

Gas price hike

For China's natural gas producers, the resources tax hike will increase their production cost. Fortunately, Beijing also wants to raise domestic natural gas ex-factory prices.

According to a government notice released late May, China will accelerate the reform of gas pricing system this year, linking the natural gas prices with alternative energy prices.

With the coming of central Asian natural gas by the end of this year, prices of domestic-produced natural gas will have to be in line with international market prices, since imported LNG prices have been international market prices.

Factory-gate prices of domestic produced natural gas from northwestern China's Tarim basin are yuan 960/'000 cubic meters for industrial users and yuan 560/'000 cubic meters for city gas users.

Imported central Asian natural gas to China's northwestern border is priced at about \$190/'000 cubic meters (about yuan 1306/'000 cubic meters). The price of domestic produced natural gas is much lower than that of imported pipeline gas. China's gas pricing system is controlled by central government and local governments. Central government sets the upstream wellhead prices and transmission fee while local governments set downstream retail prices. – Staff

Russia looks likely to miss its targets

The world's biggest gas exporter has so far managed to hide its production shortfalls from western eyes. But now its superprojects are looking less likely, which will worry its European customers. The Caspian region though could continue to play a fill-in role.

Gazprom will struggle to meet gas demand in Europe if it is forced to meet all demands placed on it by the state, according to a new study by consultancy Poyry.

The newly announced delays to Gazprom's mega-projects, such as the Bovanenkovo field on the Yamal peninsula (*IGR 626/23*), will translate into the monopoly's inability to raise production sufficiently quickly when demand picks up in Russia and Europe.

The gap could be filled by Caspian gas transported via competing schemes, such as the Nabucco project, which would strengthen the security of supplies to Europe. But Gazprom will do what it can to buy gas from the former Soviet states in central Asia, a policy that has stood in good stead in the past.

Gazprom expects to have available some 1.1 trillion cubic meters/year by 2030, but some key elements of this plan are already looking doubtful. Earlier in June it announced a series of cuts in its capital expenditure for this year.

One casualty of this was the giant Bovanenkovo field, on the hugely expensive to develop Yamal Peninsula, which has been delayed until the third quarter of 2012. That field has a very aggressive production program, rising from almost 8 billion cubic meters in year one to 115 Bcm in year three and, a few years after, reaching 140 Bcm.

This delay is a discouraging sign for Europe, as Yamal is Gazprom's key focus area, investment in which comes at the expense of the dozens of medium-sized fields that could have been developed in western Siberia, the report's author Nazrin Mehdiyeva told Platts in an

interview. This gas could feed into the existing pipelines and compensate for decline elsewhere.

But this delay should not come as a surprise: until 2002, Gazprom thought the hugely challenging Shtokman project would be on stream by 2005, before Yamal fields, which were deemed to be more expensive to develop.

Even now it is uncertain how much gas the Shtokman field will be exporting by pipeline and how much it will be liquefying for shipping. The pipeline capacity planned to be built suggests that more of the Shtokman gas could be sent via pipelines than is now envisaged.

There are four supergiants in western Siberia – Yamburg, Urengoi, Medvezh'e and Zapolyaroe – and only the last is not in decline. Gazprom has invited foreign firms into the medium-sized Yuzhno Russkoe field, but in order to secure licenses from the state for the real prizes, it has declared the Yamal a priority project and ring-fenced the coveted assets by successfully pushing through the strategic fields legislation, Mehdiyeva says.

The fields that are classified as strategic cannot be majority owned by foreign companies and can be allocated without a tender. However, obtaining licences for a large number of vast fields means that Gazprom's resources will be tied up in developing gas in some of the most hostile environment on earth, rather than on the numerous medium sized fields which are close to transport infrastructure.

Yamal consists mostly of sand and permafrost and has no rocky soil, making any kind of heavy construction difficult.

The strategic deposits legislation will continue to help Gazprom acquire more assets without a competitive tender, says Mehdiyeva. However, for some licences, Gazprom has had to fight for licences.

Kamchatka in the far east was Rosneft's prospect but now Gazprom has started drilling there (see page 17), as Gazprom can claim it is essential if Russia is to gasify its far east – something the Kremlin is very keen on, says Mehdiyeva, and which Rosneft was not so keen on.

Other deposits include the Kirinsky block on Sakhalin III. Gazprom can argue that developing Kirinskii on its own is uneconomic and thereby seek more licences for nearby deposits.

One area in which Gazprom will be unable to resist government pressure will be in building the line to Vladivostok, says Mehdiyeva. A major summit of the Asia Pacific Economic Cooperation is due to take place near Vladivostok in 2012, which will focus the mind on the gasification project. And from Vladivostok, the Kremlin can argue, a line to China is only a short stretch away.

Supplying China is more the Kremlin's goal than Gazprom's, says Mehdiyeva, explaining Gazprom's policy of building regional networks in the east, which are separate from the unified gas supply system which was built to supply European parts of Russia and Europe. It does not want to divert gas from its declining gas fields in West Siberia to supply China.

Diversification of routes

Gazprom has been diversifying its export routes since it built the massively expensive Blue Stream line to Turkey almost a decade ago, says Mehdiyeva. Throughout the 1990s, Russia had conflicts with Ukraine over the delivery of Russian gas to Europe. Now Russia's focus is on enhancing the capacity of the so-called 'northern corridor' that will bypass Ukraine.

This is being done through the construction of export pipelines, such as Nord Stream, and the construction of new pipelines within Russia. Gazprom is building the expensive pipelines from Yamal that will avoid Ukraine. It is also building interconnectors between its various routes to allow more gas to bypass Ukraine. A line from Pochinki to Gryazovets and from there to Vyborg, is one example of how existing flows via Ukraine can be redirected to supply Nord Stream, when it is built.

The Caspian states and Russia

While Russia is seeking to diversify its routes for export, Europe is trying to diversify its import routes. But the problem of delivering gas from central Asia to Europe bypassing Russia also has many strands that could frustrate European import plans.

These include the lack of commitment from the Caspian supplier states; Turkish transit demands; Iranian politics;

Iraqi politics; and the legal status of the Caspian Sea, which could allow some littoral states to attempt to block a subsea pipeline.

Mehdiyeva believes that the latter is less of a problem than generally assumed: she argues that the development of Azerbaijan's Azeri Chirag Guneshli oilfields went ahead without the resolution of the status of the Caspian Sea and without a formal delimitation of the Sea into national sectors. It also went ahead despite the protests of Russia. That might set a precedent for future negotiations on the trans-Caspian pipeline, although the evolution of Russia's foreign policy in a more assertive direction compared to the early 1990s raises the possibility of a conflict on the Caspian if Russian concerns are not given proper consideration.

The study points to another obstacle: the complex maneuvering game that Azerbaijan and Turkmenistan have been playing. Both have alternative markets – the European Union and Russia, and China and Iran in the case of Turkmenistan – and it is in their interests to prolong the bidding war.

While the development of the Caspian Azeri Chirag Guneshli oilfields and the Baku-Tbilisi-Ceyhan oil line went ahead despite the protests of Russia, Azerbaijan then was supported not only by a number of Western states including the US, but it had a strong political desire to diversify its oil exports. And Russia was governed by the generally pro-Western Boris Yeltsin.

Today's world is very different. Antagonized by the European Union over what it sees as strong support for Ukraine in its dispute over gas supplies and by the US with its Nato expansion, Vladimir Putin's Russia is not willingly going to sit back and watch its influence erode in a strategically important region, unless it is part of a bigger deal.

Another serious problem though is Azerbaijan's and Turkmenistan's lack of commitment. "They are waiting to see who gives the better deal," Mehdiyeva said.

Turkmenistan and Russia are still at loggerheads over the pipeline explosion occasioned when a massive drop in demand from Russia and significantly reduced offtake saw the line implode. This appears to boost the Nabucco consortium's plans to fill a 31 billion cubic meters/year pipeline from its starting point in eastern Turkey. A commitment to the Nabucco line would also stimulate investment in Turkmenistan's giant South Yoloten and Yashlar fields, Mehdiyeva said.

Turkmenistan's supply guarantee to Nabucco would give this EU-backed project a real boost. Ashgabat's non-committal attitude so far, adopted in part to attract more international attention, could prove counter-productive in the long term, as opportunities for Nabucco will not always be there, the Poyry study argues. – *William Powell*