

Transneft to finance Rosneft's expansion to China

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On 11 October, the CEOs of the state-controlled companies Rosneft (Russia's largest oil producer and exporter) and Transneft (the owner of the Russian oil pipeline network) signed an agreement which sets out the rules for the co-financing of the development of pipelines used for exporting oil to China. The agreement is aimed at increasing the capacity of the oil pipelines: Skovorodino–Mohe (a fragment of a branch of the East *Siberia*-Pacific Ocean (ESPO) oil pipeline used to export Russian oil to China) from the present 15 million tonnes to 30 million tonnes in 2018, and of the ESPO from the present 50 million tonnes to 58 million tonnes annually. The first investment will formally be financed by Transneft but the costs of its implementation will in fact be incurred by Rosneft, which will pay a special long-term tariff (its value will be determined by the Federal Tariff Service). In turn, the development of the ESPO will be financed with funds Transneft will receive from general transit tariffs.

Commentary

- The deal will enable the implementation of the previous Russia-China agreements, especially the intergovernmental agreements adopted in March this year on increasing Russian oil supplies to China and trade contracts signed by Rosneft and the China National Petroleum Corporation (CNPC) in June this year during the Saint Petersburg International Economic Forum (they provide for additional supplies of 365 million tonnes of oil within 25 years). The regular increase in supplies (15.8 million tonnes this year, 17.2 million tonnes in 2014, 20 million tonnes in 2015–2017 and 30 million tonnes annually in 2018–2030) requires the use of a transport route (Skovorodino–Daqing) and this entails the need to double its capacity.
- Although the deal between Transneft and Rosneft is officially being presented as a compromise, it is in fact a great success for Rosneft. The development costs of the aforementioned oil pipelines – according to estimates from the Ministry for Energy, they will reach around US\$1.46 billion (around US\$2.29 billion according to Transneft's estimates) – will be incurred mainly by Transneft. The price of increasing the capacity of the Skovorodino-Mohe section (which will in fact be paid by Rosneft) will be less than US\$310 million. This cost appears insignificant, especially given the fact that Rosneft received an advance payment of over US\$60 billion from CNPC under the contracts signed in June this year. It cannot be ruled out that Rosneft will make attempts to apply the same co-financing scheme in other Far Eastern projects (in particular, for pipeline infrastructure development, which will enable oil supplies to a plant being built near

Nakhodka as part of the Eastern Petrochemical Company's project).

- This deal indicates that, regardless of the announced cuts in the investment programmes of energy firms and the government's plan to freeze tariffs (this will also apply to state-owned energy companies, including Gazprom and Transneft), the strategic projects being pushed through by the strong players in the Russian energy sector (mainly Rosneft) will be implemented. This also proves that the dispute between the CEOs of Rosneft and Transneft, which is being widely publicised in the media, is of secondary importance in the context of Russia's determination – increasingly evident over the past few months – to regularly strengthen its position on the lucrative Chinese oil market. This is an effect of both Rosneft's successful lobbying and increasing interest from Chinese partners.