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The creeping ‘de-Gazpromisation’ of Russian exports

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During a meeting of the presidential Commission for Strategic Development of the Fuel and Energy Sector and Environmental Security held in Astrakhan on 4 June, with the participation of Vladimir Putin, Rosneft’s chairman Igor Sechin put forward a proposal to grant the right to export gas via the pipeline system to so-called independent producers (among which Novatek and Rosneft predominate). This proposal concerns gas produced from fields in Eastern Siberia and the Far East, which would be intended for the markets of South-East Asia (particularly China). Vladimir Putin, who previously had often criticised the idea of de-monopolising the gas export pipeline system (currently only Gazprom has this right), this time did not express any open opposition; this should be interpreted as a change in his position which makes the implementation of Sechin’s idea more likely.

This further reduction of Gazprom’s export monopoly (in December 2013, a law came into force *de facto* giving only Novatek and Rosneft the right to export gas in liquefied form) will not be a process of de-monopolisation in the strict sense, but only a formal confirmation of the ever stronger position of those gas producers listed above, who are controlled by influential people from Putin’s inner circle. It is also likely that the right to export gas via the pipeline system will cover not only the Asian markets, but also the European market, which is strategically important for Russia.

‘De-monopolisation’: the short-term dimension...

While Igor Sechin (who is the secretary of the commission, and the most influential lobbyist in the Russian energy sector) did not provide specifics of the planned ‘de-monopolisation’ during the meeting of the presidential commission, press reports have shown that two alternative options to reduce Gazprom’s monopoly of gas exports via the pipeline system are being considered. In the first version, the Russian company would be obligated to purchase (after deduction of export prices of transport costs) gas produced by the so-called independent producers from fields located in the eastern part of Russia, and to export it onto foreign markets (Gazprom would formally retain the status of sole exporter and owner of the pipeline). The second option would involve the so-called independent gas producers creating a special consortium which would be responsible for constructing a transmission infrastructure (the centre of which would be the ‘Power of Siberia’ gas pipeline, with a capacity of 61 bcm and a length of 4000 km), enabling the export of gas to China.

The so-called independent gas producers’ (mainly Rosneft having significant gas assets in the eastern part of Russia) interest in participating in the Russian gas projects for Eastern Siberia and the Far East is their official justification for applying for the right to export gas via the pipeline system. The immediate pretext for the announcement of the proposal was the 30-year contract signed on 21 May between Gazprom and the CNPC to supply China with 38 bcm of gas annually.

This fits in with the independent producers' consistently implemented strategy to strengthen their presence on the rapidly growing Chinese energy market (Rosneft has been intensively developing its oil cooperation with China National Petroleum Corporation (CNCP) and Sinopec; Novatek will export liquefied gas to China via the Yamal-LNG project, which it is developing with the Chinese company CNPC and French company Total). A consequence of this 'de-monopolisation' may be an increased likelihood that Russia will meet its contractual obligations to the CNPC on time (in the first years of the contract, Gazprom will not be able to provide an adequate level of production to fulfil the contract on its own). The possible creation of an export consortium (which apart from Rosneft and Gazprom may also include LUKoil, which has expressed interest in participating in the Eastern Gas Programme) would also allow the high costs of the project to be spread out among several entities (the investments in transmission infrastructure and the exploitation of the gas deposits have been initially estimated at US$55 billion).

… and the long-term dimension

In fact, Russia's gas expansion plans in Asia are a convenient excuse for the so-called independent gas producers to permanently break the Gazprom's monopoly on gas export via pipeline system.

Although officially the proposal to break up the pipeline monopoly was only reported during the most recent meeting of the presidential Commission for Strategic Development of the Fuel and Energy Sector and Environmental Security, discussion of this matter has been ongoing for several years. Its roots lie both in the ownership changes in the gas sector, primarily through the acquisition by two leading players from Putin's inner circle – Igor Sechin and Gennady Timchenko – of important gas assets; and in a decrease in the effectiveness of Gazprom itself. The effectiveness of the so-called independent gas producers at pushing this concept has been proved by the adoption of a law restricting Gazprom's export monopoly in relation to LNG. Another step was the 23 January publication on the Russian Energy Ministry's webpage of proposed changes to the Energy Strategy of Russia by 2035 (Russia's energy minister is to present the final version of this document on 1 October 2014). This document states that one of the main objectives of energy policy in the coming years should be to stimulate the development of the so-called independent gas producers, and to ensure that all market participants have equal access to the gas transmission infrastructure managed by Gazprom. Also in January this year, there were media reports that Rosneft has requested the government of the Russian Federation to introduce a thorough de-monopolisation of the gas sector. The proposal envisaged that the first stage would be ensuring equal access to the gas network for all Russian companies operating in the Russian gas sector, and to allow them to export gas (in a pilot scheme) via the pipeline system. A key element of the second stage would be to create an organisational and legal entity managing the gas transmission infrastructure; this company, controlled by the state, would ensure fair access to the gas network for all participants on the Russian market. In addition, the second stage would involve granting the legal right to export gas via the pipeline system to all market participants.

On one hand, an analysis of the programme's assumptions could indicate a willingness to carry out serious reform of the gas market (a broad de-monopolisation of gas exports, a division of Gazprom based on the separation of the legal and organisational entities responsible for the extraction and transport of gas). On the other, however, the existing regulatory changes, in particular the law on the liberalisation of LNG exports (drafted in such a way that its beneficiaries are *de facto* only Novatek and Rosneft) indicate that the real reason for their introduction is primarily a legal sanction of the growing influence of Novatek and Rosneft; both companies have announced their further expansion into the Russian gas sector (significant increases in gas production are planned: Novatek from 62.2 bcm in 2013 to 115-120 bcm in 2020, and Rosneft from 21.6 bcm in 2013 to 100 bcm in 2020).

It is highly likely that in the longer term, the process of de-monopolising pipeline exports will also cover gas supplies to the European market. This will be the result not only of the lobbying by the so-called independent gas producers (mainly Novatek, as illustrated by the statement of Gennady Timchenko during an international economic forum in St. Petersburg, when he said that the company is ready to supply gas to Europe via the pipeline system), but also of a strategic decision by the Russian government, dictated by the decreasing efficiency of Gazprom and the increasing number of legal challenges (mainly regulatory) to it on the European market. The specific de-monopolisation of the Russian presence on the European gas market (i.e. the export of gas via the pipeline system not only by Gazprom, but also by Novatek and Rosneft) could indeed prove useful for warding off the European Commission's allegations of violations by the Russian side of the EU competition rules and rules regarding the liberalisation of the EU gas market (above all the so-called Third Energy Package).

Forecast

Given the strong positions of Igor Sechin and Gennady Timchenko in the current political and business elite, which is reflected in the decisions taken by Vladimir Putin in the energy sector, it is highly likely that the plans of the so-called independent gas producers will be realised, deepening the process of 'de-Gazpromization' Russia's gas exports. The plans' final shape, however, will be a kind of compromise taking into account the interests of Rosneft and Novatek on the one hand, and those of Gazprom on the other; despite its weakening position the Kremlin still uses Gazprom to achieve important economic (such as its joint financing of the organisation of the Olympic Games in Sochi) and political objectives (making the supply of gas conditional on the state of political relations between Russia and the importer country – as in the case of Ukraine).