Russia’s Oil & Gas Strategy: Challenges & Changes

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Russian oil production is peaking

- Size and quality of new discoveries deteriorates
- Ongoing projects enter depletion phases
- Tight reserves are a challenge for existing technologies
- Tax incentives are inadequate; PSAs are banned
- Industry is dominated by inefficient state-controlled majors
- Foreign operators are discriminated
- Western sanctions are in effect
- Low oil prices make a lasting effect
Government’s outlook of Russian oil production, mln tpy
Oil production in Khanty-Mansi Autonomous District, mln tpy
Oil companies’ outlook of Russian oil production, mln tpy
Taxes in oil price, $ per bbl
### Breakeven cost of Russian crude, US$ per barrel
(estimated average if sold at $30 per bbl)

<table>
<thead>
<tr>
<th>Category</th>
<th>Cost (US$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lifting (opex)</td>
<td>$7.00</td>
</tr>
<tr>
<td>‘Amortization’ (capex)</td>
<td>$4.00</td>
</tr>
<tr>
<td>Administrative &amp; marketing</td>
<td>$4.50</td>
</tr>
<tr>
<td>Transportation</td>
<td>$4.50</td>
</tr>
<tr>
<td>Main taxes (MET &amp; export duty)</td>
<td>$12.00</td>
</tr>
</tbody>
</table>

**Total:** $32.00

Expected profit is not included, and the government wants to increase taxes.
What oil companies are doing to save funds and stay in the black?

- Attacking the government with complaints
- Cutting investment programs and current expenses
- Cutting credit exposure
- Dropping greenfield plans
- Focusing on brownfield projects with capex long gone:
  - Enhancing recovery from developed plays
  - Changing ‘optimal’ development plans in favor of quick gains
  - Provoking faster depletion
Russian natural gas: a political weapon?
Three powerful factors are making Gazprom change its business strategy:

1. Gas production glut vis-à-vis shrinking markets

2. The Europeans’ determination to enforce antitrust environment and resist Gazprom’s ‘offensive’

3. Low energy prices
Gazprom’s producing potential totaled 617 bcm, but the company sold only 444 bcm in 2014:

- 126.2 bcm beyond ex-USSR
- 48.0 bcm in former USSR
- 217.2 bcm domestically
- 52.6 bcm of resold non-Russian gas

The volume of ‘unwanted’ Russian gas: officially 173 bcm, but actually over 225 bcm

Gazprom is pulling the brakes on new upstream projects and desperately seeking new markets
Russian Gas Exports to Europe, bcma

Guaranteed Contracted Volume (GCV)

Gazprom may be facing a price war soon

The company’s ‘worst case stress’ scenario was for $169 per 1,000 cu m

Now it expects the price in Europe to average $166 in 2017-2018

How long can Gazprom go on at lower prices?

- Excessive production potential
  - Developed infrastructure
  - Government assistance

No real plans to dismantle Gazprom are on the agenda
Thank you

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