THE CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE

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ANDERS ASLUND: Ladies and gentlemen, my name is Anders Aslund. I’m the director of the Russian and Eurasian program here at the Carnegie Endowment for International Peace. For me personally, and for the endowment, this is really a great pleasure and a great honor to introduce to you Alexander Medvedev, who is deputy chairman of Gazprom’s management committee and director general of Gazexport. He will talk to us today about an energy vision to link our nations. This is one of the big questions today: How will Gazprom reach out into the wider world, and will it also reach the United States?

As you know, there is a big project that is discussed in this regard. I think everybody in the room is aware of how important Gazprom is. Do you know that Gazprom today is the 40th biggest company in the world in terms of market capitalization at $100 billion? I heard recently a presentation by another Gazprom official pointing out that Gazprom could very well increase 10 times in market capitalization in the next 10 years and become the biggest company in the world. It is the most important company in Russia and all of us here are interested in Russia and energy.

So without further ado, I’ll give the floor to Mr. Medvedev. Thank you and welcome.

(Applause.)

ALEXANDER MEDVEDEV: Ladies and gentlemen, thank you for the opportunity to discuss today’s joint stock company Gazprom and its subsidiary, Gazpromexport Limited.

Gazprom is the world’s largest natural gas producer, and Gazpromexport is by far the world’s leading commercial gas exporter. First I will profile these companies, including their key business results and strategic priorities. After that I will highlight our projects aimed at the U.S. market and discuss the issues relevant to them.

I will start by talking about Gazprom, about our growing appeal to investors, our aspirations and our diverse activities related to serving international markets. Then I will focus on Gazexport, the 100-percent Gazprom subsidiary that just received the new name, Gazpromexport, and then on our European business and our U.S. focus. I hope this presentation will illustrate the strength and reliability of Gazprom and its subsidiaries.

On this slide you can see key data on Gazprom activities, including last year’s results, which were the best ever by every measure. And today we can assume that 2005 will top last year, and it was just two days ago confirmed by results for the first quarter of 2005 in accordance with international accounting standards, which really confirms our
aspirations and predictions, because in all major figures it’s better than the first quarter of 2004 by at least 30 percent.

As already mentioned, Gazprom is the world’s biggest natural gas producer and exporter, as well as the owner of the world’s largest gas transmission system. We have been supplying major volumes of natural gas to Europe for nearly 40 years and they have earned their highly regarded reputation for reliability. One of our key growth objectives is to repeat our European success in new markets with the United States being the central focus.

I especially like this slide because Gazprom reserves have brought it to the world’s leadership, not only in gas reserves but also in the carbon reserves in total. I find this slide very comforting for us. I’m sure our customers do too. I’m pretty sure our competitors don’t, however. Furthermore, I must note that recently Gazprom acquired Sibneft, a major Russian oil company, for over $13 billion. We didn’t include Sibneft reserves in this slide, but it could only improve. With Sibneft reserves, our leadership will increase even more.

This map shows the regions of Gazprom’s natural gas production and the outline of our unified gas transportation system. This Western Siberian reserve has the transportation system as the foundation of Russian exports and Gazprom’s pride. The green symbols represent new projects of gas production and transmission in the Western part of Russia. Given the world-class scale of these projects, each of them can be called unique. Indeed, the energy industry commonly refers to a number of our fields as a “super-giant.” More about these projects later in my presentation.

Now I would like to point out that market confidence in our company has been growing steadily. The rushed development of Gazprom market capitalization and credit ratings is a clear achievement. Just last week, Standard & Poor increased Gazprom’s rating from BB- to BB. Over the last two years our market capitalization has almost quadrupled to over $115 billion. We expect this trend to continue and reach $300 billion over the next several years. If you will take away one personal insight today, it should be very simple: When you can invest in Gazprom, do it now. These achievements are beneficial not only to our investors but also to our customers and partners in consequence our ability to grow our business under the longstanding banner of strength and reliability.

And now let me turn to Gazprom’s international activities. This is my main responsibility as deputy chairman of Gazprom management committee and the director general of Gazpromexport.

International business is central to Gazprom and will stay central to Gazprom in the future. We didn’t reach the situation in which our local sales are in black yet. That’s why international sales is a key to our prosperity. It provides significant revenue to the company. We have decades of experience to build on and our increasing reach provides better sales efficiency and stabilizes our revenue.
Gazprom’s goal is to become a state-of-the-art international energy company. That is why its policy is based on a three-pronged approach: conducting company liberalization to eliminate investment restriction for foreign capital; diversify our product range to include LNG, power generation and distribution, petroleum and petroleum products, and emission trading; and last but not least – (unintelligible) – our markets by entering new geographical regions and energy businesses.

And other key strategies I will pursue: a vertical integration. Over the long term, vertically integrated energy companies over-perform those that are not. This strategy implies three ways of development. Production – here the key word is growth, growth in production at existing fields, in developing new fields and regions, and conducting large-scale geological exploration. The second one is transportation. The key word, enhancement – revamping existing infrastructure, developing new roads, building up our European transportation storage assets, and launching LNG initiatives. I would like to stress that more than 50 percent of our investment program is devoted to transportation, and this tendency will prevail in the future. Again, last but not least, sales and distribution. Here the key word is efficiency. This implies entering new markets such as the United States, optimizing our presence in our key markets, diversifying our contract portfolio, and getting closer to the ultimate goals: consumers.

Now let me tell you about the traditional core of Gazprom international business – European gas market – and about Gazprom’s exports and Gazpromexport.

On this slide you will see three stages of the development of Gazpromexport as well as the Russian gas exports in general have seen in almost 40 years. As you can see on this slide, export volumes have been rising throughout the entire period. In 2004 we have delivered almost five tcf [trillion cubic feet] of Gazprom’s gas to our customers in Western, Central and Southern Europe, excluding former USSR republics.

Now we can say that we’re in the first stage of export development, whose main features are entering such new markets as the United States, expanding our product portfolio by adding oil, petrochemicals and electric power. So Gazpromexport, which – (unintelligible) – is not just the biggest gas exporter in the world, it’s the single export channel for all Gazprom rising exports as well as the only export channel for the gas produced in Russia.

In order to meet the challenges of the weekly change in the world market, we open the fourth period in Gazprom history and we are carrying out reforms to adopt the market changes and to our new growing business. Gazprom’s entire international activities are being consolidated under a single umbrella. That is why we are reorganizing our export arm, Gazpromexport and Gazprom International Business Department.

I’m sure most of you are aware that hockey is popular in Russia. Gazpromexport has had a company team for many years. In fact, this team is in the United States now to play several NHL alumni teams. And the relevance of this is that for many people the
most important change is that we have renamed our great hockey team to be Gazpromexport. (Scattered laughter.) Moreover, in the recent history we saw at least two lockouts in the NHL, which is absolutely not tolerable for us. We even have been prepared to replace – if lockout will continue, to bring our hockey team to play and to enjoy hockey audience here.

This is now our unified gas transportation system in the (unintelligible) of the European gas transportation system. We all have rights to a number of significant transportation storage assets in Europe, including the biggest underground storage in Germany – (unintelligible) – as well as interconnector tying the U.K. with the Continent. We’re well integrated into Europe and I do believe that one day we will operate a similar pipeline system in the United States, either through direct ownership or by contract – (unintelligible) – hockey.

On a more serious note, my comment reflects how high we set our goals. The largest single new European development which we have underway is the North European gas pipeline. Last month we have signed the basic agreement on the North European pipeline with our German partners BASF and E.ON Ruhrags. This pipeline will enable us to deliver additional volumes to meet growing demand in Germany and other European countries starting in 2010. Ultimately, with the second phase completed, this pipeline will have an annual capacity of 1.9 tcf and its seabed section will be 744 miles long.

Here I would like to present a few of Gazprom’s – (unintelligible). We are the company that builds the Blue Stream through Black Sea. Now it’s the deepest underwater gas pipeline in the world. We are the company who will build the North European gas pipeline through the Baltic Sea that will be the longest underwater gas pipeline in the world.

And as a company, well, sometimes we also set our different kinds of records – (laughter) – for example, negotiations with Sweden to deliver gas for 35 years. But I hope that finally those negotiations will be finalized with the possibility to have a connection pipeline to Sweden from most European pipelines.

So far I have been looking to the West from Russia. Before I turn to the United States I would like to use a few slides to outline our activities in other parts of the world, in Asian Pacific region. We have a number of world-class activities focused in this direction. This will impact the global energy supply-demand balance. The main point I should stress here is that Russia has vast and well-located gas reserves while the demand in the Asian Pacific is soaring year after year. According to some studies, gas demand in China, South Korea and Japan can reach up to 14 tcf by 2020. I would like to point out that in the most optimistic forecast of demand, that we are able to satisfy a great part of this demand in this huge and fast-developing region. I made this clear at our recent presentation in Beijing by saying that our competitive offer is to meet the region’s energy needs and that we are ready to enter into real commercial negotiations to reach an agreement with a potential of takers very soon.
Our Eastern Siberian Far East initiatives are large and complex projects. To improve their economic viability Gazprom has worked out an Eastern Siberia and Far East development program, together with our national government. We expect it to be approved before the end of this year or early next year at the latest. The program allows pooling of the resources, aligning the interests of all the stakeholders, and specifies large-scale projects that should be attractive to investors all over the world.

Talking about our activities in Europe and the Asian Pacific region was the easy part of my presentation. Now I would like to move to more serious business closer to your home: our plans for the United States.

First of all, I would like to say that Russian gas is just as attractive to the United States customers as the U.S. market is attractive to the Russian gas supply, to Gazprom. On this slide you can see the reasons behind it. Here I would like to stress the issue of diversification. The U.S. market is a great opportunity for our market diversification strategy while Russian gas supplies will provide the United States with a great opportunity to diversify its energy supplies. This is truly a win-win situation.

As you probably know, Russian gas can reach the United States in two ways. It can be delivered to the West Coast from the Eastern part of Russia or it can be delivered to the East Coast from the Western part of Russia. I believe this fact once again shows that while oceans separate us, we are neighbors in the global energy market. One famous writer once said that tall fences make good neighbors. Maybe, but to take our Russian-American energy dialogue to a step further, I think we should use a different image: an energy bridge makes good neighbors.

Now let me start with the Sakhalin 2 project, which is located in Russia’s Far East. This is a Shell-led project aimed at Asian and North American markets. It was recently highlighted as Gazprom’s – (unintelligible) – in holding talks about entering into this project. In fact, Gazprom and Royal Dutch Shell signed last July an assets – (unintelligible) – sheet. Under this accord, Gazprom will acquire from Shell a stake of 25 percent plus one share in Sakhalin 2 project, while Shell will get access to Gazprom North Siberian gas assets, namely in – (unintelligible) – of Zapolyarnoye gas field. And when the deal is completed, we will jointly start delivering – (unintelligible) – to terminals in North America and the Far East.

Another interesting project under our consideration is a thousand miles West, back to the Western part of Russia. As you can see, one of our energy projects is not linked directly to any gas field. Instead it will potentially use our unified gas transportation system as a source of gas. The liquefaction plant was in a capacity of 5 million – (unintelligible) – under consideration near St. Petersburg. This project could come onstream in 2009.

Our key project – LNG project is Shtokman. This offshore gas field is located in the Bering Sea and contains more than 113 trillion cubic feet of gas. That’s more than
one-half of total U.S. gas reserves. One of the features of this project: its flexibility allows us to produce additional volume of gas based on the market conditions while the project phase one will enable us to produce up to 15 million tons of LNG a year starting from 2010.

Just months ago, Gazprom announced a short list of companies that had applied to participate in the Shtokman field development consortium, and that now would be invited for detailed commercial talks. Two of them are U.S. corporations: Chevron and ConocoPhillips. The rest are European. Two are Norwegian companies – Hydro and Statoil – and one French, Total.

In the spring of 2006 Gazprom will be able to select the best two, or maximum three, companies for our consortium that will turn the Shtokman project into reality. We believe that that the consortium will be truly successful if its participants can help Gazprom become a local player in the midstream and downstream business. We realize that entering new markets will not be easy. Entrenched players are usually strong in protecting their market positions, so our business can have significantly – (unintelligible). We have set ourselves the following objectives to guide us wherever Gazprom moves downstream.

Number one, we aim to reach the end customer. Number two, we strive to avoid conflicts of interest. We appreciate our current customers and the value they bring to the gas sector, but we do want to be treated as equals. Number, three, we understand the need to establish constructive dialogue with industry regulators. We plan to do so by working together with them in order to understand regulatory issues and to explain our own position. Sometimes it will not be easy. However, our strategies don’t include playing from the penalty box. We have a clear idea of what we must do and we draw encouragement from Henry Ford, who once said that if you have enthusiasm, you can achieve everything.

This slide shows in a nutshell how we see Gazprom LNG activity in the United States developing over time. At the moment, we have already established an LNG market and – (unintelligible) – activities and are working through the next phase, joining the Sakhalin LNG project. In the future, as I already mentioned, we will enable large-scale LNG deliveries from our own projects, namely Baltic LNG and Shtokman. But to do so, we need to implement the key phase of becoming co-equal players in the United States gas market. We need to get access to local distribution and marketing infrastructure, and we will achieve it.

Now I will have to disagree with – (unintelligible) – who said something like, if you want to make God laugh, talk to him about your plans. Last year we have announced our plan to begin marketing – (unintelligible) – LNG in the United States in 2005. We launched our deliveries with carbon delivered to the LNG terminal in Cove Point, Maryland. The deal was that we bought LNG from BG in Egypt, delivered it to Cove Point and sold it to Shell there. This is how we begin to run the first phase of our LNG
plan. Now we are looking for additional – (unintelligible) – LNG use based on our possibility to swap pipeline gas and LNG.

Here is a slide from the briefing we held on September 2, 2005 upon arrival of first LNG cargo to the United States on a beautiful day on Maryland’s Chesapeake Bay less than two hours’ drive from Washington, D.C. By the way, the rest should be sure that we deliver even in the bad weather.

I want to take a moment to address our social responsibility and our support of social and cultural events in Russia and abroad. Gazprom is a good, proactive corporate citizen with extensive support of cultural and social programs. Being one of the top contributors to Russia’s budget, our company feels responsible for helping our society to create favorable conditions for the development of the personalities. Following this idea, Gazprom reaches a helping hand to artists, musicians, athletes and to many others. It’s well known that Gazprom supports the Russian Olympic Games team and many international sports events. In addition to sports, we sponsor many cultural projects. And the most important, we never forget those who need our help more than others: veterans, disabled and orphans.

Let me summarize a few points here. My presentation has clearly shown, I hope, that we are focusing on two main markets challenges. The first one is to increase our presence in Europe while adapting to market changes such as liberalization and declining local production of gas in Europe, and to expand into the new business segments. The second one is to open new markets in the Asian Pacific region and the United States. We are pursuing large-scale LNG projects to sort of both East and West U.S. coasts, aiming to achieving the same degree of success there as we have done in Europe. To do so, we need positive business environment, which we can best develop within the framework of U.S.-Russian energy dialogue, and we’re working on it together with the Russian Energy and Industry Minister Viktor Khristenko, a cochairman’s forum which will held in Houston at the beginning of next week. In the next few days he will be having meetings in the White House and will sit down to talk to the top U.S. energy officials. Clearly, both our countries are keen to have reliable and affordable energy sources. Our cooperation can make it possible.

In all of our efforts to grow a global business we try to create a strong team spirit. Our ambitions go beyond leadership in the energy sector. We also try to stay fit by diversifying into sports and playing a good game. Here we come a long way. Our greatest success has to do with our hockey team. Of course we had our main win this year when we have beaten Detroit Red Wings veteran team, headed by – (unintelligible). Our team will play a rematch in Detroit this visit. I hope we’ll beat them again. (Scattered laughter.) I’m really pleased to invite you also to visit, if you will have a chance, our game, which will be before the Shell game of this Saturday when we will play Washington Capitals veteran team. And anyone willing to challenge our team is welcome.
Ladies, and gentlemen, thank you very much for your attention. I am pleased to answer your questions.

(Applause.)

MR. ASLUND: Thank you very much for a very efficient and comprehensive presentation.

Without further ado, the floor is open to questions. I am convinced that there are many important questions here, seeing who is around in the room. Who wants to start? Let’s see, down there. Yes, please. And please introduce your name and institution also.

Q: Gregory Fifer for National Public Radio. Mr. Medvedev, Thomas Graham of the National Security Council said last week that U.S.-Russia energy cooperation was largely untapped because of U.S. support for democracy, or projects supporting democracy, which are misconstrued in Russia. Can you comment on that, please? Thank you.

MR. MEDVEDEV: I am really surprised to hear that democracy is in danger in Russia. I believe that Russia is in a stable way for democratic development, and if it’s necessary I could prove that any version of corporate history of Russia is not in contradiction with this. So I could do it publicly or individually if you want. And that’s why I believe that Russia – U.S.-Russia energy dialogue is aiming to create the conditions that we will stop talking about energy cooperation but will end in real projects to deliver oil and gas to the United States, which I believe is key for energy security of the United States.

MR. ASLUND: Martin Walker, UPI.

Q: The NATO supreme commander, General Jones, last week suggested that one of the issues that would have to be on the agenda at the next NATO summit in the next meeting with Russia would have to be joint efforts to secure the pipelines and the other routes bringing Russian natural gas to the West, to Europe and down the road to the USA. Have you had any preliminary discussions on this? Are you planning any? And what thoughts do you have on the issue of pipeline security?

MR. MEDVEDEV: You see, pipeline transportation is a major transportation for us, for our export and for our local market. And we – the West, not only in Russia, to support our transportation system but also abroad. For example, we have a common project – joint project to secure supply of Central Asian gas, which will flow through our Russian territory to the European markets and also to Ukraine. And the potential involvement of the third parties in such projects should be carefully analyzed because unfortunately we have a history of creation of consortiums – idea of to create a consortium between Russia, Ukraine and Germany which is falling apart, not due to the fault of Russia or Germany. And obviously Ukraine is playing an important role as a transit country, but from the other side, Ukraine is heavily dependent on supply of
Russian and Central Asian gas for their own needs. And this balance of interests is a prerequisite that first of all export transit will not be in danger as well as the supply of Ukraine will not be in danger.

MR. ASLUND: Thank you.

Dimitry Sidorov of Kommersant.

Q: Actually, I think that the Shtokman field project is like 15 years old already, isn’t it? And basically it’s not a secret for anyone who is sitting in this audience that Gazprom is politically influenced by whatever then – again, the policy of the Russian government is. How the U.S. investors can be safe in a way that if the situation between the U.S. and Russia – I mean, political situation and political relations between the U.S. and Russia will change for the worse, they will still secure the place for – well, their place to develop the Shtokman field? Thank you.

MR. MEDVEDEV: Well, first of all, the history of Shtokman is longer than 15 years. The first discussion between the Soviet Union and the United States about the Shtokman project started in the ’70s and was successfully developed, but then was deteriorated on political reasons and then on economic reasons. Now we can back to this project in a completely new environment. First of all, I believe that we have very good political background for the project, and secondly, economics of the LNG supply to the United States is so obvious that Shtokman gas will be absolutely competitive too. And I would like to stress once again, Shtokman is much closer than any other LNG supply – than any other LNG supply to the United States.

So, in respect of the dependence and interdependence, I’m very often facing the question, is it – and even to reading some strange statements of various authorized international authorities, like for example, International Energy Agency, which put in question the reliability of the supply from Russia due to the monopolistic ambitions of Gazprom, which looks really ridiculous. First of all, though being a monopoly in Russia – (unintelligible) – Gazprom is operating internationally on a very competitive environment, because we are facing competition in Europe from Norway, from Algeria, from Libya, and from England, though the production is declining in Great Britain but still U.K. is substantial player in the market. That’s why we are not only participant of liberalized market; we have been one of the pioneers of liberalization of the market in Germany when in ’91 when there was nobody thought about liberalization. In Europe we have created a joint venture with BASF named WINGAS, which is today 15 percent market share in Germany, in – (unintelligible) – market; in operation – (unintelligible) – a competitive situation against other players of the German market.

So we are not just, say, following the course of liberalization; we are one of the founders of liberalization in Europe. The same is applied to the United Kingdom where our company is already delivering four bcm of gas annually under fully liberalized terms. So we’re fully equipped to play a role in accordance with the prevailing market conditions.
And again, it’s not one-sided dependence. As well as the importer is dependent on exporter, exporter as well is dependent on importer, because in our agency, revenue basket, export revenues is a key to our financial strength and our financial success. I believe that the more dependent companies and countries will become, the more stable regime will be in political area.

MR. ASLUND: Julia Nanay, PFC Energy.

Q: Thank you. I was wondering if you could say something about the Baltic LNG project, who’s developing it and some more about what it is.

MR. MEDVEDEV: I would like to stress that this project is not on paper; it’s on the run already. We have converted this project into investment stage and we will have a celebration at the beginning of construction of the North European pipeline in the Vyborg region in the beginning of December, but it will be just a celebration because the construction of it has already started. So the reason for construction of this project is of optimizing of our export route portfolio. Today we are exporting gas via Ukraine, via Belarussia and Poland, and via the Blue Stream project to Turkey, and these three routes is not enough to meet the growing demand and to grant us necessary level of diversification and risk minimization which is required for our growing volume of export. Already today this year we will export 149 bcm of gas – of Gazprom gas only. Last, we are exporting gas from the Central Asia republics: Kazakhstan gas, Uzbekistan gas, Turkmenistan gas.

And in order to have a 100-percent assurance that neither technological nor, say, climatic or political influence could interfere in our supply program, we take a decision to create another route which will be free of any transit risks. This pipeline, if executed in due time, will be in a position to supply 55 bcm of gas to Germany and further on: Belgium, France, the Netherlands and United Kingdom. And I would like to stress once again, this project is absolutely economically feasible. If it will not be the case, we will not go for this project.

MR. ASLUND: Thank you.

I see a hand at the back of the room. Please introduce yourself also.

Q: Pavel Vanichkin, TASS News Agency, Russia. So you talked about Shtokman mainly in the context of the U.S. market, and it’s closer to U.S. market, and as well as you said that the Gazprom wants to be a major player here in the local U. S. market. Can we infer that the American companies which are on the short list have in any way better chances in this context than the companies from Norway as well as from France?
And a quick follow-up: You said that you hope the companies will be nominated next year. Could you be more specific on that item – early next year, late next year? Thanks.

MR. ASLUND: May I add, will it be one exclusive winner or are you foreseeing a partnership of several of these companies possible?

MR. MEDVEDEV: As I told you, in our consortium we will expect to participate, besides Gazprom, two, maximum three companies, so once again, it could be three or four consortium members. And in respect of who has better chances, you know, in every beauty contest you would like the participants will be not only nice but also clever. We expect that besides their, say, parameters, they will be clever enough to give us a good proposal. (Laughter.)

MR. ASLUND: And the timing?

MR. MEDVEDEV: And timing, it’s early spring next year when we will make our final decision on the consortium membership.

MR. ASLUND: Yes, down there.

Q: Aaron Imperiale, Medtronic. On the social and philanthropic side, I was just wondering if you could comment on your engagement in health services or hospitals, things like that. Thank you.

MR. MEDVEDEV: I should tell you that both Gazprom and Gazpromexport has a program to support medical and other institutions, not only in the frame of Gazprom, whose service covers employees, which is, together with families, is more than 1 million people, and it’s very important because besides of the acting employees we have a lot of pensioners who very often require to be moved from the very fierce conditions of the northern regions to the more comfortable places in Russia to live. So we have a special program of relocation of these people.

But beside this, we are, say, sacrificing and giving financial support and equipment support for many hospitals and child houses [orphanages] in Russia. For example, I could tell, for Gazpromexport, we are supporting three such institutions which support kids without parents, and it includes all the style of possible support, including financial support, equipment support, medical support, because unfortunately the number of kids without parents in Russia is very high and we feel responsible to support.

MR. ASLUND: Thank you. One of the typical big topics with Gazprom is gas transit through Ukraine and deliveries to Ukraine. Recently this summer, there was a big splash about the current prices, which are $50, approximately, per 1,000 cubic meters, which is paid in barter for transit fees – that Gazprom would demand to increase them to $150, $160 per 1,000 cubic meters, which is the ordinary price that Gazprom charges
Western Europe. What is the actual state of Gazprom’s relations with Ukraine? What is your aim? Are you going to continue to subsidize Ukraine? And if so, why?

MR. MEDVEDEV: Just to follow, I believe it’s a common understanding on a political level that the relationship of the energy secretaries between Russia and Ukraine should be based on the international practice. And it was not just a one-sided initiative of Gazprom to insist on this, but it was also an initiative from the Ukrainian side after the new president came in power, and it was clearly stated that Ukraine would like to play in accordance with international rules. And based on this we made our proposal to switch from the barter relationship, which is completely outdated and really a direct subsidy of the Ukrainian economy, which is not compensated by anything for us, to switch to the European prices and European transit practice.

And I believe that we will continue with negotiations based on our desire to switch to these procedures as soon as possible, and we expect that it’s not only a question for Gazprom and the national company of Ukraine, Naftogaz Ukrainy, but it’s also a question of intergovernmental – (unintelligible) – because we normally should sign an annual intergovernmental protocol, which is defined in the rules of gas transit and gas sales before the year end. And Mr. Khristenko is involved in this process from our side, and from Ukrainian side’s minister of energy. But I believe it’s inevitable that without, say, any ground of subsidizing the Ukrainian economy, we should move to the, say, international practice of transit and sales.

MR. ASLUND: How fast?

MR. MEDVEDEV: I believe that our intention is to make it as quick as possible.

MR. ASLUND: Next year?

MR. MEDVEDEV: We will target to make it next year.

MR. ASLUND: Rick Herold, British Petroleum.

Q: Thank you.

Mr. Medvedev, I’d like to ask you a question please about your facing Asia program. We all know that demand in China and other places is growing very fast and that most of that demand is in the Far-Eastern part of China. That suggests that pipeline gas through the west-to-east pipeline might not be competitive price-wise, which takes us to Sakhalin supply, but that’s associated gas and there may not be enough to meet, over time, both domestic, Russian and Chinese demand. So I’m wondering what your thoughts are about Kovyktka as an addition supply in addition to Sakhalin for northeast China.

MR. MEDVEDEV: The question of Kovyktka is a very important and interesting question because Kovyktka is a huge gas field and it’s quite obvious that without
possibility to be involved in the export supplies, the economics of Kovykta looks at least in question. But from other side, the speed of development of the demand in China and the results of Sakhalin region, which could be a basis for supply of eastern part of China, is putting question when Kovykta resources could supplement or could replace the declining production of Sakhalin resources. And we have a common understanding with BP at least, from what I saw from the top level of Gazprom and the BP meetings, that it’s necessary to look the question comprehensively, and I believe initially it was a big mistake then when discussions with China went about supply of gas from a particular field. We never accept and will never accept the concept that the gas should be sold from a particular field because it will deteriorate the discussions about what’s the competitive price. Before producing and delivering gas, the gas should be sold, and as soon as we hopefully will sell gas to China, then we will decide which resource should be involved in order to meet this demand. And we are going to consider not only our resources, but resources which are available in Far East and in Siberia. Kovykta is one of the options available.

MR. ASLUND: Thank you. Did that satisfy you, Rick, or did you want to follow up on – oh, that’s fine.

Vladimer Papava, member of Georgian parliament.

Q: I have one question, a continuation of the question of Dr. Aslund about Ukraine. My question is related to gas supply to Georgia and Armenia. Would you plan to increase prices? And if you plan it, when it will be started? Thank you.

MR. MEDVEDEV: It’s a good question because just before I left I got the information that the company who is a major buyer of our gas for Georgia, Tbilgaz, is under bankruptcy procedure. And then it’s the big question, who will pay the debt which accumulated for the supply? And we have a schedule of repayment of this debt. That’s why, again, you see, it’s not possible that from our side you are declaring, say, democratic principles, market economy principles, and behaving in an old communist way. Product delivery should be paid in due time with an adequate price.

We have discussed with our Georgian colleagues that in view of the increasing cost of – (audio break, tape change) – which we are targeting to prepare to sell both to Georgia and Armenia – I would like to stress both to Georgia and Armenia, so there is not any political consideration behind – the price for the next year should be $110. And it’s much lower than our prices which we are getting in Europe. So it’s not just prices which we are taking from the ceiling.

MR. ASLUND: Yes, let me then follow on the same line. The big subsidization that Gazprom does of any country is Belarus. There the price is only $30 per 1,000 cubic meters. This is a subsidization comparison with the western price anyhow over $1 billion, which is a substantial part of the Belarussian GDP. Is this Gazprom policy or is this Kremlin policy? Will you maintain it or will you change that also?
MR. MEDVEDEV: But with respect to Belarussia, we have officially announced that the price, 46.68, will be in place for this year and next year. Subject to the Belarussian side, we will implement all the obligations with respect to the development of our business related to Yamal-Europe project.

As soon as this project will be executed – and it should be finalized in the next year – we are going to enter with Belarussia for increase of the prices in accordance with our general principles. So, again, we are not using gas as a subsidized – (unintelligible) – as well as political weapon.

MR. ASLUND: Thank you very much. I think that this has been a very good clarification to everybody here.

Ambassador Jim Collins.

Q: We’ve talked about every market –

MR. ASLUND: Use the mike, please.

Q: WTO accession has hinged in many ways on gas price and world market prices coming to Russia. What is Gazprom’s view about how that’s going to develop in the domestic market?

MR. MEDVEDEV: You see, we have signed a protocol with the European Union in respect to our entrance to WTO in which escalation of the price in local price – (unintelligible) – is in full compliance with our energy strategy because we’re as well interested when the prices will become more economical in Russia as our foreign counterparties, because it’s a basis for energy-saving technologies and better economics for gas producers including Gazprom because, again, today we are not in black in local sales because it’s a new taxation system, which – because we planned to be in black this year but it didn’t happen. We are covering our operational expenses but not all costs related to the local sales.

So I believe that the schedule which is reflected and protocol with European Union and its energy strategy under which we should reach $60 price in accordance with the schedule in 2010 is a good price. But in any case, local price of gas in Russia will never be comparable with European prices because we are a producer and our industry and our population enjoys a comparative advantage of Russian economy.

MR. ASLUND: Thank you.


Q: Thank you. Coming back to LNG, could you comment on the priority and status in your mind of the Baltic LNG project, and specifically with the increase in the capacity of the Baltic pipeline to 55 bcm, some questions have been raised about whether
there is enough dedicated supply to supply a Baltic LNG project. So should we see pipeline gas and LNG gas as competing with one another in this case? And then second, your presentation shows two dates, 2010 for Shtokman and 2009 for the Baltic LNG project. Should we understand that in a way Shtokman and the Baltic LNG project are competitors with one another?

MR. MEDVEDEV: No. Subject to the economic feasibility of Baltic LNG – which is a key question, you are right, whether transportation via North European pipeline could be synchronized with supplies to the Baltic unification plan – again, subject to this economic feasibility, these two projects are not competitive. They are supplementary to each other because it will allow, first of all, to create market base because we will target also U.S. and Canada market with Baltic LNG. And due to the lower scale of Baltic LNG, I don’t see any competition because our estimation of the market is that if two projects will be executed, we have enough room for our LNG, both with Baltic and with Shtokman.

But the final answer will depend about economic feasibility of supply of gas to some – (unintelligible) – region via the North European pipeline or possibility to synchronize additional – when, say, the volumes which are not necessary for Baltic pipeline – North European pipeline could be channeled to Baltic LNG. However, then they will be replaced when North European pipeline will be in full capacity. And we have different options for this, including the second phase of Shtokman.

MR. ASLUND: Well, to follow up on that question, Europe is starved for gas today. Everybody talks about natural gas as the big energy source of the next decade in Europe, and I see, for example, some consultants predict that there will be needed 300 billion cubic meters of additional gas for Europe in the next decade, and the biggest potential source of this is Russia. How much do you think realistically that Gazprom and other Russian gas companies can possibly supply out of this increased volume, gas volume that is expected in Europe in the next decade.

MR. MEDVEDEV: I would like to stress that reserve base of Gazprom and oil companies and independent producers is absolutely sufficient in order to meet most local demand and international demand in Europe and new markets, including China and the United States. Moreover, today we have a trend that in principle we have even certain excess of gas in the next several years. So that’s why for us, international markets are of great importance and we should really find the optimal, say, trend of development of our resources.

MR. ASLUND: Thank you. Since we need to finish in a few minutes, I would like to pose a last question that nobody has brought up before, and that’s the big question about the new relationship between the state and the private sector in Russia. We are now seeing that Gazprom, while still 51 percent state owned, is strongly turning to the western markets and going into major partnerships as we’re expecting in Shtokman, while in the oil sector we have seen on the one hand that Rosneft has taken over
Yugansk. On the other hand, that Rosneft is announcing that it will go for a big IPO of 49 percent at the end of next year.

Mr. Medvedev, could you explain to us how you see the strategy of Russian energy companies in the relationship between the state and the private sector, in the medium term?

MR. MEDVEDEV: First of all I would like to stress that Gazprom is a company of mixed capital where the state had 38 percent and now have more than 50 percent is a good example of how, as I say, management could combine the interest of the state and the interest of minority shareholders. And it’s not just a slogan for us to increase efficiency, it’s a must for us, because we are facing growing increase of the spending to go further north or offshore to produce more gas and to find new fields.

Also we are investing to support our transportation system. Currently the market conditions is favorable for us due to the high energy prices, but we are building our strategy not just on the, say, short-term vision of the favorable market conditions. And really we appreciate all the criticism which has come in to Gazprom when it’s constructive criticism. And I believe that people who follow us could appreciate that we have a new style of relationship with investors. A lot still could be done – cost spending, the budget management. It’s all on our agenda. But it’s a question of proper management, and I believe that the last four years showed that its possible to combine this, say, partial state ownership with a, say, market-arrangement approach.

MR. ASLUND: You have patiently answered many questions here and provided us with an immense amount of substantial information in a short time. Thank you very much.

(Applause.)

(END)