

**Regional Energy Cooperation and  
the Energy Charter Process:  
the increasing role of Russia, gas and transit issues**

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# EVOLUTION OF GAS MARKETS DEVELOPMENT

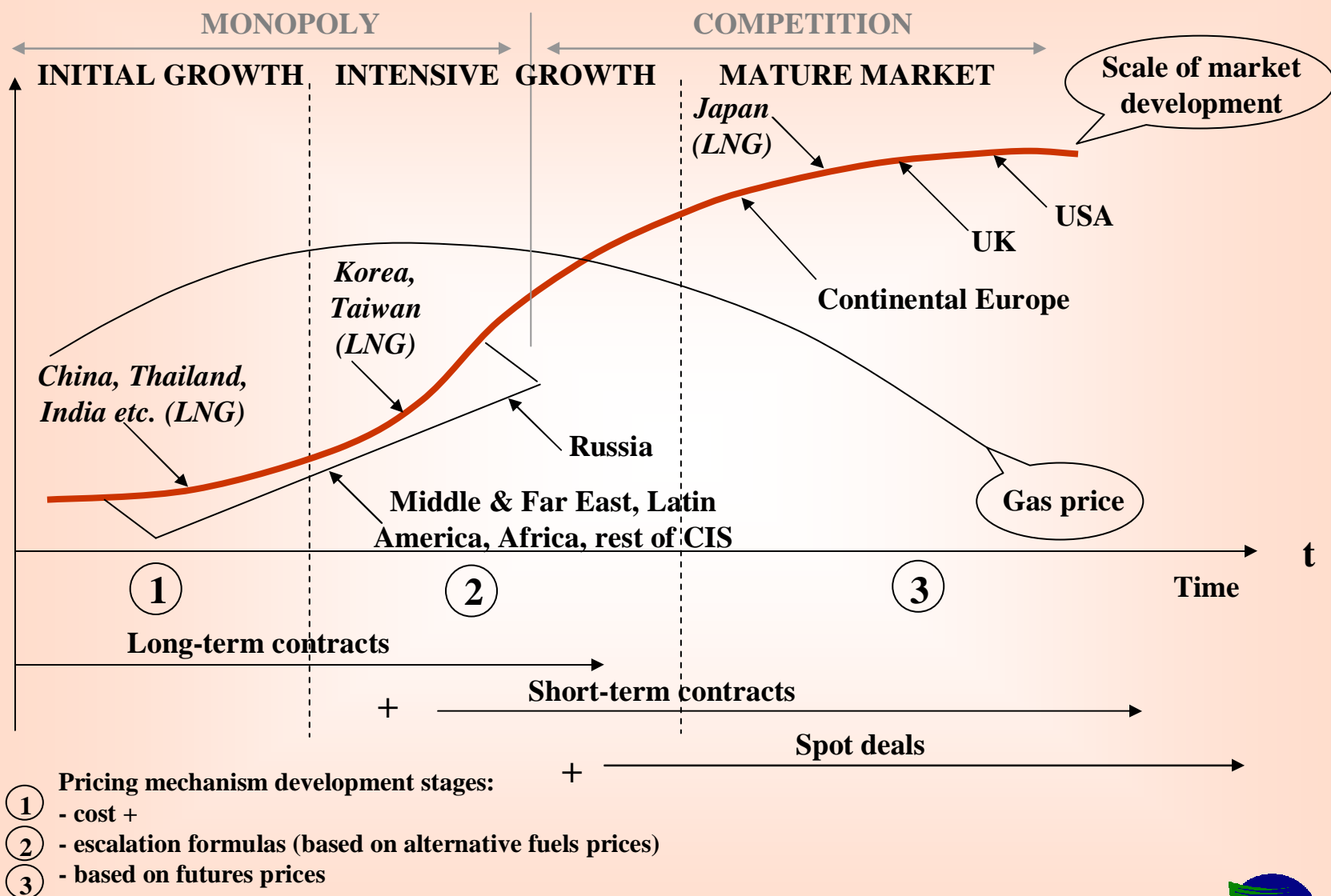
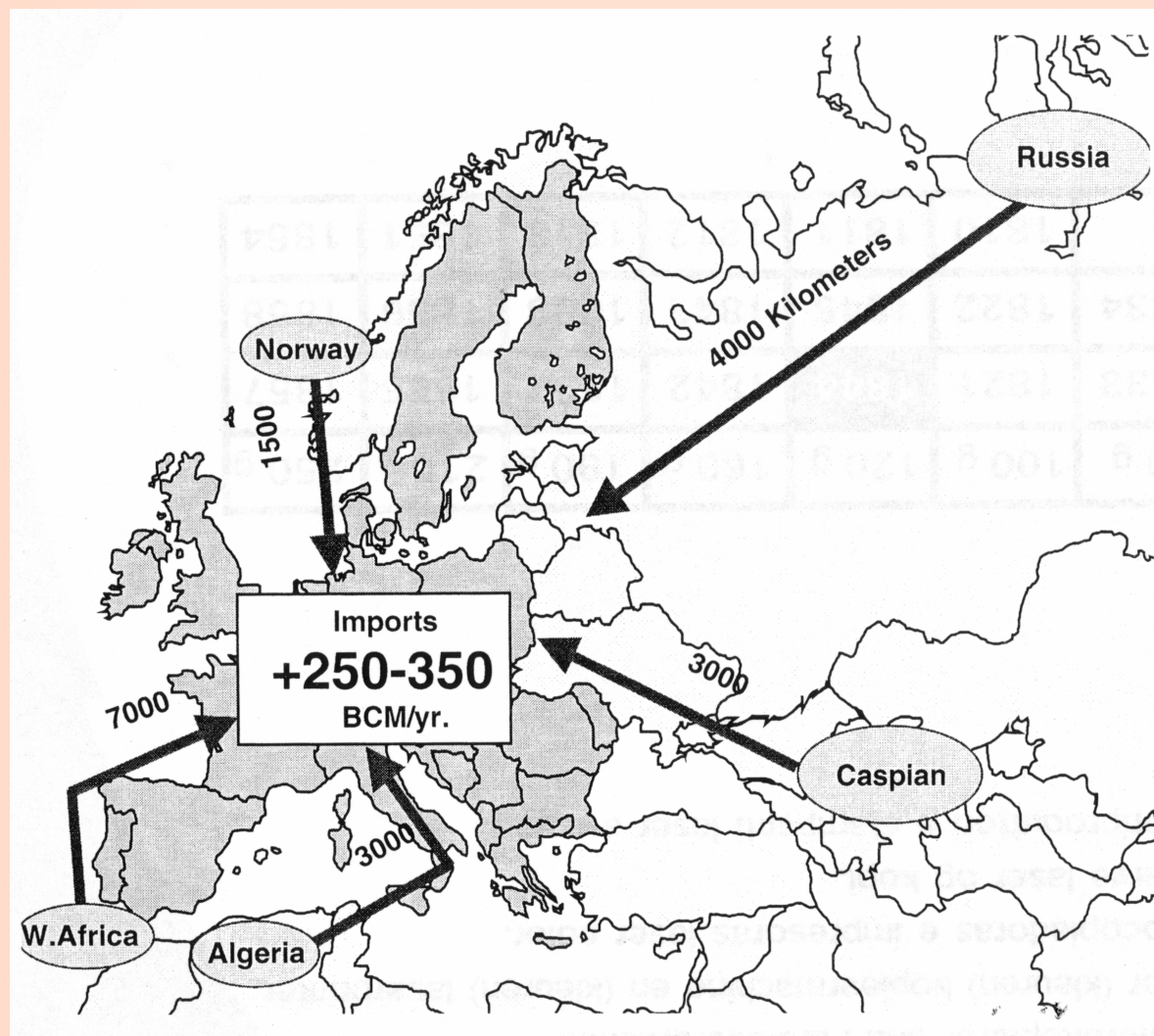


Figure 1

# EUROPEAN GAS MARKET OUTLOOK



**By 2020:**

- **Demand up 200-300 BCM/yr**
- **Imports up 250-350 BCM/yr**
- **New investments 250-300 billion \$**

Source: J.V.Genova/Exxon Mobil

# RUSSIAN GAS IN EUROPE

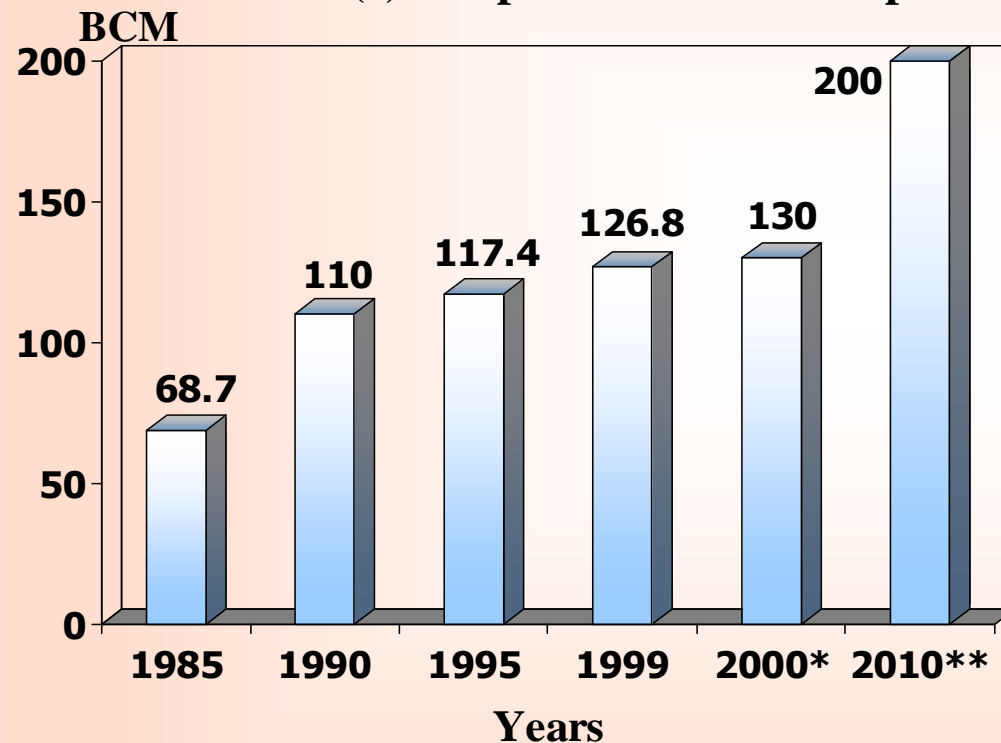
## (a) Share of Russia in gas consumption:

All Europe	>25%
Central & Eastern Europe	40%
Eastern Europe	>90%

## (b) European importers of Russian gas

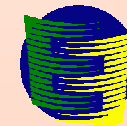
- Austria
  - Belarus
  - Bulgaria
  - Bosnia
  - *Hungary*
  - Germany
  - Greece
  - Italy
  - *Latvia*
  - *Lithuania*
  - Macedonia
  - Moldova
  - *Poland*
  - Romania
  - *Slovakia*
  - *Slovenia*
  - Turkey
  - Ukraine
  - Finland
  - France
  - Croatia
  - *Czech Republic*
  - Switzerland
  - *Estonia*
  - Yugoslavia
- TOTAL: 25**

## (c) Gazprom sales in Europe



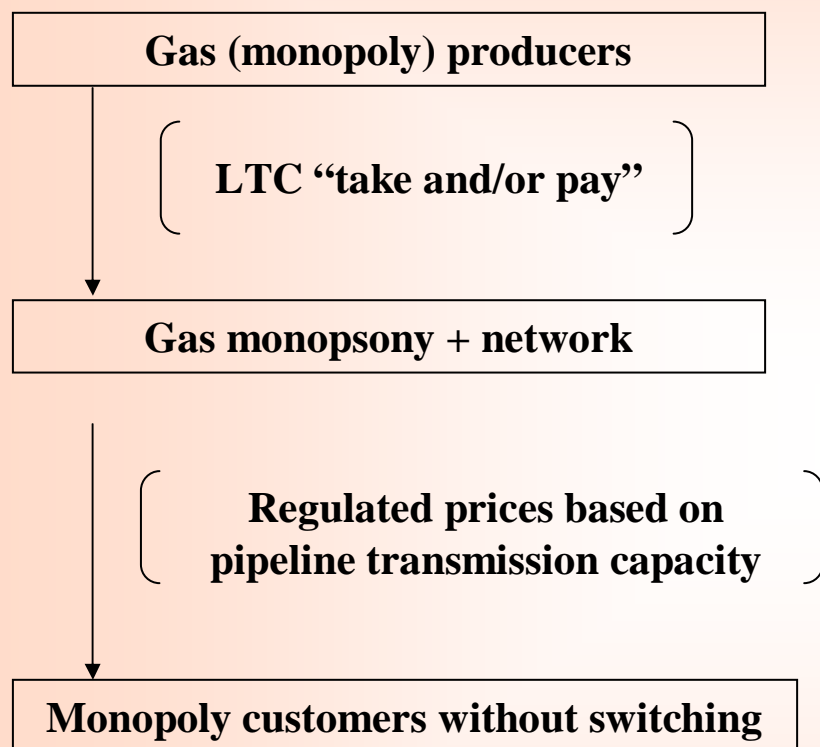
\* Estimate

\*\* Forecast



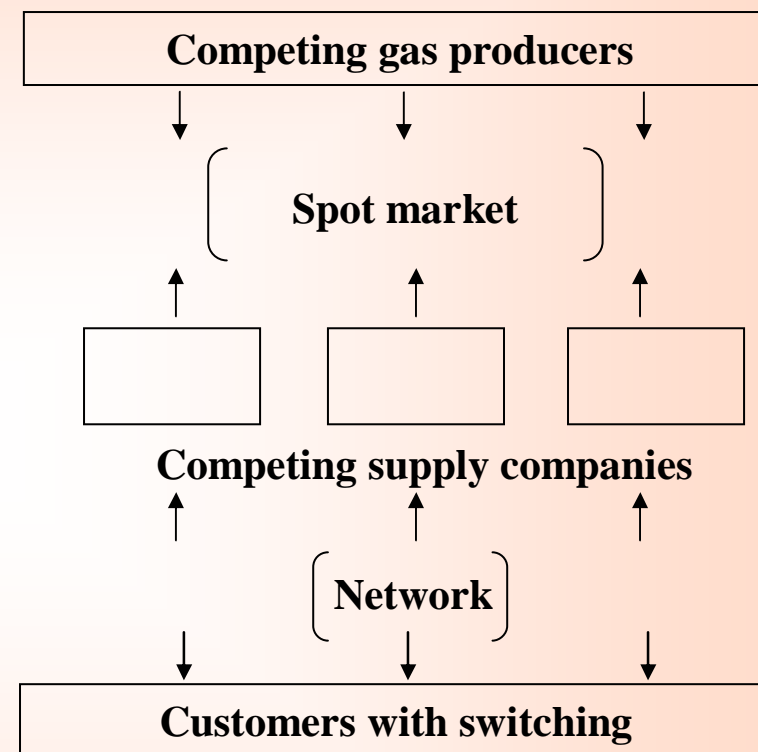
# LONG-TERM CONTRACTS AND COMPETITION IN GAS MARKETS IN EUROPE

(A) Existing organisation of the market

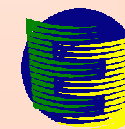


Supply-based consumer prices defined by monopoly producers and suppliers (pricing mechanism: cost-plus; escalation formulas)

(B) Future organisation of the market



Demand-based producer prices defined by consumers (pricing mechanism: spot + forward + futures)



## **GAS: DIFFERENT PROJECTS – DIFFERENT CONTRACTS**

(1) New projects in mature regions with existing infrastructure, with available transportation capacities (usually less capital-intensive projects, relatively small to the existing market) =

(a) short-term contracts (“take and/or pay”) – for the duration of payback period (?)

(b) spot deals – when payback period is over (?):

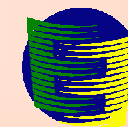
- dated
- forward
- futures

Regions: Western, Central & Eastern Europe

(2) New projects in new regions with no/lack-of infrastructure for both production and transportation (usually more capital-intensive projects, relatively big to the existing market) =

(a) long-term “take and/or pay” contracts

Regions: Russia, CIS, Asia



# **GAS: LONG-TERM TAKE AND/OR PAY CONTRACTS (LTC TOP) AND PROJECT FINANCING RISKS**

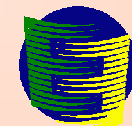
$$\text{Financing} = f(\text{revenue}) = f(\text{volume} \times \text{price})$$

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- (1) LTC TOP = mechanism of supply risks («volume» risks) reduction**
  - (2) LTC TOP + adequate pricing mechanism = mechanism of “price” risks reduction:**
    - prior to exchange pricing: escalation formulas**
    - exchange pricing: futures + hedging**
- (1) + (2) = mechanism of project financing risks reduction (long-term capital-intensive Greenfield projects, i.e. in new regions with no/lack-of production & transportation infrastructure)**
- 
- 

**LTC TOP as a mechanism of risks reduction related to investments into new (Greenfield) gas projects yet has no alternatives at the emerging energy markets**

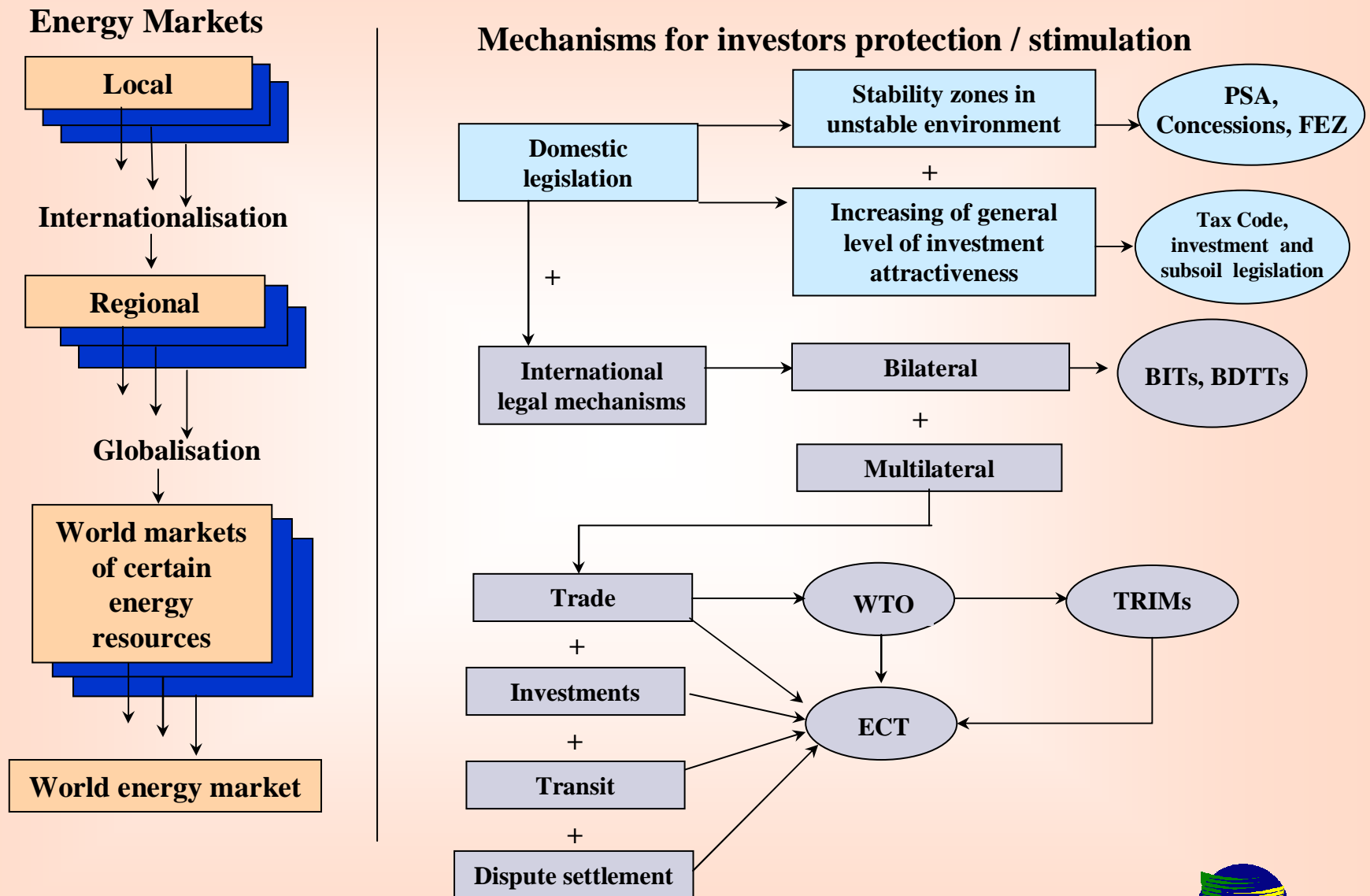


## GAS TRANSIT ROLE FOR MAIN EXPORTERS TO EUROPE IN 1999

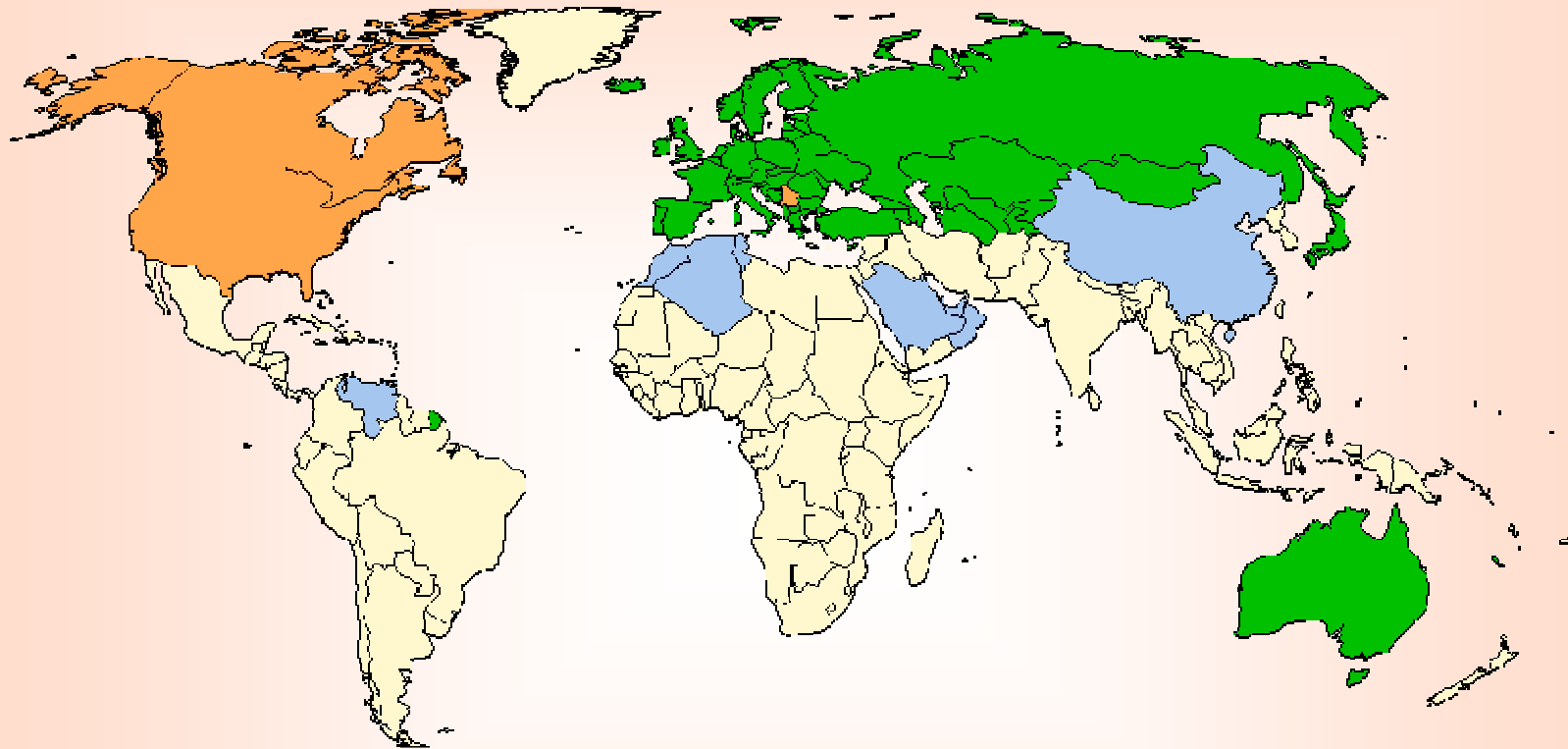
Country-exporter	Direct supplies, % of volume of exports	Transit through the territory of: % of volume of exports			
		one country	two countries	three countries	four countries
Netherlands	76,2	13,8	10,0	-	-
Norway	67,7	7,5	21,4	3,4	-
Algeria	44,9	14,8	9,6	24,3	6,4
Russia	5,4	-	8,9	67,6	18,2



# DEVELOPMENT OF ENERGY MARKETS AND MECHANISMS FOR INVESTORS PROTECTION / STIMULATION



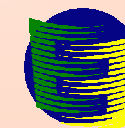
# ENERGY CHARTER TREATY: GEOGRAPHY



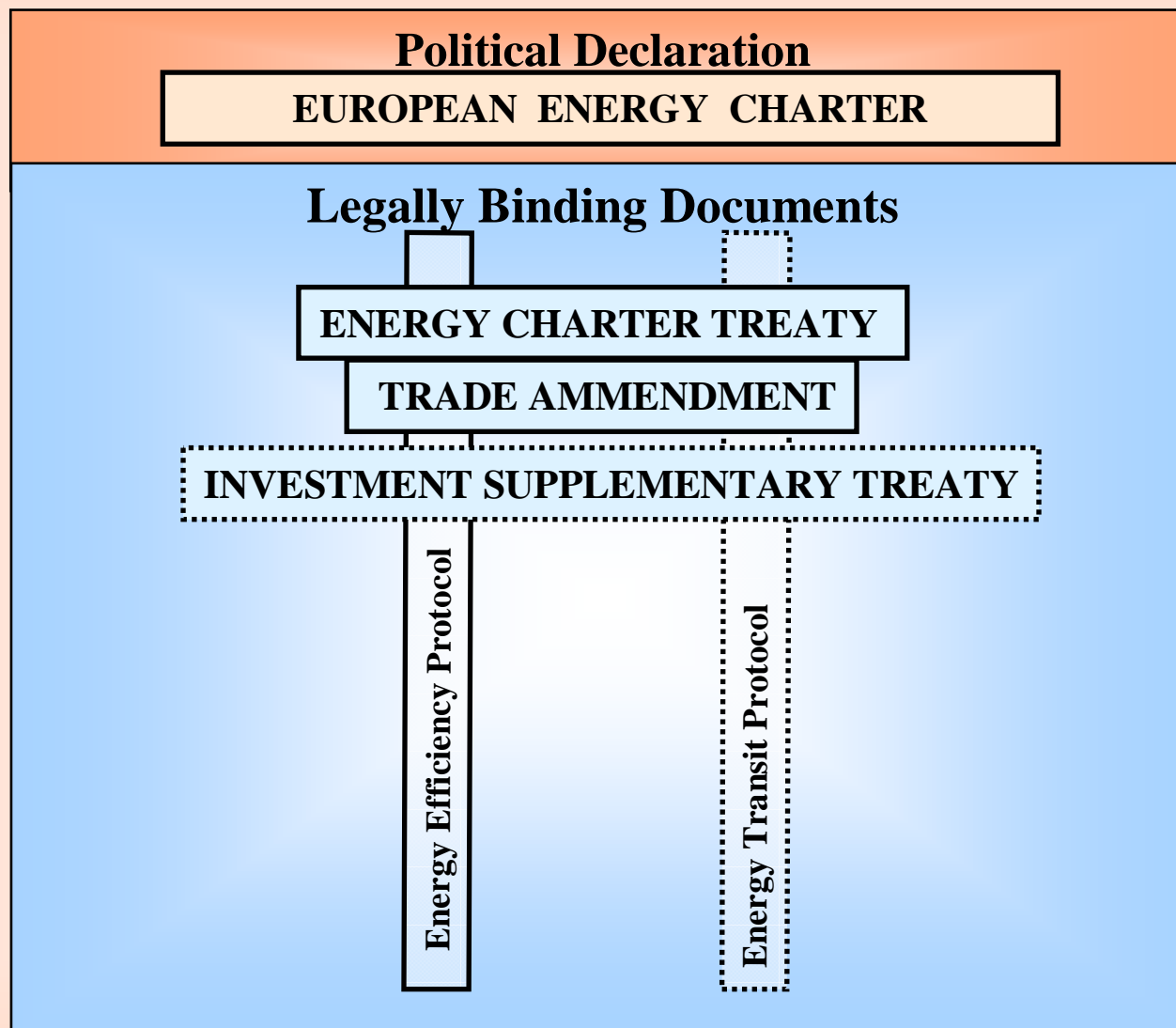
- Energy Charter Treaty Signatory States (1994)
- Observer States that have signed the European Energy Charter (1991)
- Other Observer States

## ENERGY CHARTER HISTORY

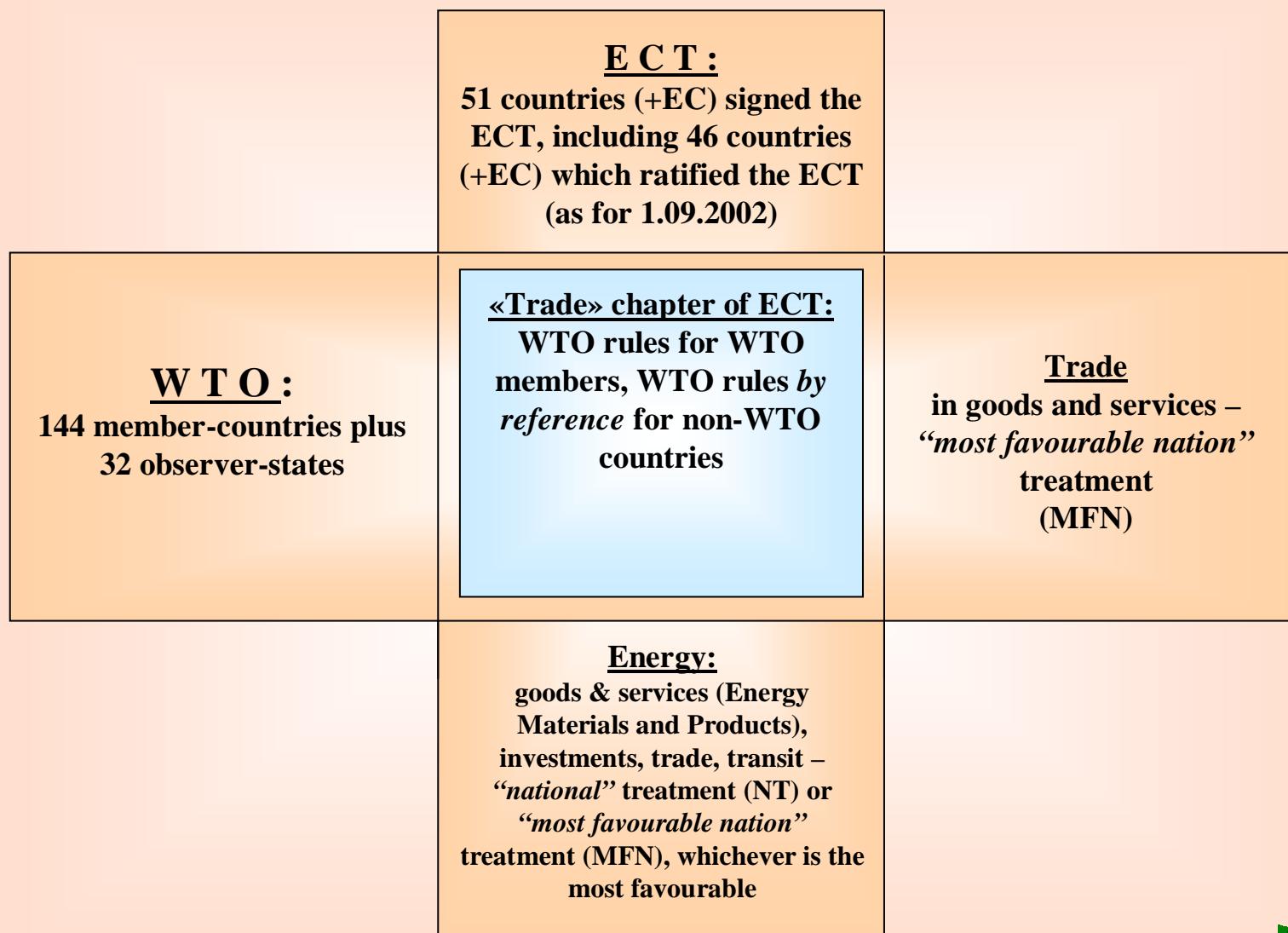
<b>June 25, 1990</b>	<b>Lubbers' initiative presented in Dublin</b>
<b>December 17, 1991</b>	<b>European Energy Charter signed</b>
<b>December 17, 1994</b>	<b>Energy Charter Treaty (ECT) and Protocol on Energy Efficiency and Related Environmental Aspects (PEEREA) signed</b>
<b>June, 1996</b>	<b>Russia started ECT ratification process</b>
<b>April, 1998</b>	<b>ECT came into full legal power</b>
<b>January, 2001</b>	<b>RF State Duma: Russia will ratify ECT, but not yet (depending on Transit Protocol)</b>
<b>As of September 1, 2002</b>	<ul style="list-style-type: none"> <li>• <b>ECT signed by 51 states + European Communities = 52 ECT Contracting Parties</b></li> <li>• <b>ECT ratified by 46 states (excl. 5 countries: Russia, Belarus, Iceland, Australia, Norway ) + EC</b></li> <li>• <b>Russia: provisional application, together with Belarus</b></li> </ul>



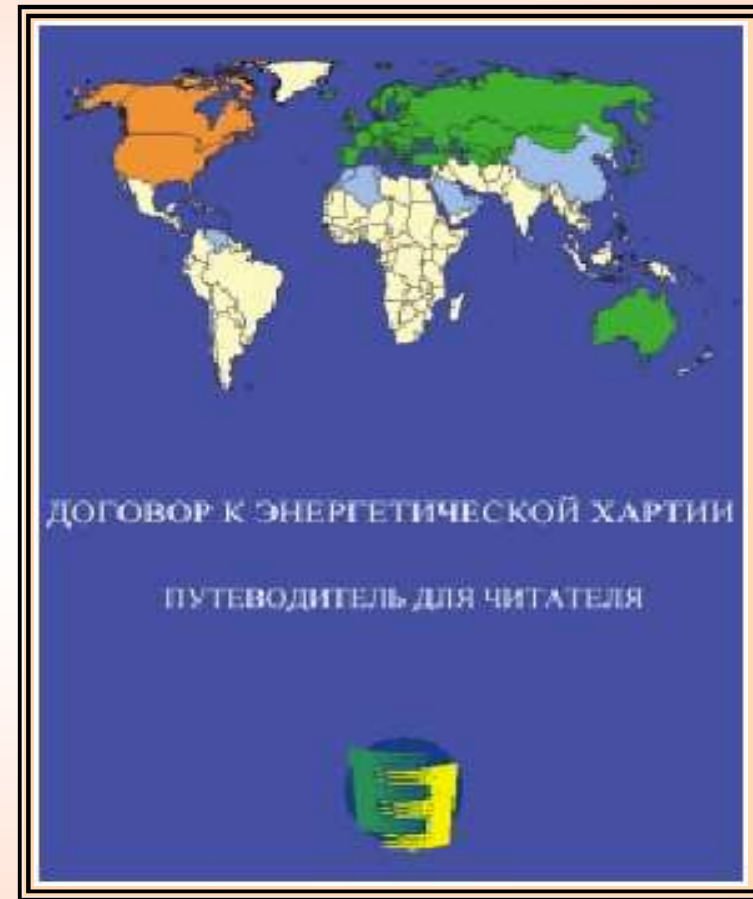
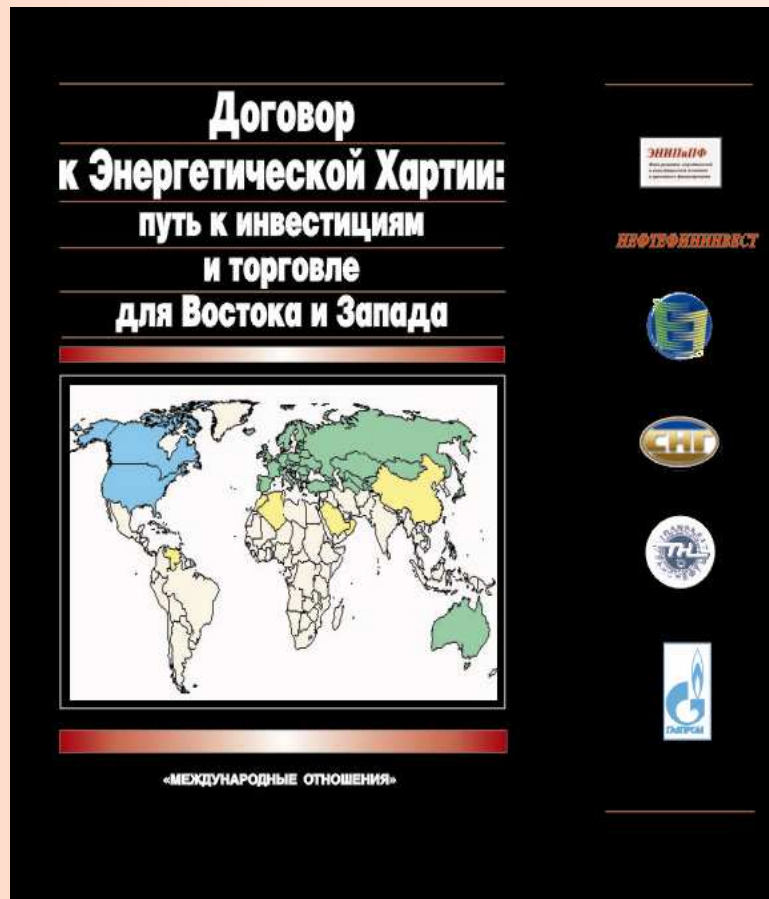
# ENERGY CHARTER AND RELATED DOCUMENTS



# CORRELATION BETWEEN GEOGRAPHICAL SCOPE AND ACTIVITY TARGET OF ECT AND WTO



## MOST RECENT PUBLICATIONS ON ECT:

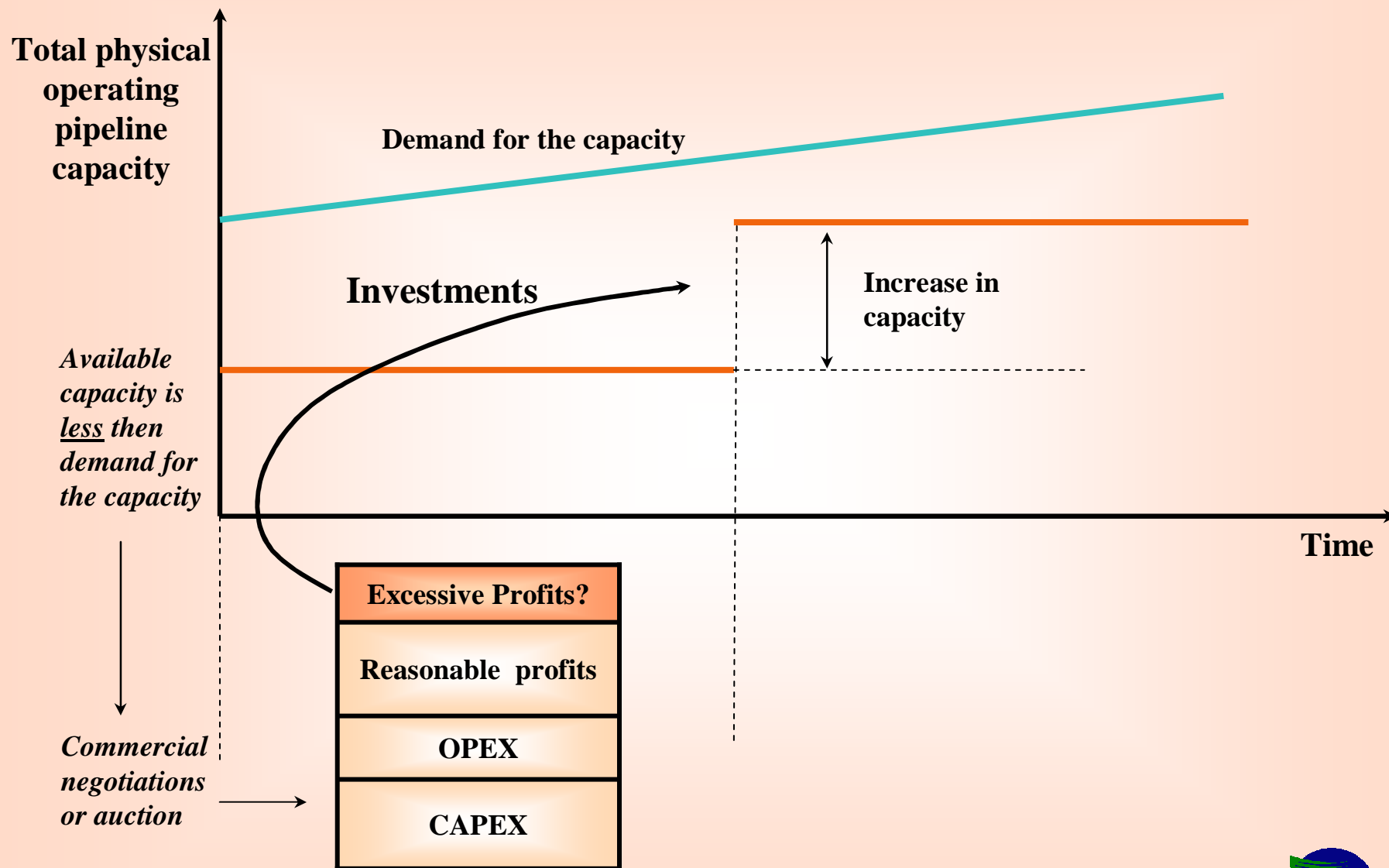


# OUTSTANDING ISSUES RELATED TO TRANSIT OF ENERGY

<p><b>1. Available capacity</b></p> <p><b>2. Environment</b></p> <p><b>3. Geographical scope</b></p> <p><b>4. Conciliation of transit disputes</b></p>	<p><b>Solved in substance</b></p>
<p><b>5. <i>Transit tariffs</i></b></p> <p><b>6. <i>Right of first refusal</i></b></p>	<p><b>Russia – EU trade-off is possible</b></p>
<p><b>7. <i>REIO clause</i></b></p>	<p><b>Major unsolved issue. Subject for bilateral consultations, in particular Russia – EU</b></p>

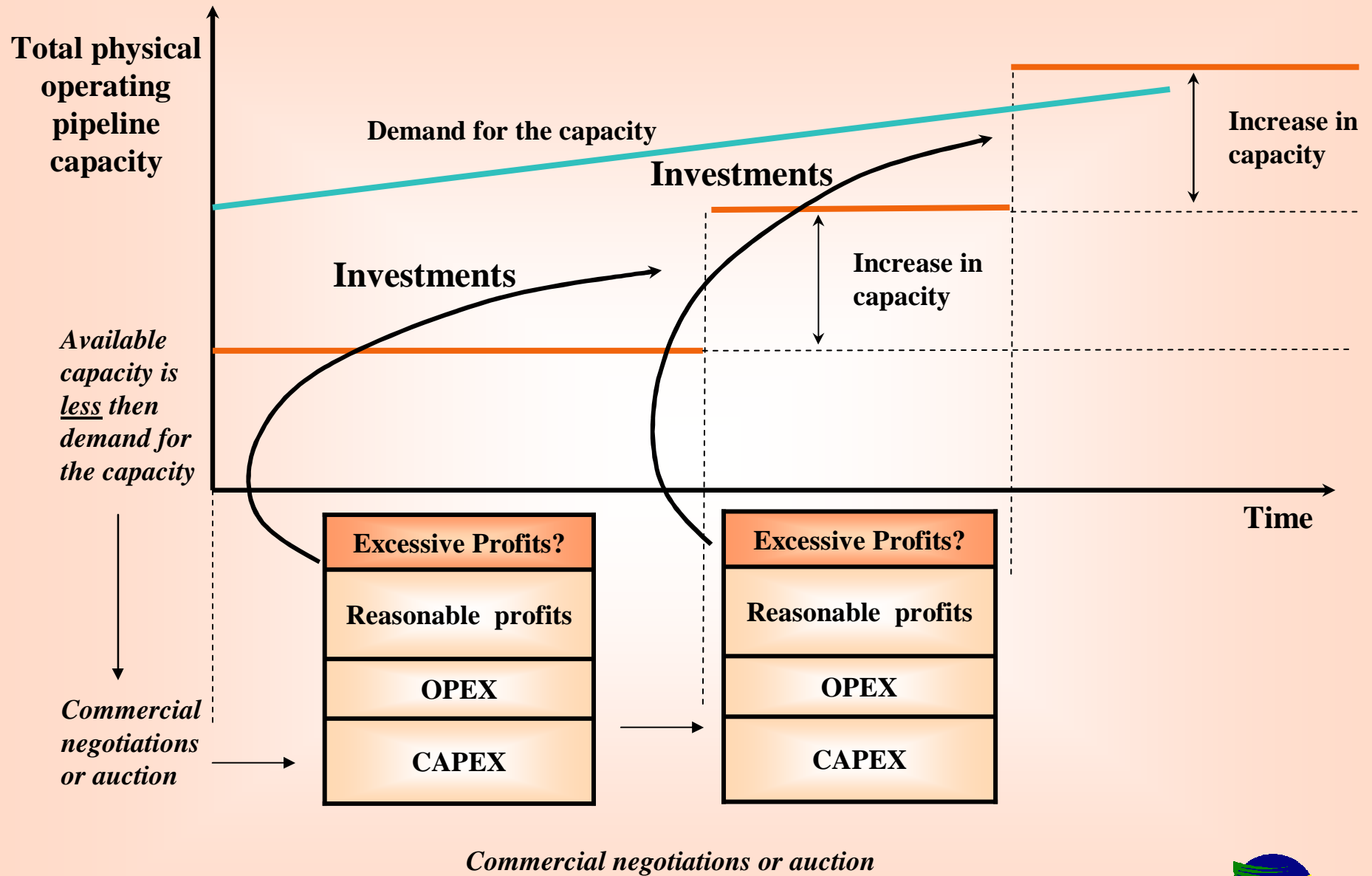
**Negotiations on Transit Protocol: under way since 2000, to be finished (successfully or not) at December 2002 Energy Charter Conference**

# TRANSIT TARIFFS

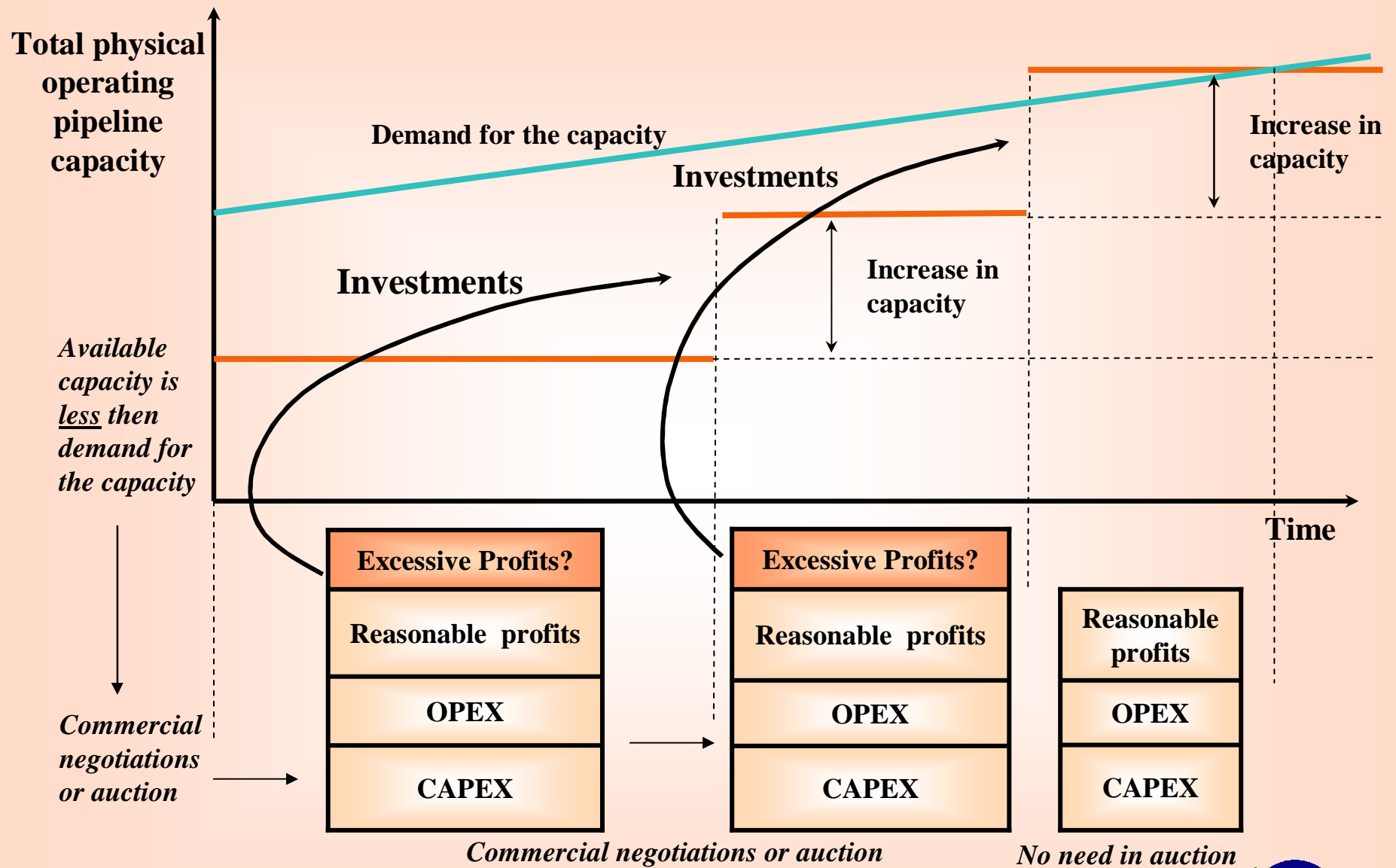




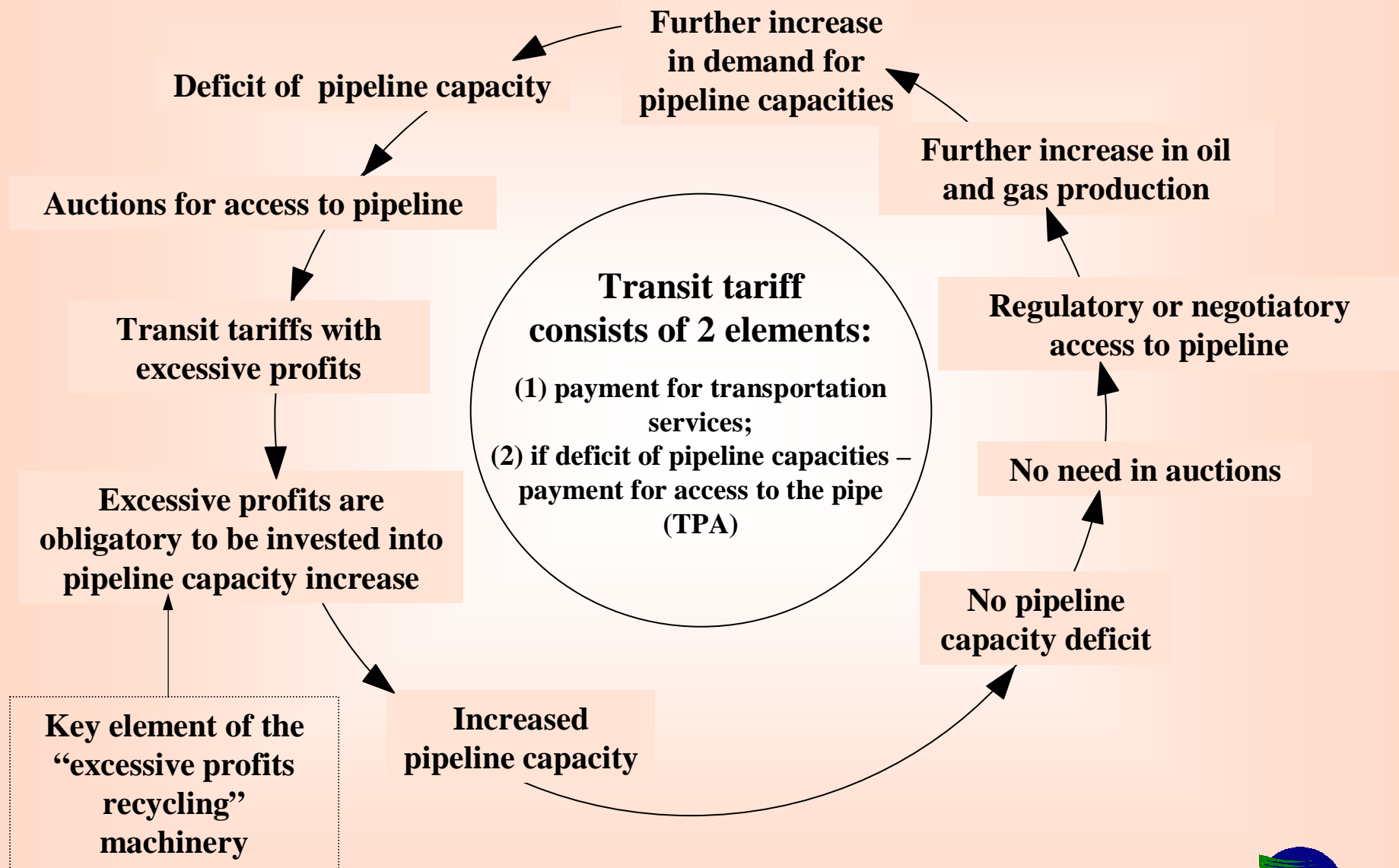
# TRANSIT TARIFFS (continued)



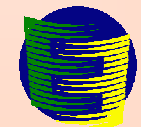
# TRANSIT TARIFFS (continued)



# TRANSIT TARIFFS AND AUCTIONS: “EXCESSIVE PROFITS RECYCLING” MACHINERY

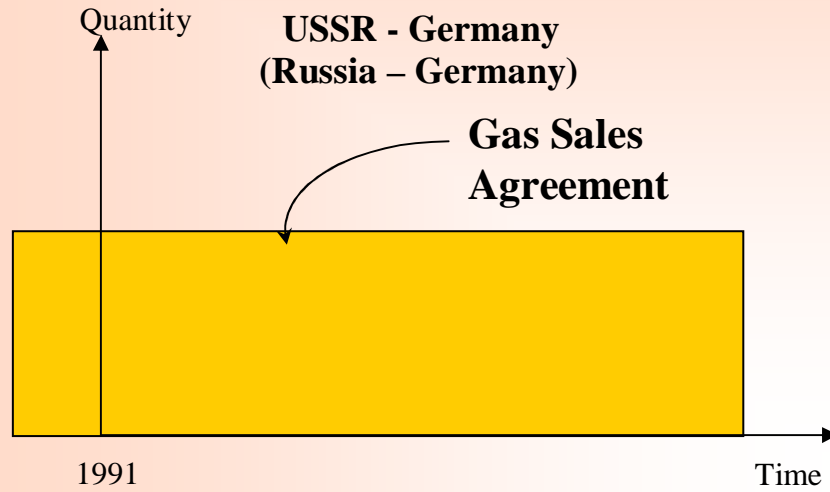


Key element of the  
“excessive profits  
recycling”  
machinery

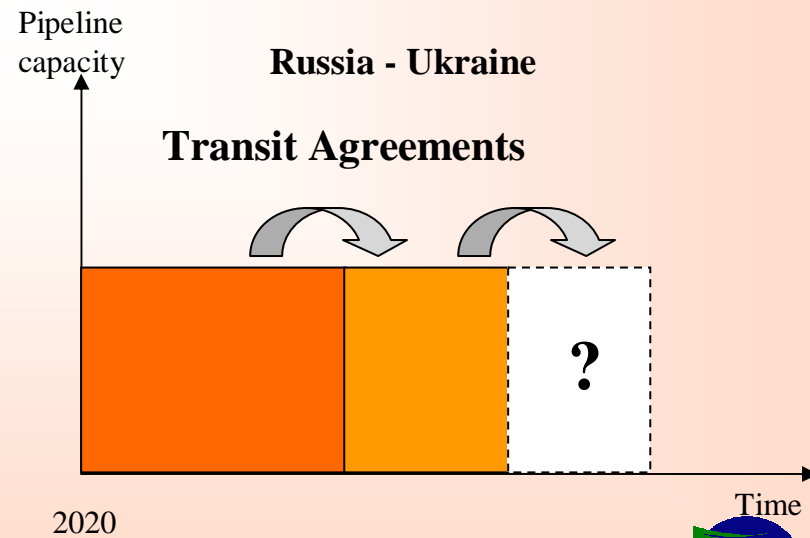
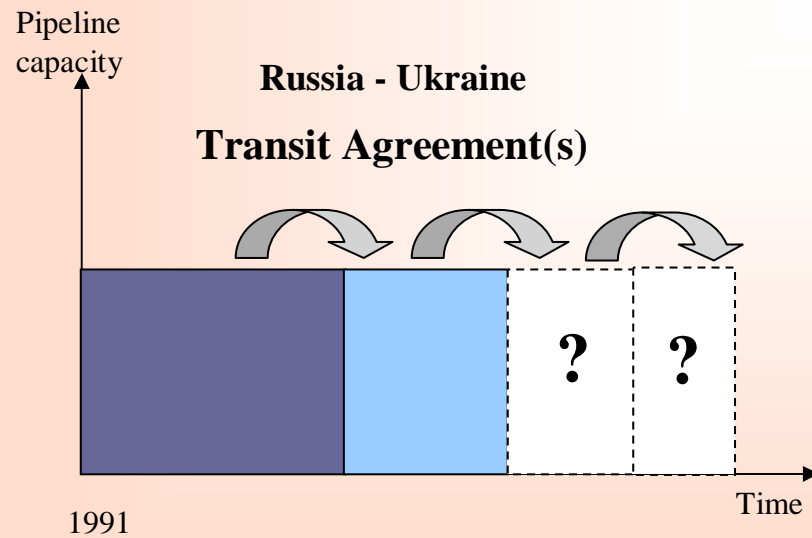
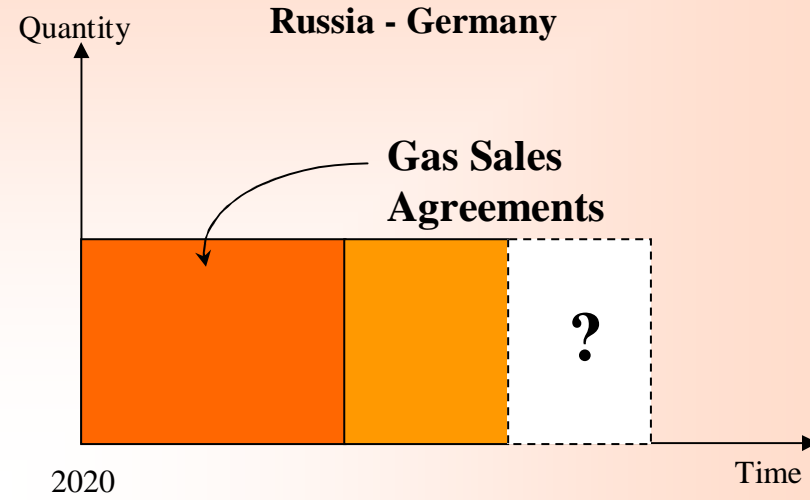


# RIGHT OF FIRST REFUSAL

Currently



In the future



## REIO CLAUSE: GEOGRAPHICAL SCOPE (EC - 15)

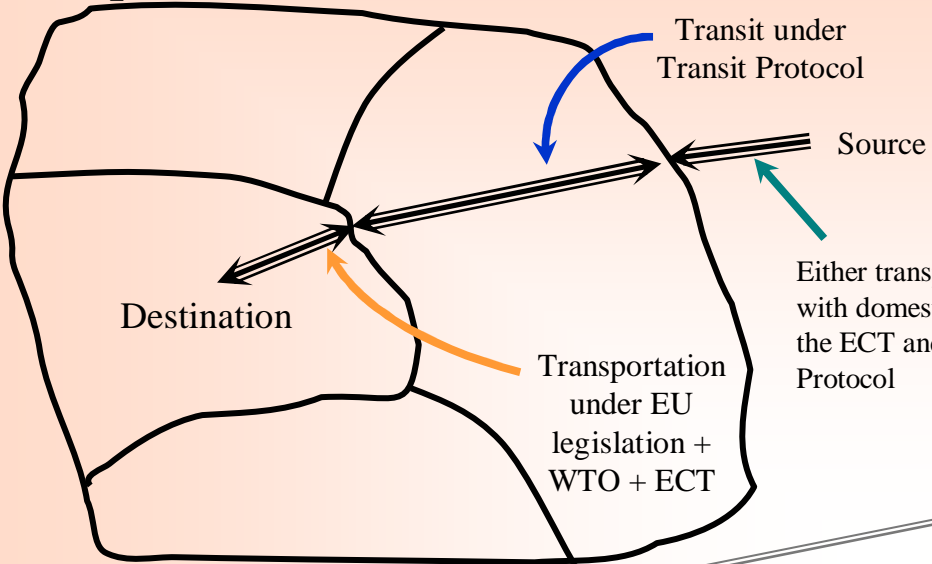


## REIO CLAUSE: GEOGRAPHICAL SCOPE (EC - 30)



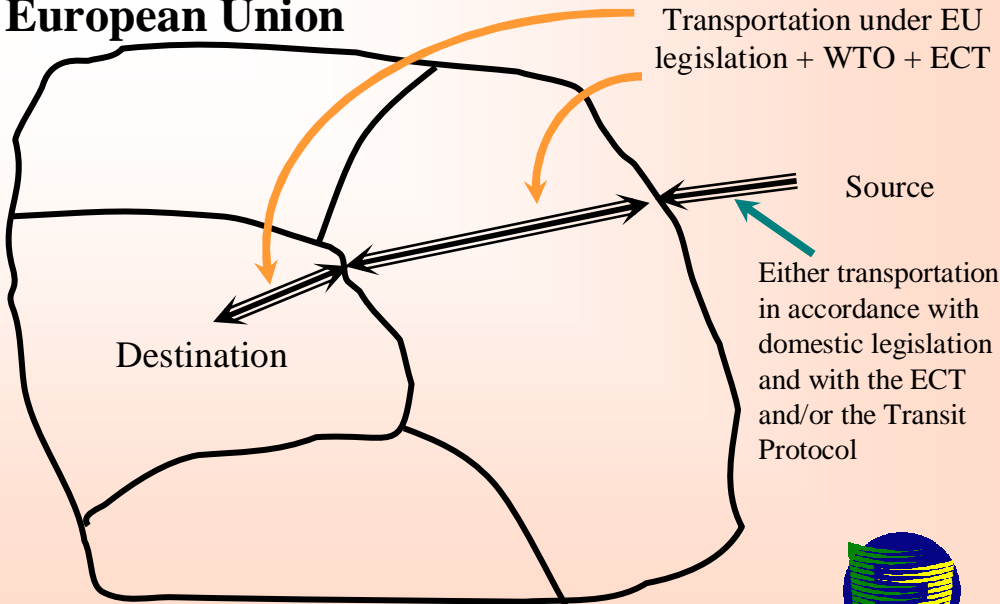
# REIO CLAUSE: LEGAL ASPECTS

## European Union

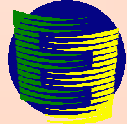


### (a) Before REIO:

## European Union

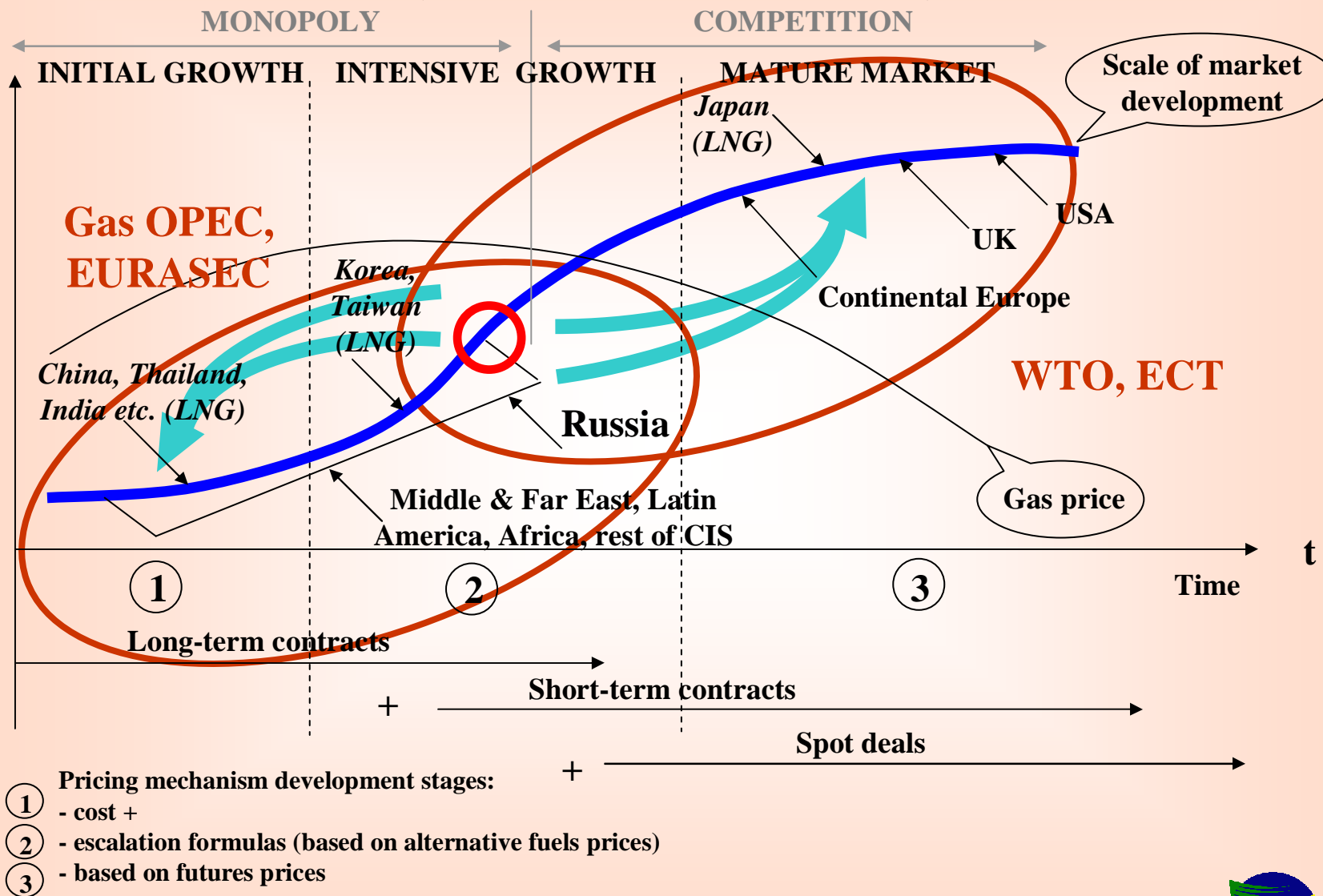


### (b) After REIO:



# EVOLUTION OF GAS MARKETS DEVELOPMENT – 2

## (With whom is Mr Putin?)





# ECT & LEGISLATIVE PRIORITIES OF PRESIDENT PUTIN

