

# Россия и проблемы развития европейского газового рынка

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# **Russia and the problems of EU gas market development**

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# Preconditions for new Russian gas supply model to Europe: commodities market

## 1) Changing contracting structures & pricing mechanisms – operation within new EU gas market architecture:

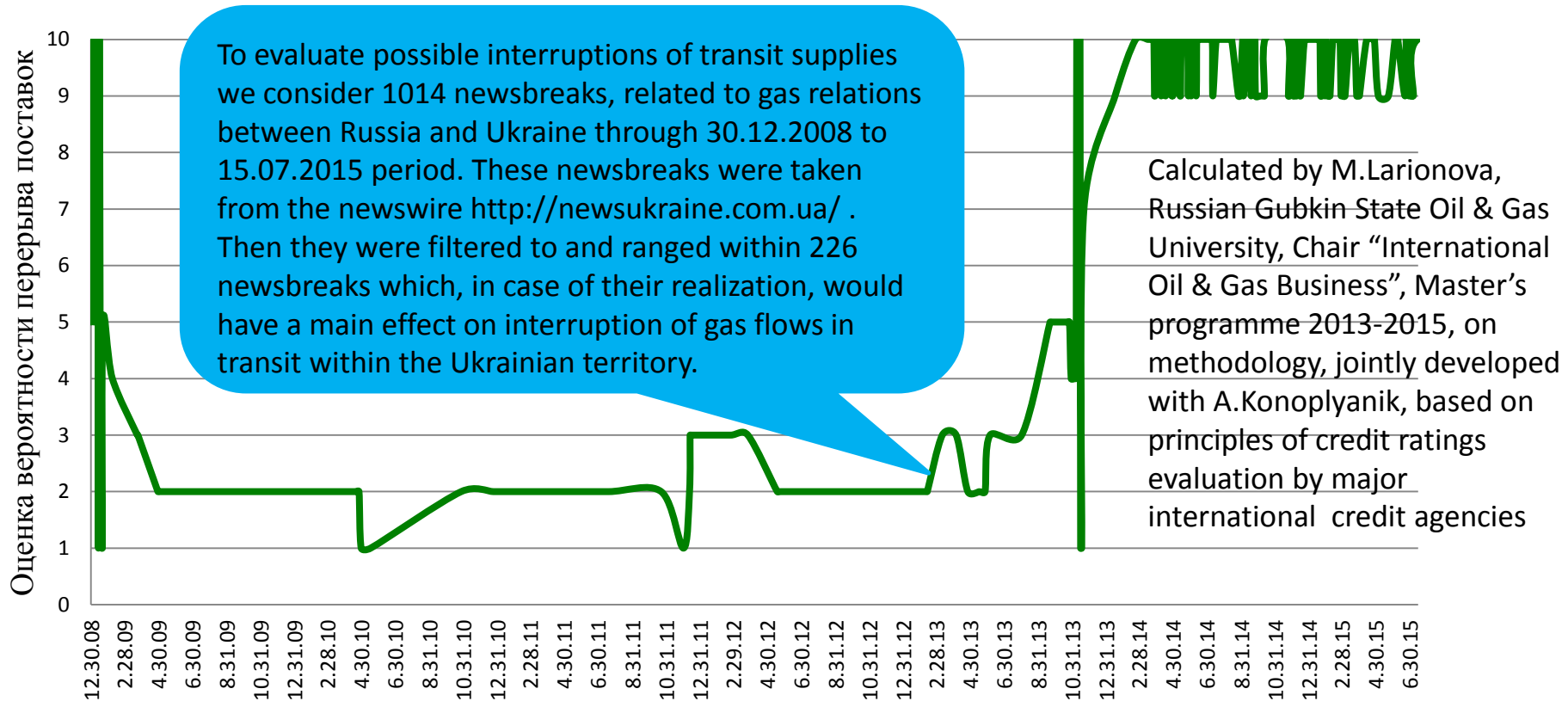
- a. From the **chain of three consecutive LTC** with supply and transportation contracts (first bundled, then unbundled, but to be mutually correlated) - to the system of “**entry-exit**” **market zones** with VTP (hubs) & bundled capacity products at IPs within unbundled commodity and capacity markets
- b. Unbundled **commodity** market: mature & oversupplied (either contractually or physically) market, “gas-to-gas” competition, two market segments – contractual & spot – in competitive coexistence, dev’t of “paper gas” market
- c. Unbundled **capacity** market: supplier as a shipper only; mandatory TPA; capacity allocation: (i) auctions by default, (ii) if more than 2 IPs (cross-border pipelines), conditional booking of new capacity by shipper – “open seasons” (Art.20(d)) CAM NC INC

# Preconditions for new Russian gas supply model to Europe: capacities market

2) Diversification of routes: from GOSPLAN's single pipe/corridor to export market - to “multiple pipelines” concept (at least two pipes/corridors to each export market):

- a. Change of concept of risk assessment/minimization: from (cheaper) central planning & direct control on each export route through to delivery point – to (more costlier) competitive choice among few routes/means of supply (taking into consideration comparative costs & risks)
- b. Economic justification of new pipelines/means of supply to mature markets: not new gas, but transit risk mitigation & liquidation of transit monopoly (Ukraine)

# Ukraine: “transit interruption probability” index (2009–2015)



(1) Very fact that Russia & Ukraine cannot solve issues between them bilaterally; UA demands EU as mediator/conciliator for searching temporary compromises + files a case against Russia in SCC = UA systematic mistrust to contractual partner ; (2) UA is in state of civil war, but considers RF as “invader”, now RF is formally “major military threat” in UA military doctrine => **permanent transit risk for supplier since it is his responsibility to provide timely delivery of contracted volumes to delivery points** (inside EU) non-dependent his issues with third parties => **sovereign right of resource owner (Russia) or its agent (Gazprom) to evaluate such risk & undertake adequate measures for its mitigation (incl. by-passes)**

# UKRAINIAN BYPASSES: Russia's alternative pipelines (two routes for each market)

- Nord Stream project pipelines
- Yamal pipelines
- Ukrainian transit flows
- Turkish Stream project pipelines

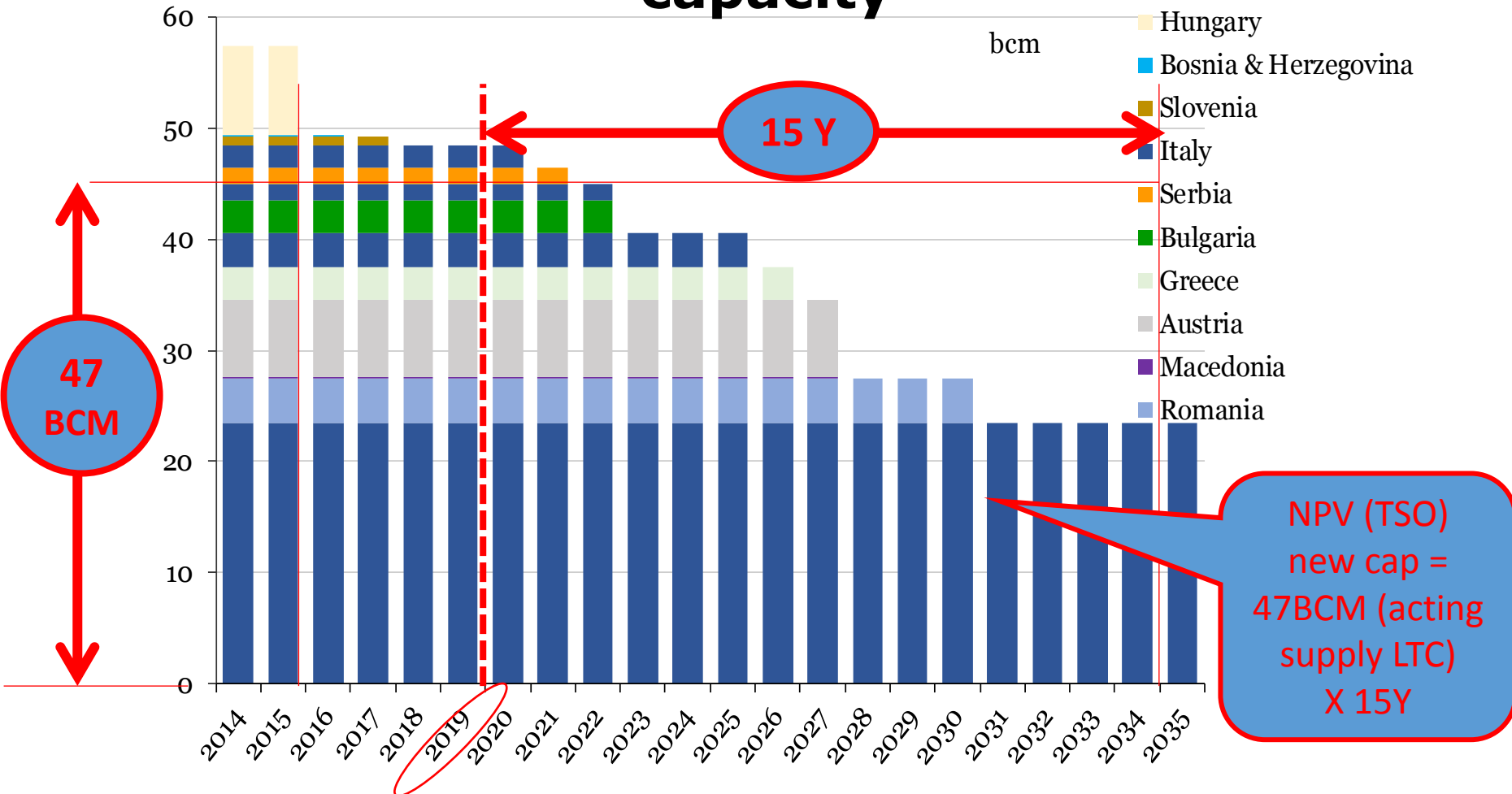


47BCM at 2019:  
How to move from Turkish-EU border to existing DPs in EU acc.to EU rules?

Bottlenecks at Ukrainian route to Southern EU (justification for South Stream with new delivery point):

- ① Ukraine transit crises Jan'2006/Jan'2009
- ② TAG auctions Dec'2005/May'2008

# Russian gas supply contracts to Central & South-Eastern EU with UA transit till 2035 = 100% security for TSO project financing of new by-pass capacity



Source: calculated by E.Orlova (FIEF) based on: "Turkish stream": Scenarios of by-passing Ukraine and barriers of European Commission". Vygon Consulting, June 2015 (fig.4, p.30).

# EU support for transit via Ukraine: the end or the means? (1)

- EU has multiply stated its support for continuation of RUS gas transit via UA post-2019 => (it seems that) this is why EU opposes redirection of RUS gas supplies to new transportation routes to EU post-2019
- But (it seems that) EU (CEC) support for existing & future transit of RUS gas via UA is not the end, but just the means; the real goal is:
  - to provide UA with steady financial flow of transit revenues from RUS supply contracts to EU via UA (with currently “unfriendly” to RF political regime in UA) – instead of donating corresponding EU financial aid to UA, and
  - financing/guaranteeing pay-back of UA-EU-USA GTS consortium (acc.to UA Law 4116a) in modernization of US GTS (*RUS participation in consortium forbidden by UA law, but transit of RUS gas is the only way to make consortium financeable*):
    - either under existing supply formula (RUS supplies directly to inside EU through UA) => RUS will continue taking transit risk via UA,
    - or by newly EUC proposed formula: delivery of RUS gas at RUS-UA border, in which case:
      - either EU companies will take the transit risk via UA by themselves (*which they are not willing yet*),
      - or there might be possible role for de facto EU *Single Purchasing Agency* mentioned in the Energy Union Package ? [*“options for voluntarily demand aggregation mechanisms for collective purchase of gas during a crisis and where Member States are dependent on a single supplier”*] ?



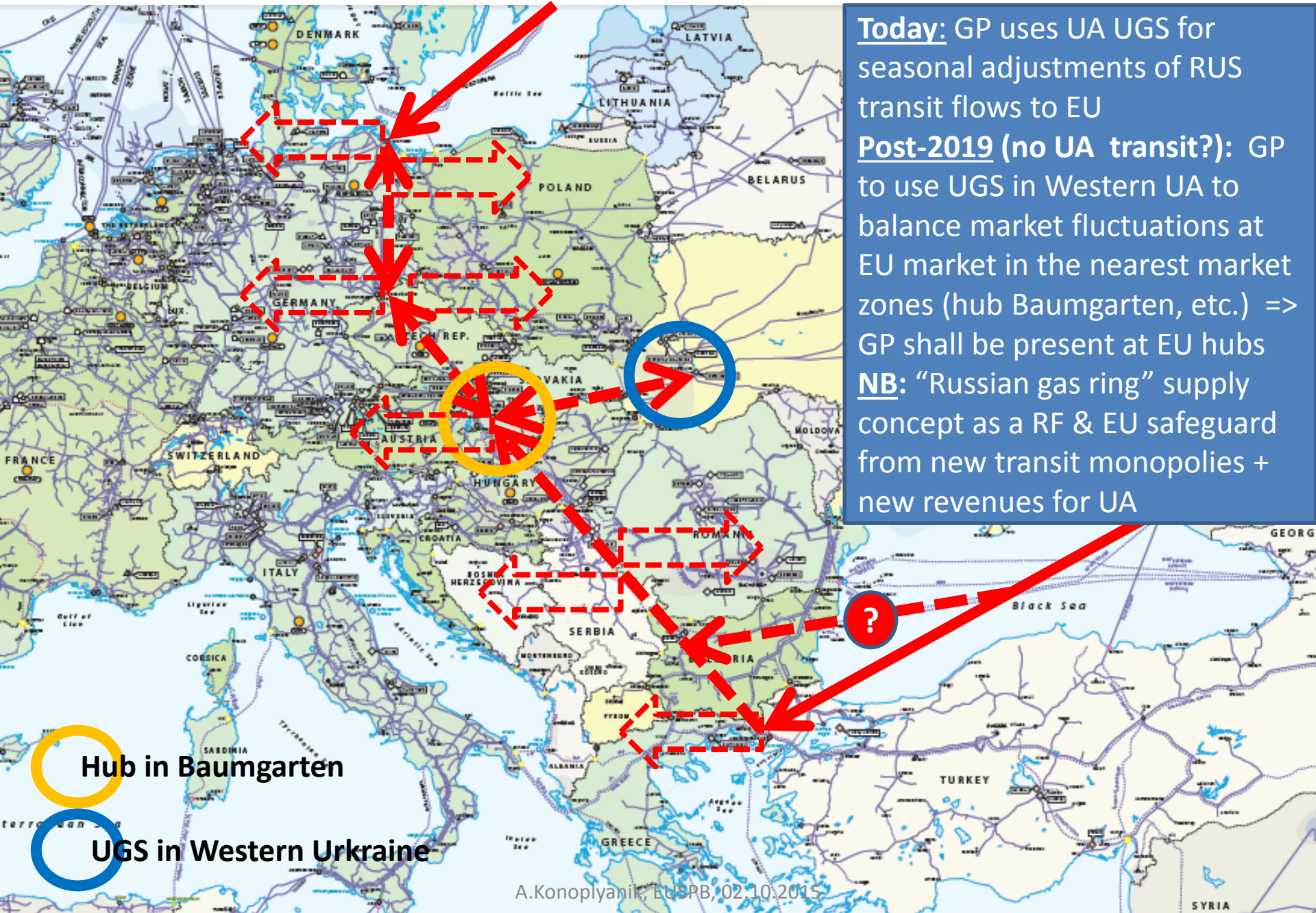
# Project-oriented & regulatory options

- Project-oriented respond from business & EU authorities: fragmented approach (“spaghetti pipelines”/not full compliance with stated demand for new capacity)
  - DG ENERGY: Central East South Europe Connectivity (CESEC)
  - Eastring (Routes A &/or B), Tesla, TAP expansion, etc.
  - Vertical Gas Corridor
- Available regulatory EU options and new respond:
  - Exemptions route (Art. 36 Third Gas Directive)
  - TYNDP/PCI procedure
  - Draft CAM NC INC (draft Amended Regulation 984/2014 Art. 20(d):
    - From draft Art.20(h) – RUS/GG experts proposal to ACER’s draft Art. 20(d) => the latter de facto presents updated version of RUS/GG experts’ proposal on “Coordinated Open Season Procedure”
    - Proposal at WS2 RF-EU GAC for “Early implementation” of Art.20(d) procedure => test study either for Turkish stream or/and Nordstream-2 extensions inside EU

# EU support for transit via Ukraine: the end or the means? (2)

- Whether EU will change its opposition to US by-passes if alternative means for UA to earn money are presented instead of gas transit revenues?
- An idea: “Russian gas circle” with expanded trade at the hub (Baumgarten) which requires regular use of UGS => role for UA UGS ? =>
- UGS in Western UA to be used not for seasonal adjustment of RUS transit flows to EU, but to adjust market fluctuations at the hub (Baumgarten),
  - this will also make Mr.Shevkovich happy since Slovak system will be fully utilized for direct &/or reverse flows both for supplies and UGS use
  - UA will be further integrated into EU energy system

# Russian gas ring diminishes UA transit risk & presents a non-transit way for UA to raise gas revenues (thus covers issue of major EU concern)



Today: GP uses UA UGS for seasonal adjustments of RUS transit flows to EU  
Post-2019 (no UA transit?): GP to use UGS in Western UA to balance market fluctuations at EU market in the nearest market zones (hub Baumgarten, etc.) => GP shall be present at EU hubs  
NB: “Russian gas ring” supply concept as a RF & EU safeguard from new transit monopolies + new revenues for UA

Hub in Baumgarten  
UGS in Western Ukraine

# Thank you for your attention!

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# New model for EU: Evolution of gas value chain & pricing mechanism of Russian gas to EU (1)

Past (Pre-2009) – growing EU market

NBRV = net-back replacement value  
MRR = mineral resource rent



Nowadays (Post-2009) – oversupplied (in NWE segment -?)  
EU market with not yet clear future trends

**Gazprom as price-taker from OIL market**



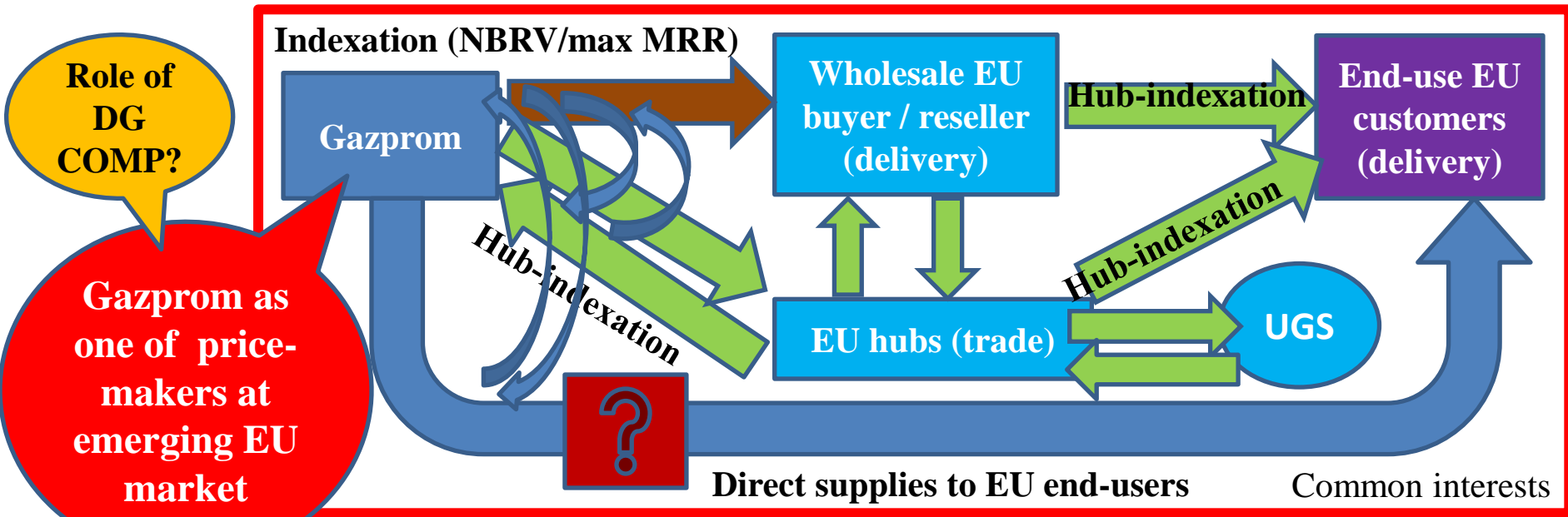
# New model for EU: Evolution of gas value chain & pricing mechanism of Russian gas to EU (2)

Future (“NO GO” contractual scheme under any (?) supply-demand scenario)

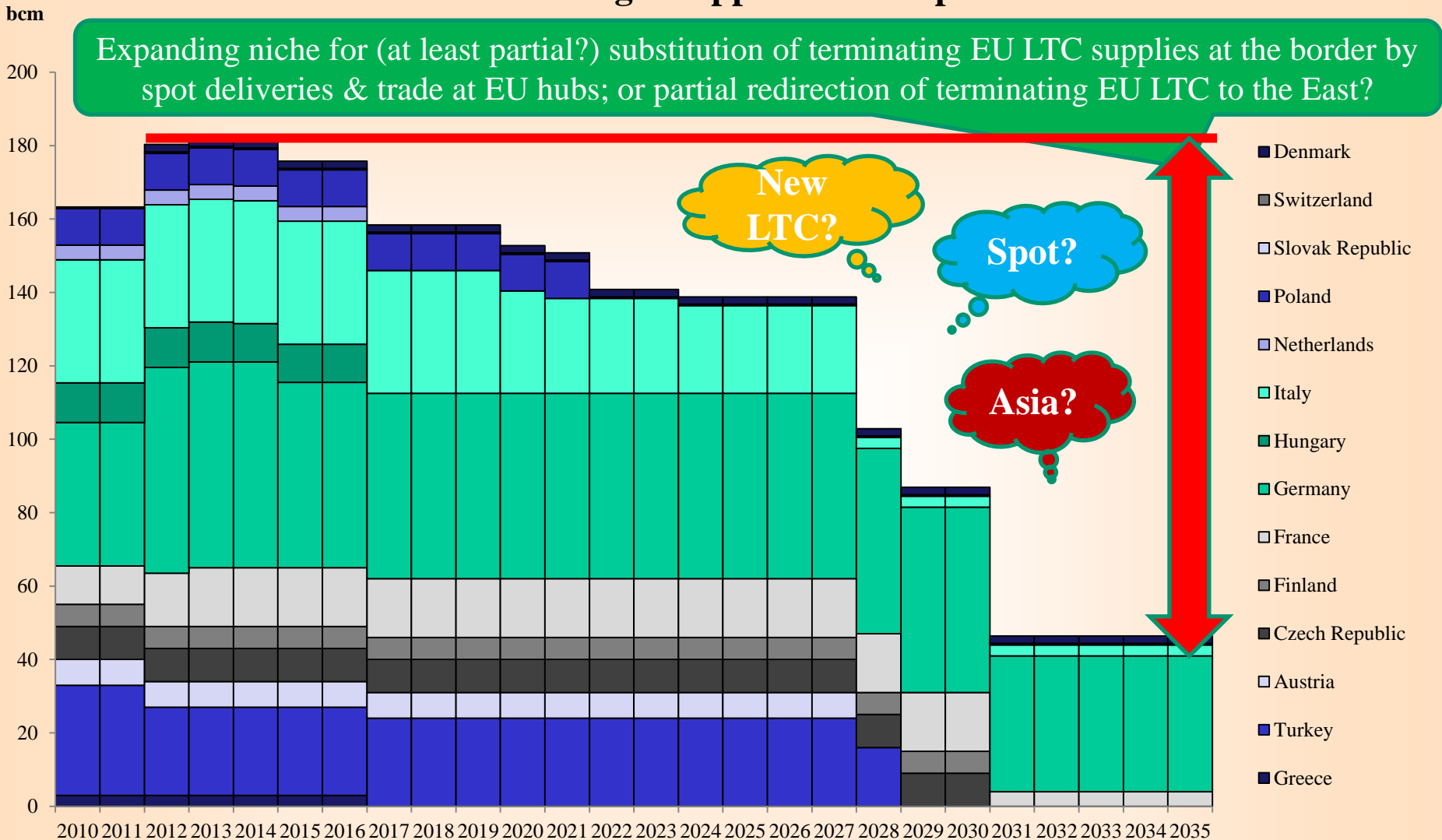


**Gazprom as price-taker from GAS BUYER'S market (with no participation on it)? => NO GO**

Future (what competitive niche for oil-indexed LTC & spot deliveries & trade to/within EU?)



# Contracted volumes of Russian gas supplies to Europe



Source of primary chart): ERI RAS (T.Mitrova), reproduced in & taken from «The Russian Gas Matrix: How Markets Are Driving Change», Ed. by J.Henderson & S.Pirani, Oxford University Press, 2014, Fig.3.1/p.53.