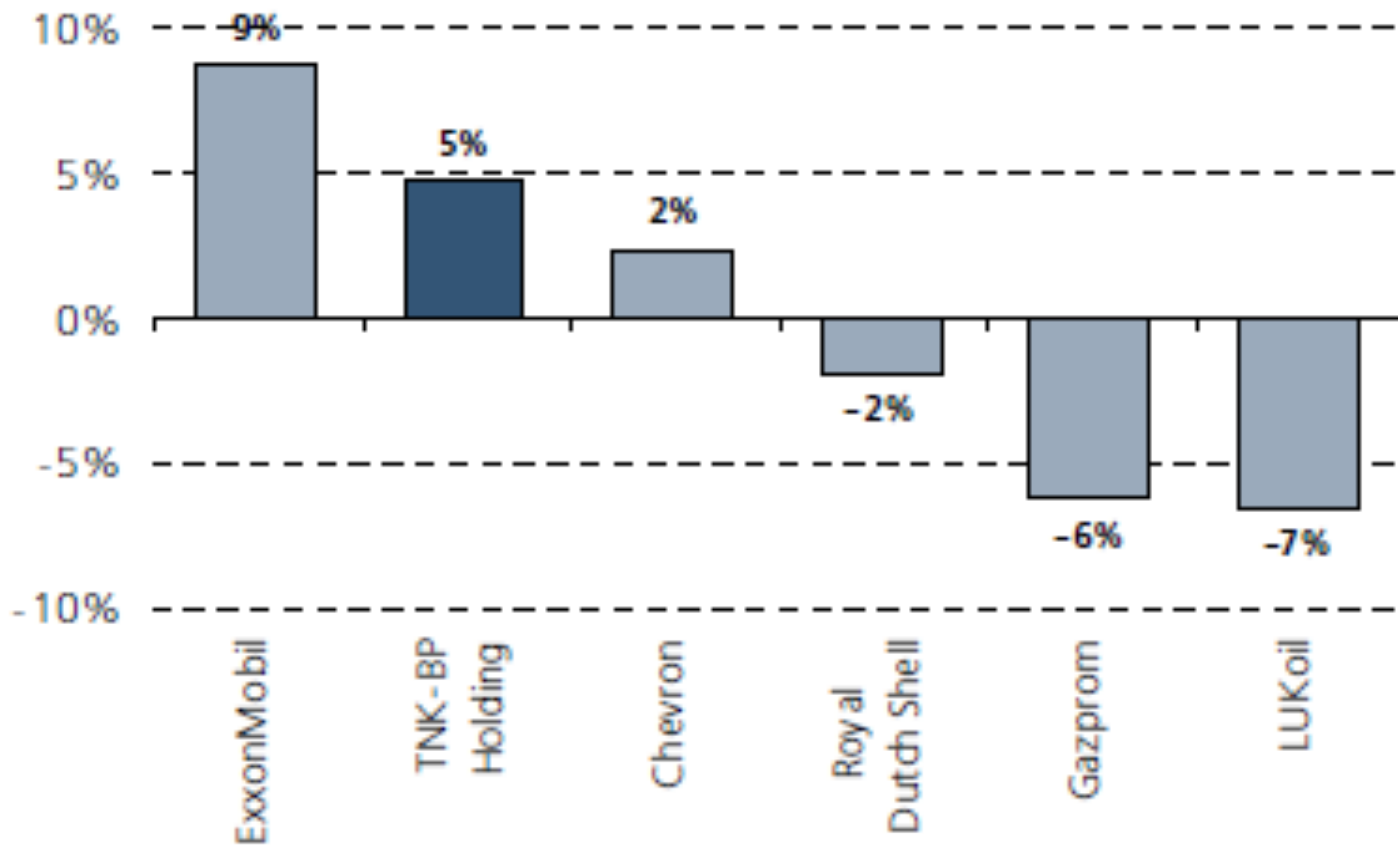
(4) Excluding Nizhnevartovsk and Krasnoleninsk refineries

(5) Excluding share in Mozyr refinery

Source: Rosneft Investor presentation, October 23, 2012.



Change in oil and gas output, 2007-11*



*oil output for TNK-BP Holding and LUKoil

Source: Companies



Forthcoming publication:

When markets meet politics : Decoding Russia' s oil industry

by Ahmed Mehdi & Shamil Yenikeyeff,
OIES: Oxford, February 2013

