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Gazprom's position on the Russian gas market weakening

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As the difficulties Gazprom has faced in recent years on the European market have multiplied[1], so more and more symptoms have appeared which may suggest that the company's dominant position is deteriorating. The decision made by the Russian government in June 2011 to double the tax Gazprom has to pay on the extraction of gas, which was later approved by parliament, was the first time in many years when the company's fiscal privileges were withdrawn. The process of Gazprom's assets being taken over by private companies and business partners from within Vladimir Putin's closest circle is underway. More and more frequently attempts are being made to challenge the company's monopoly in areas of key importance for the functioning of the entire gas sector, such as Gazprom's exclusive right to dispose of the Russian gas transportation system and its exports monopoly. Competition from independent gas producers on the domestic market is growing, and Gazprom is gradually being pushed out of some of that market's most profitable segments (industrial clients).

The emerging tendencies in the Russian gas sector derive from a number of factors – from the situation on the European gas market, through difficulties hampering the development of the sector in Russia itself, to the private interests of the current ruling class and its business partners. The plans for a structural reform of the monopoly (including isolating gas transportation system from Gazprom), presented since 2000 by the Ministry for Economic Development and since 2003 by the Russian Association of Industrialists and Entrepreneurs (RSPP), suggest a direction for the changes necessary to stimulate the sector's development and improve the efficiency of Gazprom itself. However, the monopolist's current business model gives the government full control over this strategic enterprise, which is a core of Putin's concept for developing Russia as a global energy power. Despite Putin's recent statement that he "does not rule out privatising Gazprom in the future" (made at a meeting with political scientists in Moscow on 6 February this year), any structural reform of Gazprom (and consequently, a weakening of the state's control over it) seems unlikely in the foreseeable future. Still, the developments on the domestic market – growing pressure from other gas companies (oil corporations and independent producers) and changes on the European market[2] – may result in the weakening of Gazprom's monopoly privileges and a gradual deterioration of its special status within Russia.

[1] The difficulties Gazprom is facing in Europe are caused, among other factors, by the financial crisis. Since 2009 the demand for gas has been lower than in previous years, and the volume of Russian gas sales has fallen (from around 168 billion m^3 in 2008 to around 148 billion m^3 in 2010). Another reason for this drop is the radical change in the European gas market: a sudden increase in the supply of LNG and the resulting oversupply of gas, as well as the attempts made by the EU to reduce its dependence on the Russian supplier (including antitrust regulations concerning the energy market). For more on this subject, see Ewa Paszyc, 'Nord and South Stream won't save Gazprom', *OSW Commentary*, January 2010.

[2] For example, an improvement in the market situation and a significant increase in demand for gas in Europe could force measures which could stimulate independent producers (gas companies and oil corporations) to increase their extraction volume; one such measure could be the liberalisation of access for all gas producers to the gas transportation system.

Putin's oligarchs – a new chapter in the redistribution of Gazprom's assets

In 2001 Alexey Miller – Gazprom's CEO, newly appointed by President Putin – started his term in office with a spectacular campaign aimed at regaining Gazprom's former assets which had been taken over in the 1990s by private companies and business people associated with his predecessor, the company's long-time CEO Rem Vyakhirev. The largest beneficiary of Gazprom's assets, the Itera company, was deprived of the concessions, companies and shares in the company's extraction companies (Rospan, Severneftegazprom, Purgaz, Sibneftegaz etc.) which it had obtained for a very low price. Gazprom regained the control it had lost during Vyakhirev's term in office over Sibur, Russia's largest chemical holding, and Stroytransgaz, a company involved in the construction of pipelines, whose major share packages had been taken over by relatives of the former managers (including Vyakhirev) and the company's political protectors[3].

In line with the rules of property redistribution followed by subsequent Kremlin-based groups, after Vladimir Putin assumed the presidency, the regained Gazprom assets (along with many other properties) were redistributed to people associated with the new ruling class. The most valuable parts were acquired by Putin's friends, collaborators and business partners whom he had worked with during his career in St. Petersburg city hall, or his close allies from the period of his KGB service. Other, less impressive items fell to relatives and acquaintances of people associated with the ruling group and the new Gazprom executive team.

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What differentiates the current process of dividing up Gazprom from that performed in the 1990s is its much larger scale during Putin's second term in office, which accelerated in its final months and is still continuing today. Some of the controversial transactions were made at Putin's direct request (such as the sale of the insurance company Sogaz to Bank Rossiya in 2004 for an exceptionally low price). The takeover of the assets – in non-transparent, multilevel transactions – involves a network of mediator companies registered in tax havens, which makes it difficult or almost impossible to identify their true owners. The assets isolated from Gazprom some time ago and regained by the team led by Alexey Miller currently form an important part, and in many cases the initial start-up capital, of the dynamically developing new oligarchic empires. The biggest beneficiaries of the current phase of dividing up Gazprom's assets include the following persons:

- **Gennady Timchenko**

Novatek: the gas part of the empire[4]

The profitable purchase of Gazprom assets has contributed to the spectacular growth of Novatek – Russia's second largest (after Gazprom itself) and the largest of all independent gas producers (its expected total extraction volume was 52 billion m³ in 2011)[5]. A jump in quality for Novatek happened when in 2009 a major package of the company's shares (23.5%) was acquired by Gennady Timchenko, whose acquaintance with Putin dates back to their KGB intelligence service and his cooperation with St. Petersburg city hall in the oil trade[6]. Since then the Russian state has supported the transformation of Novatek into a strong actor on the Russian gas market by any means possible. Among the assets which Novatek purchased from Gazprom were share packages in the Severenergiya (25%) and Sibneftegaz companies (51%); these were reclaimed from Itera, whose total resources are

[3] Including Viktor Chernomyrdin, a co-founder of Gazprom, and prime minister of the Russian Federation from 1992–1998.

[4] Timchenko's main asset is the Gunvor company, Russia's largest oil trading entity (around 40% of the RF's exports). In November 2011 Timchenko consolidated 93% of shares in the TransOil company, one of Russia's largest freight rail operators (holding 23% of the oil transport market). Timchenko is also a shareholder in Bank Rossiya (around 10%) and a founder of the St. Petersburg-based judo club Yarva-Neva, whose honorary president is Vladimir Putin.

[5] For comparison: Novatek's extraction volume levels in 2009 and 2010 was 32.8 and 37.8 billion m³ respectively. The company's development strategy provides the extraction volume to double by 2020, to reach over 100 billion m³.

[6] Timchenko cooperated with St. Petersburg city hall, among other initiatives, in the controversial 'Oil for Food' programme managed by Putin in the early 1990s. Timchenko's business partner and co-owner of Novatek (27.2%) is Leonid Mikhelson.

estimated at 1.6 trillion m³, together concessions to exploit several fields. Another important asset purchased by Novatek was the Yamal LNG company, along with its property, the Yuzhnoye Tambeyskoye field (over 800 billion m³). In July 2011, in order to win foreign investors and ensure the profitability of the Yamal LNG project, the government granted it significant tax reliefs (zero tax rate on extraction (NDPI)), and lifted the export duty on any LNG produced in the future[7].

In August 2011, as the only participant in the tender procedure (potential competitors were not allowed to take part), Novatek gained concessions for another four fields in Yamal (estimated at over 2 trillion m³). So in less than two years, the confirmed volume of resources owned by Novatek increased six-fold – from 690 billion m³ (at the end of 2008) to over 4 trillion m³ (as of 2011).

The company's prestige has increased due to its international contracts, including its alliance with a strategic partner, the French company Total, which purchased slightly over 12% of Novatek's shares with the option to increase its package to almost 20%, and which since November 2011 has been a shareholder in the Yamal LNG project (20%). The Norwegian company StatoilHydro and Qatar Petroleum International can be considered as other strategic partners.

Novatek is the only independent gas company in Russia which can compete with Gazprom on the EU gas market and acquire shares in Western concerns. In July 2011, the German energy concern EnBW offered to sell Novatek 25% of its shares (more than half of its package)[8] in VNG, one of the largest gas importers and distributors in eastern Germany (negotiations are underway). Several other European enterprises have also expressed interest in Novatek as a possible shareholder. Novatek's potential partners expect cheaper supplies of gas compared with that delivered by Gazprom under its long-term contracts. Novatek's own extraction costs (similar to the costs borne by other independent gas companies in Russia) are several times lower than the costs borne by Gazprom. This would harm Gazprom's export monopoly, however.

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Timchenko also, within a short period of time and for symbolically low prices, bought other Gazprom assets which the monopoly had considered unrelated to its basic business. He consolidated 80% of shares in Stroytransgaz, a company created by Gazprom specialising in the construction of oil and gas infrastructure objects, with profitability guaranteed by large contracts realised for the gas monopolist and other energy companies (including Inter RAO UES). In late October 2011, another Gazprom asset, Russia's largest chemical holding Sibur, became the property of Timchenko and his business partner Leonid Mikhelson. Its new owners purchased a package of nearly 50% of Sibur's shares from Gazprombank, thereby increasing their total share package to 95% (in 2010 Mikhelson bought a total of 46% of the holding's shares). The purchase of nearly 100% of Sibur's shares was possible mainly thanks to a loan provided by Gazprombank.

- **The Rotenberg brothers[9]**

Stroygazmontazh: the pipeline business

In 2006, the brothers Arkady and Boris Rotenberg – Vladimir Putin's childhood friends and fellow sportsmen from a St. Petersburg judo club (and members of the Yarva-Neva club, whose honorary president is Vladimir Putin) – received a profitable contract from Gazprom

[7] The amendments to the Russian Federation's fiscal law, signed by President Medvedev on 21 July 2011, also cover the oil and gas deposits on the Black Sea, the Sea of Okhotsk shelf and in the Far North, with state-owned concerns Rosneft and Gazpromneft holding concessions to exploit them. For the Yamal projects, the zero NDPI rate will apply until the cumulative extraction reaches 250 billion m³. So far, this only applies to gas used in the production of LNG. Gazprom has also applied for the tax on extraction carried out as part of its Yamal projects to be lifted.

[8] EnBW owns 48% of shares in VNG. The control package is owned by EWE.

[9] Apart from the assets acquired from Gazprom, the Rotenberg brothers own shares in SMP-Bank; control over a dozen distilleries which are part of Rosspiritprom; co-own Mostotrest, Russia's largest bridge construction company; and have won contracts for the construction of toll highways (currently on the Moscow–St. Petersburg).

concerning pipe supplies. The next year, Gazprom introduced the brothers to big business by selling its gas pipelines construction companies to them. The Stroygazmontazh company created as a result of their consolidation is Gazprom's largest contractor, carrying out multi-billion-dollar strategic projects of transfer hubs like Nord Stream, Sakhalin-Khabarovsk-Vladivostok, Dzhugba-Lazarevskoye, and so on. In 2010 Stroygazmontazh and Stroygazkonsulting (a company owned by a Jordanian Ziyad Manasir, the brothers' acquaintance) won two-thirds of the tenders for the construction and modernisation of sites owned by Gazprom.

The companies owned by the Rotenberg brothers are also Gazprom's pipe suppliers. In 2005–2010 they won 45 of the 48 tenders announced by the company to supply pipes and other elements for the assembly of gas pipeline networks. Since 2009 they have owned 50% of Eurotube, a steel trading company registered in Germany, which is the largest supplier of pipes (over a third of the total market share) to Russia. Eurotube's main client is Gazprom, although it also supplies pipes to Transneft, Rosneft and other Russian businesses.

In April 2010 the Rotenberg brothers were mentioned on the Forbes list of billionaires, and Gazprom sold them another non-core asset – the company Gazprombureniye, which implements 70% of the company's contracts (involving geological analyses, construction, renovation, maintenance of oil and gas wells and underground gas storage facilities) and carries out work in the Bovanenkovo gas field in the Yamal Peninsula.

- **Yuri Kovalchuk**

SOGAZ, Gazprombank, media: a financial and media empire

Some of Gazprom's assets have formed the basis for a spectacular surge in the holdings and influence of Yuri Kovalchuk, another of Putin's acquaintances from St. Petersburg and the co-founder (alongside Putin) of the Ozero co-operative society for summer residences. Gazprom's shares were gradually acquired from 2004 at bargain prices by the commercial Bank Rossiya, which Kovalchuk controls; these have multiplied the bank's capital from US$216 million in 2005 to US$9.6 billion as of the end of 2010[10].

In 2005 Gazprom sold its company SOGAZ, one of Russia's largest insurance companies, to Bank Rossiya for around US$100 m. Under the bank's control SOGAZ's premium rates increased dramatically, due to the insurance contracts it entered into with large state enterprises (Russian Railways, Rosenergoatom, etc.). For example, the premium rate for its recent contract (November 2011) with Gazprom for the period 2012–2016 amounted to nearly US$3 billion. The subject of the contract is the insurance of the company's property (over US$1 billion) and additional medical insurance (US$1.2 billion). According to SOGAZ's annual report in 2010, the value of its assets exceeded US$3 billion, and the value of contracts concluded last year was US$2 billion.

Along with the assets making up the Gazprom-Media group, Kovalchuk has gained control over Russia's largest nationwide media (TV and radio stations, newspapers) and thus created Russia's biggest media holding. He also took over Video International company – a giant on the Russian media advertising market.

In 2005 Bank Rossiya purchased another valuable asset from Gazprom, the company LIDER, which among other activities manages the company's pension fund and the Gazfond investment fund. As Lider's owner, Bank Rossiya acquired the company's Gazprombank package (43%) along with shares in various subsidiaries of Gazprom which it transferred to Gazprombank's assets[11]. This enabled Kovalchuk, the largest shareholder in Bank Rossiya (30.4%) to acquire, among other items, significant media assets important for the Kremlin in the run-up to the electoral campaigns, and thus in effect control over the Gazprom-Media holding. On this basis, he has created Russia's largest

[10] According to its annual report, as of the end of 2010 the value of assets owned by Bank Rossiya was 267.07 billion roubles, its equity 26.02 billion roubles, and its net profit 1.6 billion roubles.

[11] Gazprombank was the 'deposit box' for assets Gazprom considered as not directly related to the company's business profile (which included the control package of the Gazprom-Media holding, Atomstroyeksport, United Machinebuilding Plants, Sibur), and the direct seller of these assets.

media holding (including the national TV stations NTV, TNT, REN TV, Petersburg, 5-Kanal, the *Izvestiya* newspaper, the Video-International company – a giant on the Russian media advertising market – and many others).

The market situation demands Gazprom's privileges to be curbed

During his two periods as President (2000–2008), Vladimir Putin significantly strengthened the position of the gas company in both Russia's economy and its politics. In 2006 the Duma adopted a law which guaranteed Gazprom exclusive license to export all types of gas. In the same year, in order to prevent potential competition from Central Asian gas on the European market, a ban was introduced on the international transfer of gas via the territory of the Russian Federation. The government made every effort to improve the monopolist's financial situation. In 2003–2010 the share of excise taxes and duties in Gazprom's export revenues was reduced from 26% to 16%. The future profitability of the company's undertakings on the domestic market was guaranteed by a government programme involving a gradual increase in the wholesale price of gas in Russia (on average by 15–20% per year); this was launched in 2007, and is aimed at levelling out the profitability threshold of the domestic and European markets.
It became apparent that all changes on the gas markets, both domestic and European, both good and poor economic situation, posed serious challenges to the company's monopolist position. For example, the problems Gazprom faced during a period of prosperity on the EU's gas market (2005–2008), which were related to maintaining the volume of extraction necessary to meet demand from domestic clients as well as the expected increase in exports, mobilised other gas producers (oil companies independent of Gazprom) to increase their production. This posed a challenge to the privileges enjoyed by the monopolist, involving very significant reduction of the profitability of gas production outside of the Gazprom system (in particular the lack of access of independent companies to the gas transportation system and export contracts, which hampered the sector's development).
Despite a major change in the market situation after 2008 (a drop in demand for gas in Europe caused by the economic crisis), there was an upsurge in the extraction of gas by Russian producers independent of Gazprom. This resulted from the growing profitability of the domestic market, which translated into greater expectations for those companies regarding the conditions for operation on the domestic market.

The pipeline monopoly. Gazprom's exclusive right to dispose of the system of Russian pipelines is its most widely criticised privilege[12]. The monopoly hampers or blocks other companies' operations by limiting or refusing to accept supplies provided by independent producers to its pipelines, eliminating the possibility of connecting new fields to the system, etc. One of the few exceptions was a long-term contract concluded in 2010 with Novatek, enabling the latter to supply 10 billion m^3 of its gas to the pipeline network per year.

Gazprom hampers or blocks other companies' operations by limiting or refusing to accept supplies provided by independent producers to its pipelines, eliminating the possibility of connecting new fields to the system, etc.

The Gazprom leadership's reluctance towards any projects to split up the company has gained unequivocal support from Vladimir Putin. During his presidency Putin repeatedly rejected proposals to restructure the company and projects to transform the gas transportation system into an independent structure modelled upon Transneft (with continued state control over the transfer infrastructure).

[12] Gazprom gained full control over the gas transportation system in 1997 by way of compensation for the obligation to supply cheap gas to the domestic market (at that time, the regulated domestic prices were lower than the production costs). The current gas prices in Russia are 3 to 5 times higher (depending on the region) than Gazprom's own average costs.

Prime Minister Putin's comment on this suggestion (in February 2011) came as a surprise. He criticised Gazprom for excessive use of its monopoly rights to dispose of the gas transportation system; he did not question the principle of Gazprom's exclusivity in this area, but he returned the issue of liberalising access to Gazprom's network to the public debate. On 7 July 2011 the Federal Antitrust Service (FAS) filed a bill with the government concerning non-discriminatory access for all gas producers to the gas transportation system. Despite the undisputed need to adopt such a solution (Gazprom's extraction programme is stagnating, and there is a need for independent companies to stimulate the growth of gas production[13], limit the consumption of petroleum gas, and increase the competition on the domestic market, and so on), it seems unlikely that the gas transportation system will undergo real isolation from Gazprom in the foreseeable future. For example, the recent FAS bill filed with the government (in October 2011) merely obligates the monopoly to disclose information on available transfer capacity on individual routes and on the number of registered applications for gas transfer and connection to the system. On the one hand, the incompleteness of this proposal testifies to the power of Gazprom's influence concerning its privileges over the legislative process; but on the other, it suggests that the very fact that the issue is being dealt with at such a high level is a sign that pressure on the company is growing.

[13] The extraction potential of Russia's independent gas producers (including oil corporations), which control around 30% of the country's gas resources, is estimated at 400–500 billion m^3 per year (the actual extraction volume of independent companies in 2010 was 142 billion m^3).

The export monopoly. Under the law, the only exceptions from Gazprom's export monopoly have been those projects carried out on the basis of Production Separation Agreements (PSA). However, none of the companies which carried out two such gas projects in Russia has been able to sell gas to foreign clients independently. The first project, Sakhalin-2 (with Shell as its operator), was taken over by Gazprom together with the contracts for the export of LNG, already signed at that time. The gas part of the other project, Sakhalin-1, was suspended. Despite the plans laid by the investors (the American company Exxon Mobil as the operator, Japan's SODECO, India's ONGK and Rosneft) – who as early as 2006 had signed a preliminary agreement with the Chinese company CNPC to export gas to China – Gazprom decided that the gas from Sakhalin-1 would be used for domestic consumption. In February 2012 Exxon offered to sell Gazprom its gas assets in the project.

The first crack in Gazprom's exports monopoly was the company's unprecedented consent to sharing the export revenues with Novatek. The agreement concerning the conditions for the export of liquefied gas from the Yamal project carried out by Novatek stipulates that Gazprom formally maintains its exporter status and receives a small fee, while Novatek takes the export revenues.

The first crack in Gazprom's export monopoly was caused indirectly by Novatek. The agreement between Gazprom and Novatek (signed in March 2010), concerning conditions for exporting around 15 billion tons of liquefied gas per year from the Yamal LNG project operated by Novatek (which is scheduled to launch in 2016) stipulates that Gazprom will formally maintain its exporter status and receive its agency fee, whereas Novatek will have a major share in the revenue generated from the sale of gas. Gazprom's unprecedented consent to split the export revenue would probably not have been possible without the political protection extended to Novatek by the Russian government.

Other gas producers are not so lucky. Despite the lobbying efforts undertaken by the influential deputy prime minister Igor Sechin, the state-owned Rosneft has been applying since 2005 for the possibility to export gas to China, so far without success. The subsequent rounds of talks between the company and Gazprom concerning the proposed creation of an export joint venture have also been futile. Another company, TNK-BP, which applied

for the right to export gas to China (from the Kovykta field in the Irkutsk Oblast) had to sell the Kovykta project to Gazprom due to the lack of any such possibility, among other reasons. Other Russian companies have attempted to bypass Gazprom's exports monopoly. For example LUKoil, without any mediation on the part of Gazprom, signed a memorandum of understanding in 2010 with China's CNPC which provides for supplies of around 15 billion m^3 of gas per year (starting from 2014); however, this concerns gas from projects carried out in Uzbekistan. In May 2011 the Yakutsk Fuel and Energy Company (part of the Summa Capital investment group) opened talks with the Korean company KOGAZ on the possible export of gas to Korea.
Vladimir Putin has not ruled out liberalising Russian gas exports in the future; yet in his opinion, Gazprom's monopoly in this area prevents Russian companies from competing on various markets, and supports gas price stability.

Increased competition on the domestic market. In the context of the change in the situation on the domestic market, which since 2007 has not generated any losses due to the gradual increase in the price of gas, and has been running at a profit since 2008, Gazprom faces growing competition on the part of other suppliers (Novatek, Itera and oil corporations). Gas delivered by Gazprom, which is also provided on the domestic market under long-term contracts with the 'take or pay' clause at regulated prices, is more expensive (by 10–15%) than the gas offered by its competitors. Also, the supply conditions Gazprom offers are less favourable; for instance, the company requires 100% of the due amount to be paid in advance, while other suppliers demand a mere 30% in advance. Prime Minister Putin's repeated suggestions to eliminate the 'take or pay' clause from domestic contracts have so far fallen on deaf ears[14]. In 2009–2011, Novatek acquired a share in the most profitable market of the monopolist's corporate clients in several oblasts; for example, it entered the market in Chelyabinsk oblast, and in November 2011 it purchased 51% of the company Mezhregiongaz Chelabinsk from Gazprom, with the option of increasing the share package to 100%. The agreement between Novatek's chief and the oblast's governor stipulates an increase in the supplier's share of the oblast's gas market to 90% by 2020.

The relatively unrestrained development of competition on the ever more lucrative domestic gas market may suggest that the Kremlin plans to reduce Gazprom's activity to exports at the expense of the company's involvement in the domestic market. The monopolist's own extraction costs are growing so rapidly that expensive Russian gas can only generate decent revenues on foreign markets.

In 2009, Inter RAO UES and OGK-1 (power stations and thermal power plants in the Perm and Moscow oblasts and in the Yamalo-Nenets autonomous *okrug*) availed themselves of the right to terminate their agreement with Gazprom, and since 1 January 2010 have been buying gas from Novatek (under five-year contracts). Furthermore, Itera has taken over some of Gazprom's clients in the Sverdlovsk and Moscow oblasts. LUKoil and TNK-BP have announced ambitious plans to develop their gas market segments and increase production volumes, and Rosneft is involved in talks with Gazprom concerning the creation of a gas trade company in Russia.
The activity of gas producers and oil corporations independent of Gazprom on the domestic market is growing rapidly. According to estimates, as of 2011 these companies have 100% of the market share in Sverdlovsk oblast, 95% in Kemerovo oblast, 58% in Tyumen oblast, 55% of Novosibirsk oblast, and their share in the Russian market as a whole has exceeded 25%.

[14] In March 2011, Vladimir Putin appealed to Gazprom's governing bodies to lift the 'take or pay' rule in relation to domestic clients, and to eliminate penalties for too low or too high demand compared with the contracted volume. In October 2011, Putin ordered deputy prime minister Igor Sechin, the government's energy sector custodian, to prepare the necessary documentation.

Conclusions and forecast

• Both Gazprom itself and the Russian gas sector have recently been subject to processes which may challenge the state-owned company's unique status, with all that this implies for such a change in Russia's economy and politics. The possible repercussions include:
- the redistribution of property;
- the spectacular development of Novatek – the government's new favourite in the gas sector;
- the erosion of Gazprom's monopolist privileges;
- the weakening of the company's dominant position on the domestic market.

• Gazprom's assets have formed the basis for the multi-billion fortunes of Putin's oligarchs: Gennady Timchenko (Novatek), the brothers Arkady and Boris Rotenberg (involved in the import of pipes and the construction of pipelines, among other activities), Yuri Kovalchuk (active in the insurance and media sector, among others) and many other people associated with the current ruling elite. Any further redistribution of the monopolist's assets is a privilege of the government. In Russian reality, nobody questions their unwritten right to dispose of the assets of state-owned enterprises (and in fact not just the state-owned companies, and not only Gazprom), and the gas concern has never been a strictly commercial undertaking. This current phase in its development differs from the previous ones in terms of its scale and the provenance of its beneficiaries – their close connection with one key person – the leader of the elite.

In 2009, Inter RAO UES and OGK-1 availed themselves of the right to terminate their agreement with Gazprom, and since 1 January 2010 have been buying gas from Novatek. Furthermore, Itera has taken over some of Gazprom's clients. LUKoil and TNK-BP have announced ambitious plans to develop their gas market segments and increase production volumes.

• The spectacular growth of Novatek can also be examined in the context of politics. The empire controlled by Gennady Timchenko, which was created some time ago, has started to develop its gas segment only recently. Timchenko acquired the most significant and most profitable gas assets from Gazprom in the last three years. According to numerous analysts, this is one of the most spectacular episodes of the increasingly dynamic process of transferring assets from state-owned to private companies involving people from various levels of government. The transfer of assets from Gazprom to private companies registered outside Russia may be a form of safe investment, representing the current elite's provisions for the future. It cannot be ruled out that – considering the critical approach towards Gazprom on foreign markets which see it as a tool of Kremlin policy – the growth of Novatek is a part of Moscow's plan to create a new market player and introduce it to the European business as a strong 'independent' gas company which could strengthen Russia's position on the EU market.

• The ever more frequent challenges to Gazprom's monopolist privileges, in particular the right to dispose of the domestic pipeline network, may be much more important for the developments in Russia's key sector. True liberalisation of access to the gas transportation system would be a breakthrough for the Russian gas market, as it could initiate a reform of the whole sector. This seems rather unlikely in the immediate future, because the government – which has adjusted Gazprom's business model to their needs and purposes – is not interested in truly weakening the monopolist. The result of the growing need to introduce such a solution will most probably be a half-measure – perhaps a new legal act which would provide a formal framework for the company's relations with other entities and prevent it from blocking certain projects (as in the Kovykta case). In the longer term, though, the liberalisation of access to the monopolist's network seems unavoidable. The company will gradually lose its share on the domestic market to the independent producers, which will force the opening up of the network.

• In the foreseeable future, the company's monopoly on exports seems less at risk, mainly due to the role of Gazprom and the export of gas as important tools in maintaining Russia's influences in Europe and the CIS. In the context of changes on the European gas market (the oversupply of gas, growing competition between the suppliers, and diversification of supply routes), and of frequent challenges to Gazprom's pricing policy by its customers, maintaining the export monopoly in order to block competition and maximise prices is no longer reasonable, but on the other hand, the lifting of this monopoly could damage the company's position on the domestic market.
Currently, any exceptions to this rule (as in the case of Novatek) will only be possible at the request of Vladimir Putin, and only for those selected few companies which are under the government's strict control. Only a change in the market situation – a significant increase in the demand for Russian gas which the concern would be unable to cover – could force liberalisation of the export monopoly, but even so that would not bring about its abolition.

• What seems difficult to stop, is the process of other producers pushing the monopolist out of the domestic market. Had it not been for the crisis which eliminated the threat of a gas shortage in Russia, Gazprom would have had serious problems covering both domestic and foreign demand. Until the future launch of the Yamal fields, over the next ten years Russia will barely be able to reach the expected extraction volume without the active participation of independent companies. Their investments in expanding their production may be profitable when wider access to the increasingly lucrative domestic market is guaranteed.

In the medium term, Gazprom is likely to remain Russia's main gas supplier; at the end of 2010 it controlled around 70% of the Russian market. The relatively unrestrained development of competition on the ever more lucrative domestic gas market may suggest that the Kremlin plans to reduce Gazprom's activity to exports at the expense of the company's involvement in the domestic market. The monopolist's own extraction costs are growing so rapidly[15] that expensive Russian gas can only generate decent revenues on foreign markets. The monopolist may see the domestic market as its priority (with all the resulting consequences for independent producers) only if there is a collapse in the exports of Russian gas.

[15] The quality of Gazprom's resources is decreasing year on year, and its costs of extracting gas from the fields in Western Siberia, 60% of which have now been exploited, are on the rise. New projects require massive investments.

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