
Russian Oil Exports - Changing Directions

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Introduction

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Russian Oil Production/Exports - Current Picture

- **Oil is the number one energy asset of Russia - second largest oil exporter after Saudi Arabia**
- **After significant declines following the dissolution of Soviet Union, Russian oil production has rebounded to approximately 9 mbd and is expected to reach 9.5 mbd in 2005**
- **Approximately 5.2 mbd of Russian oil production was exported in 2004**

Russian Oil Production/Exports - Current Picture (cont'd)

- **Russian oil exports are achieved by means of pipeline (60%), rail (33%) and barge (7%) - our focus today is on pipelines**
- **Russia's current oil export pipeline capacity is approximately 4 mbd**
- **Two-thirds of current Russian oil exports are to Central and Eastern Europe (includes exports to Germany)**
- **Artificially low domestic prices for oil that cannot be exported**

Russian Oil Production/Exports - General Trends

- **Substantial oil production growth since 1991, but growth is now slowing - reasons include the "Yukos Effect"**
- **Increasing export costs - rouble/dollar exchange rate has contributed to recent increases, but so too have tax increases**
- **Non-CIS exports stagnant or falling**
- **Exports by rail declining from historical peak in 2003 and major destination shift from Black Sea ports to China (rail only)/Barents Sea**
- **Substantial investments in extra export pipeline capacity are proposed**

Existing Russian Oil Export Pipeline System

- **General Characteristics**

- Transneft monopoly on crude pipeline transportation
- Physical/commercial bottlenecks and inefficiencies (particular constraints in northern and arctic regions)
- High tariffs and taxes (oil export tariff raised to a record \$140 per ton from 1 August)
- Reliability/safety issues
- Debate as to introduction of effective quality bank system
- Oil producers have expressed discontent with Transneft's tariff structure, its export pipeline routes and its access priorities

Primary Russian Oil Export Pipeline Routes

- Transneft network comprises almost 49,000km of oil pipeline



Political Considerations

- Role of Transneft as an instrument of the Russian State
- National aspirations to diversify export routes
- Key oil export directions (current and proposed) are (1) East to Asia (2) Baltic Sea and (3) Black Sea
- Geopolitical aspects
- Precedence will be given to sea ports/projects in which Russia has a stake (will discuss in context of BPS)
- Potential role of private investors in export infrastructure projects at the expense of Transneft - Premier Mikhail Fradkov has previously stated that there will be no private pipelines in Russia, while Transneft's president has stated that "The current situation where oil companies are themselves determining their export volumes, in my opinion, is not right"

Case Study 1: Far Eastern Oil Pipeline

- **The Project:**

- Transneft proposal calls for Phase 1 from Taishet to Skovorodino (30 mt per year capacity) with rail shipments from Skovorodino to Pacific until Phase II. Estimated Phase I cost is \$6.5 billion. Phase II involves expansion of Taishet to Skovorodino line and extension of pipeline to Pacific coast, bringing total pipeline length to around 4,000km and project total cost to around \$11.5 billion. Construction is intended to begin in Q3/Q4 2005



Case Study 1: Far Eastern Oil Pipeline

- **Drivers:**
 - As Western Siberian reserves decrease, Eastern Siberian exploration hoped to increase
 - Massive increase in energy consumption by China, Japan and South Korea (but branch line to China not certain)
 - Russia's Asian geopolitical priorities
 - Attractiveness of Eastern Siberian oil investments questioned by some analysts - production will need to receive export prices (c.f. local prices) in order to be profitable
 - Increases Russia's ability to select buyers - increases diversity of export routes

Case Study 1: Far Eastern Oil Pipeline (cont'd)

- **Hurdles:**
 - Project success depends on exploration results from Eastern Siberia (oil supplies rather than demand tend to drive oil pipeline projects). An estimated \$7b in upstream exploration/production investments will be required. Large-scale licensing needed in the immediate future
 - External finance (particularly for Phase II)
 - Environmental concerns with routing - Lake Baikal UNESCO reserve
 - Pipeline faces competition from state-owned rail, which is seen as more efficient at current volumes (volumes expected to be 10mt in 2005 and 15mt in 2006 by rail). Investments in 2005 for Russia's main railway company (RRC) include resources for infrastructure to increase oil exports to China

Case Study 2: Baltic Pipeline System (Expansion)

- **The Project:**
 - BPS commenced operation in December 2001
 - Proposed expansion of Baltic Pipeline System in 2005-06 from 47.5mt per year to 62.5mt per year. Completion targeted for Q1 2006



Case Study 2: Baltic Pipeline System (Expansion) (cont'd)

- **Hurdles:**
 - Definite schedule for expansion and finance obtained, but proposed Indiga Project and expansion of Varandey (advocated by Lukoil) would likely divert Timon Pechora volumes
 - Lukoil and Rosneft have been slow to commit additional volumes to the BPS
 - Baltic states concerned that expansion will deprive them of Russian oil transit revenues

Case Study 2: Baltic Pipeline System (Expansion) (cont'd)

- **Drivers:**
 - BPS originally constructed to provide enhanced transit from Timon-Pechora and Western Siberia basins in an "all Russian" system to the all weather port of Primorsk - high political motivation
 - Direct outlet to northern European markets
 - Reduces dependence of Russia on transit services of Latvia, Lithuania, Estonia and Finland

Case Study 3: Black Sea - Bosphorus By-Pass Projects

■ The Projects:

- **Burgas - Alexandroupolis** (April 2005- participant countries sign a memorandum of Cooperation. Interested parties include TNK-BP, Lukoil, Gazprom, Rosneft and Hellenic Petroleum)
- **Burgas - Viole** (December 2004 - participant countries give "go-ahead". The project has EU support and finance arranged from OPIC, CSFB and others)
- **Constanta - Trieste** (June 2005 - participant countries sign agreement endorsing project. BP, OMV and Chevron Texaco are among interested parties, the project also has USTDA support)
- **Kiyikoy - Ibrikhaba**
- **Samsun - Ceyhan**
- **Plotsk - Brody**



1 Burgas-Alexandroupolis
2 Burgas-Viole
3 Constanta-Trieste
4 Kiyikoy-ibrikhaba
5 Samsun-Ceyhan
6 Plotsk-Brody

— Existing pipelines
..... Projected pipelines

Case Study 3: Bosphorus By-Pass Projects

- **Drivers:**
 - Bosphorus shipping congestion concerns and associated transit costs - the "Turkish Knot"
 - Environmental concerns

- **Hurdles:**
 - Uncertainty of future available oil volumes at Black Sea ports
 - Ability of project sponsors to obtain through-put commitments to support project finance
 - Samsun - Ceyhan option needs to overcome general wariness of exporters in placing "too many eggs in the Turkish basket"

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