

Seeking a fairer deal

INTERVIEW WITH ALEXANDER MEDVEDEV

DEPUTY CHAIRMAN OF THE MANAGEMENT COMMITTEE, GAZPROM AND GENERAL DIRECTOR, GAZEXPORT



ALEXANDER MEDVEDEV graduated from the Moscow Institute of Physics and Technology and holds a PhD in Economics from the USSR Academy of Sciences. From 1989-91, he was Director of Donau Bank in Vienna and subsequently Director of IMAG until 1996. He joined OAO Eastern Oil Company as Vice-President in 1997 and served as Director from 1998-2002, at which time he joined Gazprom, taking up his present appointment.

Gazprom's market capitalisation recently surpassed that of Royal Dutch Shell. How significant is this in terms of the ongoing reform and internationalisation of the company?

I believe that the recent increase in the market capitalisation of Gazprom is not simply a one-off event, but rather a reflection of our long-term commitment to create a more efficient and transparent corporation. This process is an essential part of our strategy to become a world-leading energy company, although clearly it won't happen overnight.

Recent events, such as the removal of the so-called "ring fence" (which formerly limited foreign ownership of Gazprom shares) and the announcement of our ADR listing in New York have obviously been well received by the market. I think it is also a reflection of the fact that more and more long-term investors are looking to acquire and hold Gazprom stock.

We are not content to be members of the US\$200 billion market cap club; our goal is to become a US\$300 billion market cap company. We know that this will take time – probably between three and five years – but we know what needs to be done and this naturally includes improving relations with investors. I am convinced that Gazprom has the potential to grow in all major economic parameters, including market capitalisation.

Where do you see the company relative to the likes of BP and ExxonMobil in the longer term?

If you look at our reserve base, it is quite clear that we could overtake both these companies if we improve certain parameters like productivity and efficiency, particularly in terms of our production. We have a long-term view of how to achieve this and it is no joke to say that Gazprom could achieve greater market capitalisation than both the companies you mentioned in the foreseeable future.

At the moment, our share price to reserve ratio is around eight or nine times less than that of BP, due to the market's perception of the overall Russian risk as well as its perception of Gazprom risk. But in the last three or four years we have shown our commitment to transform the company into a corporation in which the interests of the State and the interests of our shareholders are combined, irrespective of the type of shares they hold.

What makes a successful public-private company? Did you have a particular model in mind when you set out to reinvent Gazprom in this way?

It's a question of management. The Executive Board and the Board of Directors – which is responsible for the strategic direction of the company – communicate very effectively with each other, but that doesn't mean that we have the same opinions on every subject. Take the issue of local gas price increases, for example; there are different opinions in the government about this and different opinions among the board of directors, but we both agree that the increase in local prices is good not only for Gazprom but also for the Russian economy, for structural reform and for the development of energy saving technologies. We will consistently defend the necessity to increase the local price of gas for industrial and commercial customers, especially for the power sector.

One of the principal topics for discussion at the G8 summit will be the issue of energy security. How do you see Gazprom's contribution to this subject?

Gas is playing an increasingly important role in the overall energy balance in Europe, as it is in other parts of the world, and it is no exaggeration to say that Gazprom is a guarantor of energy security in the gas sector. Why? Because we invest a huge amount of money in developing and supporting our transportation system and our reserve base, in order to meet the growing demand from Europe.

On the one hand we have a very solid portfolio of long-term supply contracts, while on the other we are actively involved in the new forms of trade in the liberalising markets in Europe, such as the United Kingdom. In fact, we recently delivered our first cargo of LNG to the UK, so we are well equipped to operate in accordance with the realities of the market.

Gazprom was a pioneer in the process of European gas market liberalisation through the creation of Wingas, our joint venture with Wintershall. Having bought gas from us on long-term contracts, around 50 per cent of Wingas' contracts now have a maturity of one year, so the company has fully adapted to the new situation.

As well as diversifying geographically into markets such as the US, Canada, China and Korea, we are also diversifying our product range. Besides LNG, we are moving into oil and oil products and, following the

acquisition of Sibneft, we are now a serious player in the oil business – and we intend to continue our expansion in this field. We are also a leader in petrochemicals, following the re-organisation of SIBUR (now 75 per cent controlled by Gazprombank), and this business is an important part of our vertical integration concept.

Last but not least, we are looking to expand our activities in the power sector, in order to maximise the synergies between gas and electricity. We have a very clear vision of how we intend to develop our business in the next twenty to twenty-five years, and one of our main priorities is to go further downstream – both to defend our commercial interests and to provide the necessary level of comfort to our customers.

Some European countries may be uncomfortable with the increasing market dominance of Gazprom, particularly following the Ukraine dispute earlier this year. What is your response to such concerns?

Energy security is a two-sided issue; it's not simply a question of reliability and security of supply, but also one of security of demand. If you look at the current structure of the market, it is clear that Gazprom is operating in a highly competitive environment. Russian gas competes with Norwegian, Algerian and Libyan gas, and we are facing some discrimination in our attempts to be a player in the market. That is why I find it intolerable when liberalisation is presented as a one-way street.

The interests of producers should be carefully analysed and incorporated into the construction of the new European energy policy. The current Green Paper looks very one-sided, because the interests of producers are not taken into account properly and the responsibilities of the transit countries are not fully presented. This is why dialogue is so important. The actions which we took in respect of Ukraine last December and January were not intended to put the security of Europe's supply at risk but to cement it, so that we will not face the risk in future.

How do you see the future of Gazprom's downstream business? Will this grow organically or by acquisition? If the latter, how do you respond to the current wave of European nationalism and do you expect the UK to keep to its liberal principles in this area if you decide to bid for Centrica?

I cannot give any concrete names of acquisition targets but we monitor all the available options and will choose between internal development via our wholly owned subsidiaries, or jvs, or via acquisition. It is clear that there are potential synergies for European players, who are short of energy, to partner with Gazprom.

The entire gas business is based on partnership and moreover, decisions taken today could have an impact

over twenty or twenty-five years, which is why we are very careful in our investment decisions and in our selection of partners.

Demand for gas is growing and the favourable environmental impact of natural gas is assuming greater importance. If Europe is serious about its environmental obligations, then there is no alternative to gas; despite the advances in clean coal technology and renewed interest in nuclear, fossil fuels will prevail for at least the next two decades.

On the subject of Centrica, we enjoy a very constructive dialogue with the UK takeover panel. I do not believe that we will face any discrimination based on so-called political arguments.

How do you see the role of foreign oil and gas players developing in Russia, and what criteria do you apply in choosing foreign partners?

We operate a very transparent approach in this respect: we are ready to invite foreign partners to participate in upstream projects in Russia in exchange for the equivalent value in assets which are strategically important for us. This approach works well and we are applying it in the case of the Shtokman project. In the case of the Yuzhno-Russkoye gas field project, we are finalising asset-swap arrangements with our German partners and our Sakhalin II project with Shell is another good example.

Russian reserves are obviously interesting for our Western partners because there is a lack of good reserves worldwide and the probability of major new discoveries is very low, while Russia's reserves are big enough to meet the demand of Europe, America and Asia. In exchange, we would like to have access to downstream, and to upstream reserves outside Russia, because we want to have a diversified portfolio of assets and to be involved in all parts of the value chain. And it will be good not only for us but also for our customers.

Where do the energy-hungry economies of China and India figure in your plans?

We know the scale of the potential demand in China and once our current commercial negotiations are completed we will have a clearer idea of the precise demand. I hope that these will be concluded this year and that we will be able to begin supply on schedule.

In respect of co-operation with Chinese and Indian companies, we have framework agreements with CNPC and ONGC, and we have an offshore project in India with GAIL. We understand that the current situation requires comprehensive cooperation, which is why the Russian market is open not only to Western companies but also to Chinese, Japanese and others. **F**

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