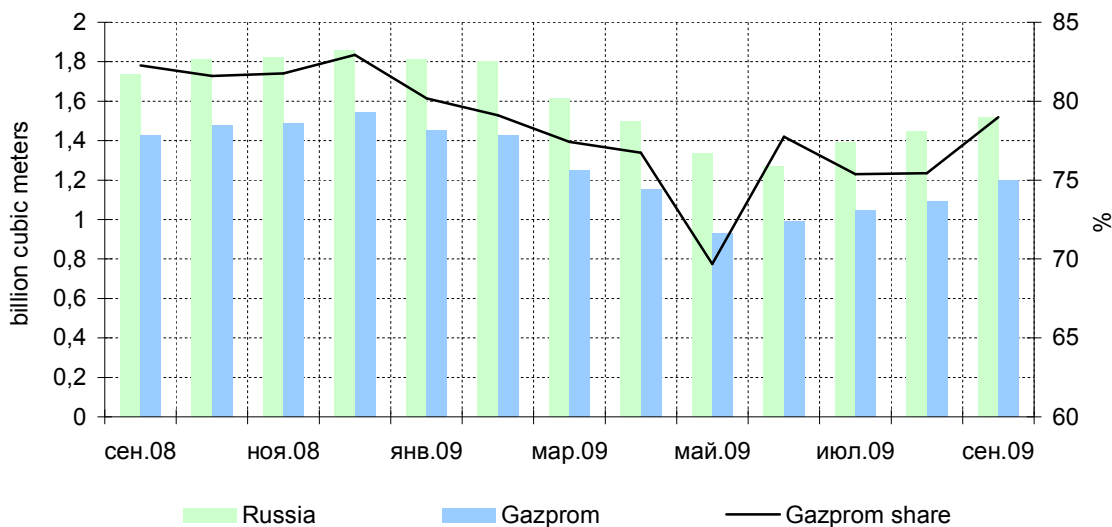


GAS PRODUCTION ON THE RISE, RISKS REMAIN HIGH

BY KIRILL LEBEDEV, IFS SENIOR ANALYST, 5 NOVEMBER 2009

The global economy plunged in the face of the crisis, and one of the consequences has been a decline in primary energy consumption. Falling gas demand has had a strong implication on Russian producers. Daily gas extraction slumped more than 38% in Russia and 55% within the Gazprom group between January and May 2009.

Daily gas production



Source: Central Control Agency of the Power Sector

Last May Gazprom gas production fell to a several years' low – 70% (versus usual 82 to 86%) of Russia's total gas extraction. After the cold weather set in and gas demand started to rise, Gazprom immediately addressed the increased need and produced 43.5 billion cubic meters of gas in October (against September's 36.2 billion cubic meters). However, the 2008-2009 gas extraction indicates that the monopoly has not been on a wave of huge success and the industry might face other risks by the end of the year. October's robust production growth (almost 21%) followed a marked decline, i.e. it is owed to a low base effect. Gas production fell 1.5% between October 2009 and October 2008.

When outlining the industry prospects, we should take into account possible feedstock insufficiency.

The monopoly's reserves of Cenomanian deposits are being depleted, while import of Turkmen gas has been halted following the Central Asia–Center pipeline breakdown.



Nevertheless, Gazprom should be ready to meet domestic and foreign consumers' needs, as demand for gas will certainly grow in winter.

Pricing terms will be a stumble block in negotiating gas supplies from Turkmenistan that wants a decent price for its products. Turkmen gas is pumped to Ukraine, and we all remember the nonpayment scandal the risk of occurrence of which heightens as the gas price rises.

The beginning of 2010 might be marked with a new energy crisis that will affect Gazprom's foreign currency revenues and Russia's status as a reliable gas supplier to European states. European consumers might be left without energy as it happened last winter.