

## Russia and OPEC: Partners or Competitors?

*Armen Oganessian, Editor-in-Chief of International Affairs, adviser to the Minister of Foreign Affairs of the Russian Federation:* I am pleased to welcome the participants in the roundtable organized by the *International Affairs* journal with support from Russia's Foreign Ministry, the Union of Oil and Gas Producers of Russia, and the World Policy and Resources Foundation. As a result of this discussion, we would like to understand – just as we would like our readers to understand – what resources for cooperation with OPEC Russia can count on. At the moment, our contacts are rather limited. Needless to say, we are interested in the entire array of issues that are in some way or other connected with the Russia-OPEC subject.

*Yuri Shafranik, Chairman of the Board, Union of Oil and Gas Producers of Russia:* I have a few points to make. First, Russia has yet to work out a line of conduct with OPEC that would define the advantages and disadvantages of cooperation with the cartel, as well as our public and confidential position in relations with OPEC.

Next, here is one of the main questions for the next several decades: How important will Russia and OPEC be as players on the hydrocarbons market and what weight will other states and associations have in the global oil business? I am confident that Russia and OPEC are significant players. It is another matter that their importance and influence are changing. With regard to OPEC there is a diversity of opinion – from positive to negative. I remember that when the crisis was just beginning, when the prices were beginning to fall, the Saudi oil minister said that OPEC favored oil price fluctuations within a band of \$40-60 per barrel. The minister acted on the assumption that oil producing countries should be first of all interested in a world economic upturn and only then decide on how to make a profit on the market.

I have a favorable view of OPEC; the Organization has been around since the 1960s and in the past 20 years it has been operating efficiently

enough. Russia needs to cooperate with OPEC. Today it is OPEC, not Russia that controls oil price dynamics in the world.

Finally, about Russia's accession to OPEC. This must not be done under any circumstances. But it is outright imperative to look for interaction and frank communication with this organization. At meetings with OPEC member states' foreign ministers, Russia should have an equal level of representation.

***Vitaly Bushuyev, General Director, Energy Strategy Institute:*** To define our relations with our partners in the world community, it is essential to have our own view of the development of the global energy situation not just for the current period but also in the long term.

Our institute has completed a major project to forecast the development of the global energy sector through 2050. We believe that the past crisis indicates that the future development of the global energy sector will be uneven, new "bubbles" will appear, and there will be new crises and changes in technological standards, energy demand, and the economic development paradigm in general.

I would like to make three points. First, we are entering a period when globalization, in particular energy globalization, is giving way to energy regionalization. Many consumer countries have set a course toward the development of their own energy sources and achieving energy self-sufficiency, and this is having a serious impact on the position of those companies or exporting countries that have been dictating their terms on the market. Securing independence from imports can have a serious impact on the situation of exporting countries, especially if it reaches 60% of energy consumption. The result will be that demand for energy imports could fall significantly. So the period after 2012 appears to be very dangerous in the short term.

Second, the United States has serious plans for the introduction of electric vehicles. By 2020, up to 50% of vehicles in the United States will have electric engines and by 2050, the share will be 80%. In that event, of course oil demand will fall very seriously. These plans cannot be ignored. But if we do not look so far into the future but talk about 2014-2016, prices, price dynamics will remain a key factor here. I have every reason to say that both Russia and OPEC no longer influence the pricing policy on the world market. Prices on the world market are determined by people who have available capital, and oil prices are evidently expected to fall. So far all our forecasts have been fulfilled. In 2006, we spoke

about prices rising sky high, to \$60, and then they went up even further, to \$100 and more. From March 2010, we started talking about a price rise due not to economic growth but the infusion of free capital in different sectors that is bound to spread to raw materials. We viewed the short-term period of 2012 as risky. We should be talking not about a concrete price but the risks that can arise.

Finally, third, OPEC deserves respect if only because it acts more than it talks. Russia has something to learn from the Organization. A long time ago, OPEC oil exporting member countries adopted a development strategy to be followed after the oil boom, and they are not afraid of oil production decline in their countries. They are developing oil refining capacities, demonstrating flexibility in business diversification.

Finally, about Russia's accession to OPEC. This must not be done under any circumstances. But it is outright imperative to look for interaction and frank communication with this organization.

**A. Oganesyan:** Cooperation strategy consists in mutual survival in a market environment. This year the United States was in panic because it did not know where to get energy resources from. However, if you take a broader look at the situation, taking into account Asia's growing role and the opening of new markets, does it not seem to you that this will play some compensatory role with regard to the mass introduction of electric vehicles in the United States?

**V. Bushuyev:** I am skeptical that a trend toward increasing demand will manifest itself sooner or later. There will be no rise in demand either in the United States or in China or in other countries. There will be none in the United States because it has clearly set a course toward limiting domestic energy consumption and energy imports. Although even despite increasing shale gas production it will still have to buy something, maybe not on such a scale. I believe that in China, too, demand will not be growing at the same rate as now. The Chinese also have set a course toward electromobility. In Europe, the situation with energy resources is stable while demand in Africa is not much of a factor. There is no energy shortage anywhere in the world. The only issue is the price. The Americans benefit from keeping the prices high – at \$100-120 per barrel – because

that helps them solve the political problem of developing their own resources. But those who talk about a price of \$150 per barrel forget that with such a price the global economy will freeze.

**Stanislav Zhiznin, President, Center of Energy Diplomacy and Geopolitics:** I have been studying OPEC since 1997. What has changed during these 13 years? In 1997, the decision was made to develop our ties with OPEC without undue haste and prepare a draft cooperation memorandum. Then reality brought some serious changes with the oil price plummeting from \$22 to \$9 per barrel and in 1998 oil industry executives and major oil companies asked the Russian Ministry of Foreign Affairs to analyze the situation and issue recommendations on what we should do with OPEC. A brainstorming session was organized – a conference with the participation of major company chiefs. After that the OPEC secretary general was invited to visit Russia while Russia received an official invitation to participate in OPEC ministerial meetings.

Initially, there was a flurry of activity – contacts, trips, and ministerial meetings. All Russian companies took part. When the oil price rose, they calmed down and the level of representation declined: The meetings started to be attended by deputy ministers and then by ministry department heads. But that is unacceptable since OPEC is an international organization interaction with which requires compliance with certain protocol rules. So our relations plunged.

Then the oil price plummeted again, from \$150 to \$40 per barrel and Russia upgraded its relations with OPEC to the level of deputy prime minister. I. Sechin led the Russian delegation at Organization sessions three times. Russian oil companies also raised their profile. At that time we again received an invitation to join OPEC. The issue was studied and the decision was made that we should not join it, since there were more minuses than pluses. In 2008, we submitted a draft memorandum of cooperation between the Energy Ministry and OPEC. An official reply has yet to arrive. In that same year, the OPEC secretary general met with the Russian president in Moscow.

During the upturn in our relations in 2003-04 and 2008, three Russia-OPEC seminars were held in Vienna and Moscow, organized by the MGIMO (Moscow State Institute (University) of International Relations). Russia did not send a delegation to a fourth seminar, in Vienna, and it did not take place.

What is the situation now? OPEC has stopped inviting observers from

Russia to its sessions. After OPEC sessions, symposiums are held in Vienna two or three times a year, and these are very important events. They are attended by top level officials – ministers from OPEC member states and independent states such as Norway, Mexico and the U.S., and heads of national oil companies from OPEC member states. However, Russian representatives have not once participated in such symposiums, let alone spoken there.

And here is another important fact: Last year OPEC's 50th anniversary was celebrated in Riyadh, but Russia was not invited.

OPEC is in active energy dialogue with the European Union; they have an interaction mechanism and a well defined agenda. It also has ties with China.

OPEC regards Russia, Kazakhstan and Azerbaijan as potential members. Most of all they are wooing China as they take an interest in the Caspian region. They did not exactly set up a Russian department but at any rate, there are several people studying Russian there. Their first goal now is Kazakhstan.

We have common interests with OPEC member states: Both we and they are interested in a stable, predictable oil market and reasonably high prices.

***Ivan Ivanov, Member of the Russian Academy of Sciences:*** Russia is the largest exporter that had no way of influencing energy market prices. We occupied an intermediary position between oil consumers – the Organization for Economic Cooperation and Development (OECD), the International Energy Agency – and oil exporters – OPEC. We did not like OPEC discipline. We missed our chances for a qualitative improvement in our cooperation. We are establishing significantly closer contacts with oil consuming countries. I believe that we need to think well before doing anything together with our partners – oil consumers. There is now talk about joining the OECD, but if we are to join it we must also join the International Energy Agency.

It would be useful to consider the idea of joint Russian-OPEC expert market forecasting. If OPEC shows interest in Russia lowering production levels I would do that because it would have no impact one way or the other. What is important for us is export, not production. Furthermore, we need to think about diversifying Russian oil exports, 30% of which to Asia is carried by rail; unfortunately, Russia does not have an oil tanker fleet.

Another point. Almost all large oil exporting countries are OPEC members except Azerbaijan and Kazakhstan. In this situation it is important to understand how we need to act. After all, this area is not closed – it is very close to us and we should clearly see the prospects of these two countries.

*Alekander Gorban', Director, Economic Cooperation Department, Ministry of Foreign Affairs of the Russian Federation:* Cooperation with OPEC should be multidimensional.

As for joining the OECD or the IEA, we cannot do that yet. We cannot apply for IEA membership without being an OECD member. From my perspective, OECD membership is no less important than WTO membership because the OECD is a kind of accumulator of ideas and of very extensive experience in socialist and capitalist competition. Incidentally, we could gain a good deal from that. As for forms of cooperation with the IEA, this is up to us to choose. But it is not necessary to join it and thus irk OPEC.

We will not annoy them by our consistent steps, even if they do not respond to OPEC's interests. As is well known to all of its member states, it is OPEC's practice to make decisions not to increase oil exports, but countries do that anyway. When Saudi Arabia significantly increased oil export, OPEC took offense. And if we want to raise it, we just go ahead and raise it: We can always say that we have so decided in a gentlemen's agreement.

As for the pricing policy, it is of course a sensitive issue. It is practically impossible to predict what will happen or when. If we look back into the past we will see that no one expected the price to reach \$148 per barrel. Such price "bubbles" are inflated when an opportunity appears. Financial speculators play a leading role here. No one can influence these financial machinations. We underestimate the impact of the psychological factor on financial speculators. They themselves do not even know when they will get spooked and start pulling out their capital. But that could happen at any moment. This can only be influenced by establishing a powerful financial structure. The G 20 is trying to do something about it but there have been no genuine success stories yet. Now France will hold the rotating presidency at the G 8 and the G 20. In this connection Nicolas Sarkozy came up with a very interesting initiative relating to our present discussion: He proposed that Russia develop a new pricing system for raw materials. These are not only hydrocarbons but also food-

stuffs, metals, etc. Although we backed the French initiative in general, I have not noticed any serious work being done on that. However, it is a very important matter.

**Valery Nesterov, senior oil and gas analyst, Troika Dialog Investment Company:** Cooperation with OPEC countries indeed has a long and rather sad history. Sometimes it is even suggested that it is a kind of theater where there is plenty of hypocrisy and insincerity and that there is little use from this cooperation the basis for which is indeed very limited. Cooperation only becomes relevant when oil prices plummet and all producers start thinking about what to do. When prices rise, everyone calms down and forgets about cooperation. OPEC cooperates successfully with the EU, the International Energy Agency and other organizations. We have extensive experience in general communication. The problem is, in particular, that our structures are bureaucratic and clumsy. Here is a simple example. Troika Dialog holds large-scale international forums every year with about 1,500 participants from dozens of countries – prominent economists. The most difficult thing is to get a Russian representative to attend. Within six months, representatives from New Zealand or Caledonia will have replied whether they will come or not. But it is impossible to get any reaction from Gazprom or Transneft.

Western experts take an active part in discussions but it is very difficult to get Russian experts to participate. Our mentality needs to be altered toward greater openness. We need closer cooperation with Europe. The negative attitude toward OECD and IEA membership is not entirely understandable. As market analysts we believe that such partnership – IEA membership – is very useful. For example, our company closely cooperates at the level of oil and gas analysts because we help them understand and write about Russia. They also help us, providing information on world markets, methodologies, etc. We meet when they come to Moscow. Thus, a recent forum was addressed by IEA chief economist Fatih Birol and BP chief economist Christof Ruehl.

Now about forecasts. We have great respect for all forecasts, and study both our Russian forecasts, although they are often subjected to fair criticism, especially on gas, and foreign forecasts – by the U.S. Department of Energy Department, the IEA, etc. We, and the market, do not trust forecasts very much. Here is a recent BP forecast. It suggests that demand in China will be high during this decade and that the share of oil in the energy balance will be falling but the volume of oil consumption



will grow. All of that is very interesting, and the electric car part is also very interesting, but the situation may change. We may be too assertive, for example, in our first assessments of shale gas. One should be also very careful about the assessments claiming that oil consumption will be higher than now. Even if the growth rate is 1%, it is still growth. There will also be regional shifts in consumption patterns. But the most important thing – and there is no doubt about that – is that oil is becoming more costly and difficult to produce. There will be demand for oil in the future and this oil will be produced by OPEC. At present, this is 40% and according to trustworthy forecasts (because they have plenty of resources but we have little and Norway has little), it will be 46%, 50% and more. So we should as a minimum talk to them (it is another matter if they do not want to), continuously maintaining contacts on the working level. And there will definitely be points of overlapping interests. Russia's cooperation with OPEC is very important. Russia must not lag behind other countries and other organizations.

**A. Gorban':** As for our cooperation with the IEA, we do cooperate. The question of whether we join it or not is not directly linked to cooperation with them. IEA officials visit Moscow and our officials meet with them; there are constant contacts via the Foreign Ministry. As for cooperation in general, in my opinion, any interaction is good even if it does not produce the results we expect. At least we can understand clearly what to expect from a particular organization or partner. It is an experience, which is always precious.

**Mikhail Krutikhin, senior analyst, RusEnergy Agency; Editor-in-Chief, The Russian Energy Weekly:** It would be not a bad idea to understand how OPEC sees the situation from its own perspective.

If I go to one of my clients (and we advise foreign companies, embassies, auditors, banks, etc.) and tell him that we build our recommendations on the basis of an economic strategy, say, through 2020, it is unlikely that they will continue working with me; no one takes these strategies into account because they are simply not justified.

To cooperate with businesses and OPEC countries, it is important to understand how they see their partners. In other words, who makes decisions and what these people are guided by when they do. What OPEC can see right now is that Russian oil production (according to that strategy) will rise to 535 million tons a year. According to other forecasts, it will



stagnate. There are only a few projects that in some way or other ensure aim for this production level. And then we remember that the average size of newly discovered oil fields between 2004 and 2009 was 2 million tons per field. In other words, these are small fields that large companies are not interested in developing. If we talk about huge deposits, for example, in the Kara Sea, it should be borne in mind that this oil will be worth its weight in gold and that no one will get that oil for ten years if it is there in the first place. In assessing Russia's role from the OPEC perspective, it needs to be remembered that Russia's market role will not increase and there are also other uncertainties. How will Russian oil be exported and in what direction? To Asia or to Europe? What we are seeing at present is that Western Siberian oil, which should be going to Europe, is in fact increasingly moving in the direction of Kozmino, Skovorodino, Datsin, etc., i.e., to Asia. How can any forecasts be made in relations with Russia when, for example, it is suggested that export projects, such as Druzhba, should be scrapped? That idea met with strong opposition from the Foreign Ministry, and the decision was made to close only the western branch of Druzhba. So from OPEC's perspective, it is not always very easy to predict how Russia will behave as an oil exporter.

Then it is important to consider the big difference that exists between OPEC members and Russia, given that there are mainly national oil companies there pursuing national interests. As for Russia, the interests pursued by our oil exporters are mainly selfish, to put it mildly – not national. At one point Russia reduced oil production at OPEC's request. But I would like to remind you that supply fell within a space of just a few days and then it was offset by a production increase: It was raised by precisely the same amount it had fallen. How can OPEC – from its own perspective – do business with us? It is true that oil companies do not send their representatives to OPEC seminars, symposiums and sessions because indeed they are not interested in that.

There are different ideologies, completely different systems of assessing the production and export potential. So it is wonderful if we develop such forms of cooperation as seminars and symposiums but I do not think that we will be able to ensure any coordination with OPEC.

**V. Bushuyev:** If we were of no interest to Western or Eastern countries, no one would be coming to us. But they keep coming, taking interest, asking around, and offering cooperation. This shows that we are useful and relevant to the international community. In particular, OPEC representa-

tives attend all conferences and forums – the Russian Fuel and Energy Complex in the 21st Century, the International Energy Week, and so on – furthermore, at the highest possible level, and they not only listen to but also discuss these problems. It is another matter whether Russia will be able to influence these processes. I agree that Russia will not be in a position to exert any significant influence on oil supplies because its share is not very large. But it is important to understand something else, namely that financial processes cannot influence the Russian fuel and energy sector either. In addition, no outside macroeconomic factors, especially political factors can affect supplies. This, however, does not mean that we can not influence some processes one way or another. I think that pessimism is hardly justified here.

**M. Krutikhin:** As recent experience shows, big foreign investors are not moving into the Russian oil and gas industry, limiting themselves to simply monitoring the situation. Several periods have passed since I started providing consultations to these investors in 1993. The first was a period of euphoria, when we were helping them establish joint ventures.

Then came a period where we were only advising foreign investors on one subject – how to get out of Russia and keep their pants on.

Finally came a period of situation monitoring because what was happening was completely illogical, inexplicable from the point of view of economics and common sense. So everything had to be explained.

At present a new period is emerging where some companies find niches and start working. But large companies are pulling out. British Petroleum is being cited as an example, but it is an exception. The company got stuck in Russia and became exposed to pressure, falling into the trap of its own strategy. Foreign companies are not interested to operate in Russia because of the bad investment climate.

**Yuri Shcherbanin, Department Head at the Diplomatic Academy:** I would like to note that we in Russia tend to be somewhat skeptical, distrustful of much of the news coming from abroad. The same could happen with electric cars. Last year there was a good deal of reporting about the development of this sector and the building of electric car making plants. The German transport minister said their commercial production would start in 2012 and that currently infrastructure was being put into place. I'm not saying that in two to three years the entire world will embrace electric cars. But if some technological breakthrough does take

place, as a result of which fuel consumption in the transport sector will start falling due to transition to electricity, what shall we do with oil and oil derivatives then? How should Russia's oil strategy be formulated?

Going back to the subject of OPEC, I would like to say that the famous saying from the Russian movie *White Sun of the Desert* – “the East is a subtle business” – has failed to get home on the conceptual or practical level. Since 1998, when the first meeting was organized between R. Lukman and B. Nemtsov, relations with the OPEC countries and OPEC per se have been plagued by negligence. However, people from the East remember everything. There is another problem. There is talk about a draft agreement between the Energy Ministry and OPEC. All oil exporting nations have one ministry and one company. But we have one ministry and a dozen companies. We are being asked how all of that can be coordinated. What can the Energy Ministry realistically do?

It seems to me that the question about Russia's accession to OPEC is as rhetorical as the question about Russia's admission to the European Union or NATO. After all, everyone understands: Supposing Russia joins OPEC, but what if they decide tomorrow to limit production and oil producers say, “What? Are you nuts?” VTS 1 project costs need to be recouped and VTS 2 costs also need to be recouped. What are we supposed to reduce? The Primorsk port alone costs \$85 million a year. The St. Petersburg port is stepping up export volumes. So there is no question of OPEC membership – I don't think that this is serious enough.

The situation with Kazakhstan and Azerbaijan is similar. Kazakhstan has announced that it aims to produce 100 million tons a year (15 million for domestic consumption and 85 million for export). Because in the next 10-15 years they want to make money from oil and turn the country into another Kuwait. They do not need OPEC. Everything there is geared toward export. And you can not join OPEC: Tomorrow they will tell you to cut production from 100 million to 20 million. The same goes for Azerbaijan.

***Sergei Vasiliev, Deputy Director, International Institute of Energy Policy and Diplomacy, Moscow State Institute (University) of International Relations (MGIMO), Ministry of Foreign Affairs of the Russian Federation:*** We are interested in OPEC and even have to cooperate with it, in part because the joint international programs that we are implementing within the framework of the Bologna Process both in economics and management together with different universities require close

links with organizations, in particular OPEC, that influence the international energy market situation. The International Institute of Energy Policy and Diplomacy can be an arena, a platform where such non-political cooperation can develop. This includes personnel training for international cooperation on the analytical level, sharing of experience, exchange of expertise, exchange of research results, and seminars. Our graduates are interesting to OPEC as future professionals in the field. We are in constant contact with them, and our cooperation is developing. A few days ago we received the latest message of greetings from the secretary general.

**Sergei Serebryakov, Director, Center for Global Energy Studies:** A good deal has been said about the need to cooperate with OPEC in some form or other. It seems to me that one such form of cooperation could be a program or some joint research projects in conjunction with the Academy of Sciences. The Academy of Sciences has such programs with leading oil companies such as Shell, as well as with some others. The process started at the Moscow State Institute of International Relations could be continued, but with a greater emphasis on research. There are a large number of institutes affiliated with the Academy of Sciences that deal more with oil and gas. In addition, there is an institute of economics and an institute that deals with political issues and cooperation so some joint projects could be organized with them. Don't forget also that there is the Gubkin Russian State University of Oil and Gas that recently acquired the status of a National Research University. It seems to me that it could also be used as an additional platform for MA and other training programs and joint projects.

**A. Oganesyan:** Are OPEC member countries interested in joint programs with Russian research centers and universities?

**S. Serebryakov:** It seems to me that they are. The way they look at this is that being in Russia makes it possible to get more objective information, get more data to work on later.

**S. Zhiznin:** OPEC had an idea of establishing an OPEC University that would be financed via a separate foundation. But they have yet to agree on the location. Saudi Arabia is showing the most interest. It will probably be based there.

**Yu. Shcherbanin:** About personnel training. I believe that this issue calls for a differentiated approach. There are OPEC countries that are not interested in training programs in Russia – these are some Mashriq countries. And there are countries that send their students here anyway – to Tyumen, Ufa, etc.

**Aleksei Gromov, Deputy General Director, Energy Strategy Institute:** How should we position ourselves in the oil sector? The most advantageous position for us is cooperation with all relevant organizations on an “equidistant” basis. Today, I think, Russia is playing somebody else’s games. For example, energy saving is not our game; the quotas related to hydrocarbons production that are constantly talked about at the international level are not our political idea, not our political game either. Until we have formulated our policy line on the international arena we need to pursue an extremely cautious, “equidistant” policy of interaction with such influential energy players, the energy agency, OPEC, and others.

**A. Oganesyan:** It seems to me that we have not identified very many opportunities for cooperation, but some have been outlined. I would like to make a few comments on another matter. Our approach to energy resources tends to be marked by an element of linearity; we are aware of falling demand – that is indeed the case. But oil and the oil business are so powerful that they can easily provoke an abrupt change in the present situation. The oil and gas sector can become an engine for entirely new branches and innovative discoveries. However, oil, its price, the scientific potential, the pressure exerted on this industry, and life itself will compel a search for methods of survival. It is in the interests of both Russia and OPEC countries for big oil to survive, not to fall, so that demand for it will not decline. In this respect we have a powerful base for cooperation.

Everyone has been stunned by the discovery of graphene, which has made it possible to convert the computer into paper, fold it and put it into a pocket. Who could have predicted that the discovery of graphene would bring such results, but today this is the reality not only of fundamental science but also of practice. Something like this can bring about a revolution in industry as a whole, including the oil industry. This is also where we need to cooperate.

*Key words:* OPEC, energy resources, hydrocarbons, Russia-OPEC cooperation memorandum