

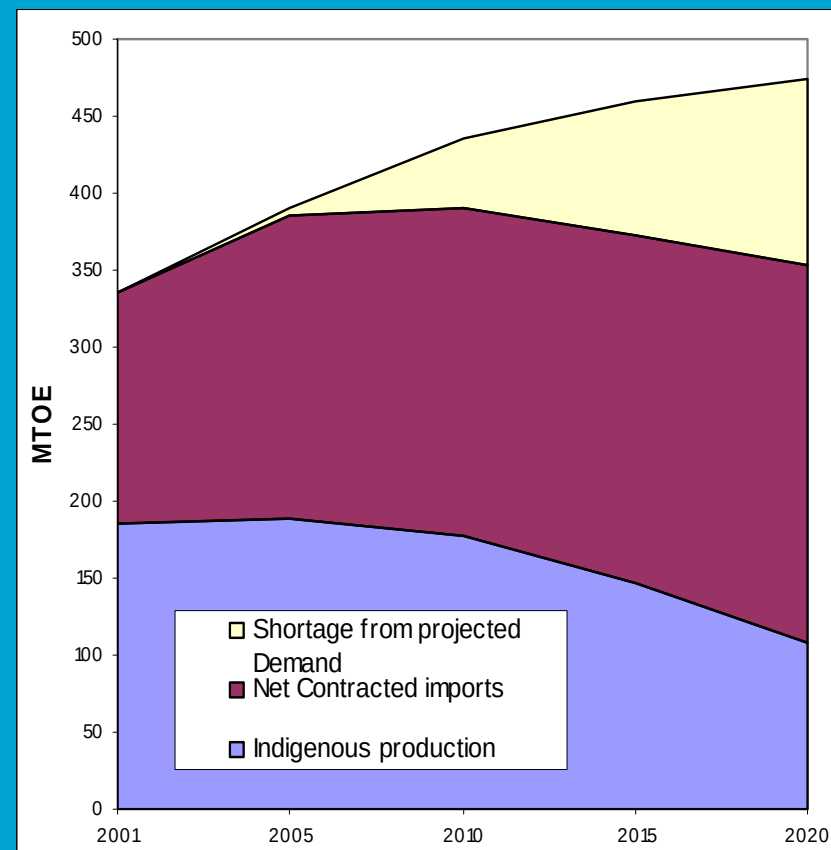
Gas Transit Risks in Eurasia and their Impacts on Transit Infrastructure Development

*Paul Shapiro, Senior Banker, EBRD Natural Resources Team
19-20 October 2004 • Brussels, Belgium*



The European gas imbalance

- Shortage 100bcma within next 7 years
 - current import + 1/3
 - 50% already under contract => to be met
 - 50 bcma new volumes => to be contracted



Source: Eurogas



Challenges for increased FSU exports to Western Europe

- Meeting these increased gas flows to Europe is a challenge:
 - New field development in remote areas
 - Refurbishment of existing gas transportation systems
 - Construction of new gas transmission infrastructure
 - Securing adequate contractual arrangements
 - Management of political issues at both ends

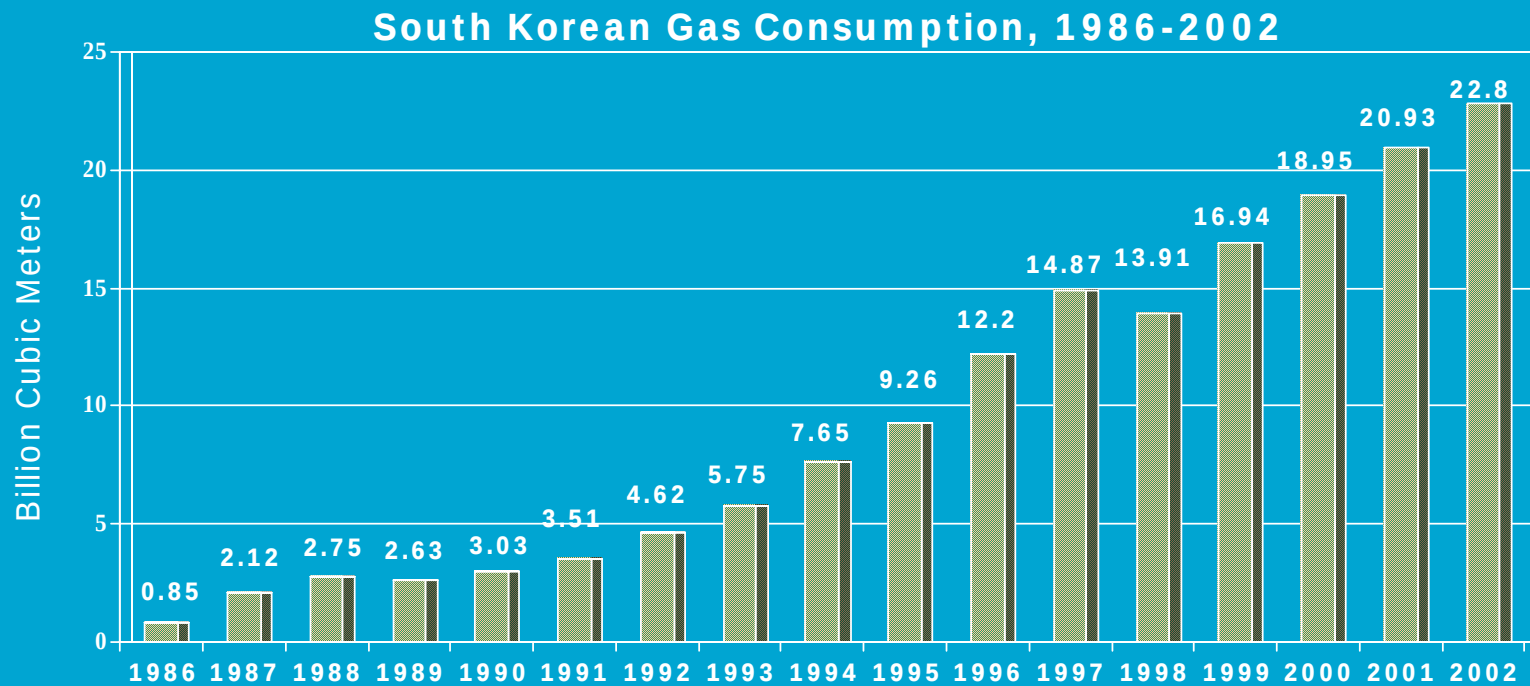


Key projects for the future: Midstream

- Ukrainian gas transit system upgrade: \$1bn?
 - International consortium
 - Political hurdles
- TransBaltic gas pipeline: \$6bn?
 - Financing of Russian stake
 - With or without Shtokman?
- Yamal-Europe II: \$2bn?



Strong Asian Gas Demand Growth



Siberia-Asia Gas Pipeline Proposals

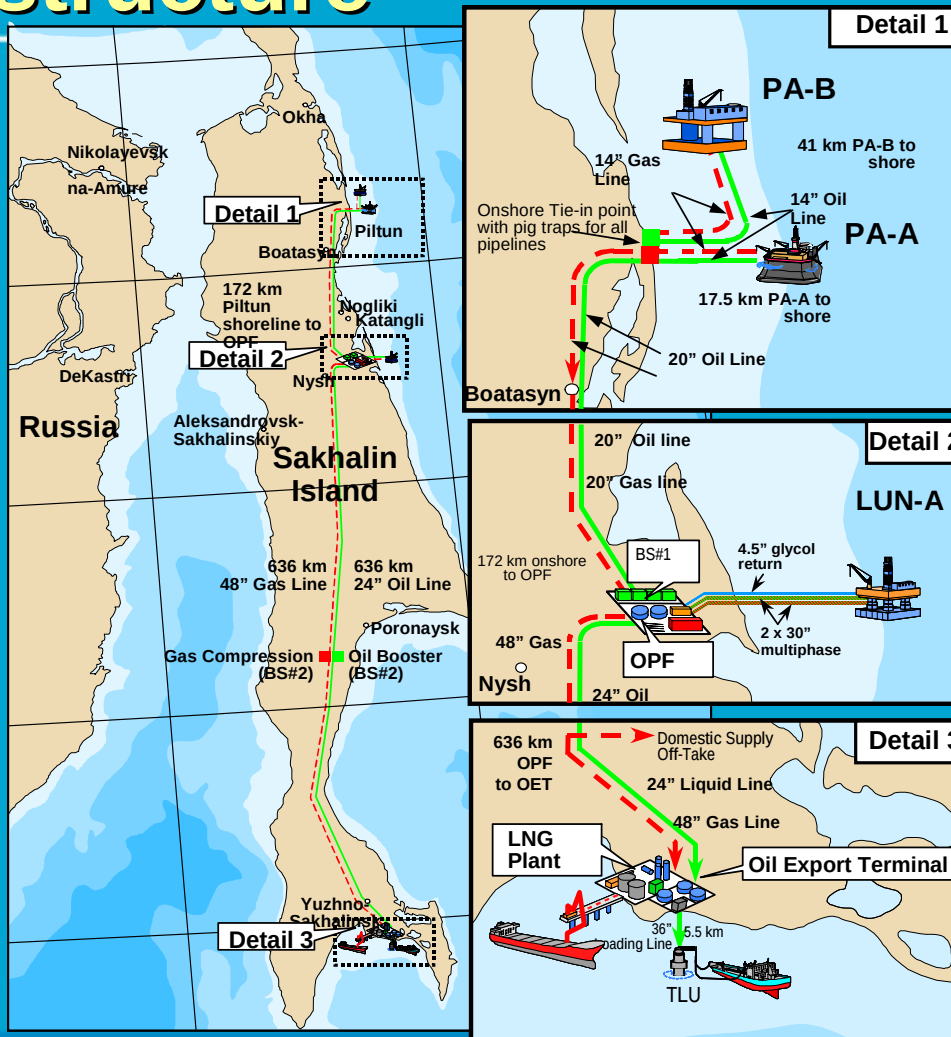


Current and Proposed Asian Pipelines



Sakhalin II Phase 2 - Key Project infrastructure

Oil & Gas pipelines stretching the length of the island



Additional offshore platform

Development of Lunskeye gas field through offshore platform

Construction of LNG plant and oil export terminal



General Perspective

- Huge investment need by 2010
 - At least \$10bn upstream + \$10bn midstream
- Very high investment concentration
 - \$1bn entry ticket minimum
- Substantial legal challenges
 - Legal framework in FSU / Offtake arrangement in EU
- Many sector reforms necessary
- Large political hurdles Regional cooperation
- Huge competition from the East
- Generic project finance challenges



Regional and Sector Reform Issues

- Technical Issues
- Unbundling of Activities and Services
- Rationalise Tariffs, Transit Fees and Taxes
- Enforce Payment Discipline
- Regulatory Framework
- Attracting Strategic Investors and Privatisation
- Political Issues
- Civil and Social Progress
- Environmental Issues



Technical Issues

- Routing of infrastructure to Soviet production
- General deficiency of internal and transit pipes for current export demand
- Antiquated pumps and metering
- Lack of batching and separation facilities
- Deficient local parts and service industry
- Current expense of “clean” technology



Un-bundling

- Gas trading, transit and bulk sales
- Long distance gas transport – high pressure network
- Local gas distribution
- Gas Storage
- Unbundling removes distorting cross-subsidies and promotes commercialisation



Rationalise Tariffs, Transit Fees and Taxes

- Full cost recapture tariffs with incentive for maintenance and investment
- Geographic price differentiation for transit cost
- Full deduction for tax purposes of necessary depreciation



Payment Discipline

- Comprehensive gas metering
- Progressive restriction of supply for late or non-payment
- Forgiveness, conversion or other renegotiation of arrears
- Build sinking fund for arrears from profit



Regulatory Framework

- Service Obligations
- Conditions of third party access
- Monitoring of gas trading
- Bulk and end user tariff setting and monitoring mechanisms
- Independent regulatory body



Political Issues

- Patronage and Funding
- Affordability, Subsidies and Welfare
- International Competition

Economic, Military and Ideological

Offensive and Defensive

- Governance and Efficiency



Environmental Issues

- Legacy of Environmental Damage
- Demands for impact minimization
- Differentiation of social impacts
- Agitation for “Renewables”



Civil and Social Issues

- Routing
- Human Rights
- Consultation process and compensation
- Shift in focus from purely environmental aspects of large oil and gas projects to more 'political' topics like
 - Revenue management
 - Transparency
 - Corruption
 - Democracy



Safe, Fair and Sustainable

- Environmental and health and safety aspects
- Fairness and transparency for all parties involved
 - Tariff payments to Governments
 - Consultation
 - Land compensation
 - Publish what you pay / receive
 - Disclosure of key agreements
- Benefits for the local population
 - Community investment programmes
 - Transparent revenue allocation
 - Regional development initiative



Generic Risks

- Construction / Completion Risk
 - contractual structure (delays, cost over-runs, etc.)
- Operational Risk
 - technological integration and experience / viability
- Utilisation / Supply Risk
 - type of throughput arrangement
 - fundamentals (Market/Competition)



Generic Risks cont.

- Competition / Market
 - effect of oil price (linked to gas and oil products)
 - regional supply / demand
 - impact on tariff
- Political & Regulatory Risks
 - regulatory intervention (tariffs & export volumes)
 - political turmoil / disputes / violence / nationalisation
 - discriminatory taxation



Risks and their mitigation

- Economic & financial
 - minimised through financial package and due diligence
- Technical risks
 - reliance on strong and technically competent sponsor
- Environmental risks
 - sponsor commitment to appropriate guidelines
- Political risks
 - minimised through involvement of IFI's and ECA's



Lessons Learned

Chernogorskoye, Komiarcticoil, Polar Lights, Samotlor, West Siberia II Oil, Chernogorneft, Geoilbent, Gas Transit and Gas Transit II, SeverTEK

- engagement of independent technical adviser to review condition of the borrower's assets
- advance structuring of reporting for the Bank's monitoring purposes
- conducting sensitivity analysis on the basis of conservative assumptions
- ability of a relatively small project to create a transition impact



HOW EBRD CAN ASSIST



Available Financing Sources

- **Equity**

- Strategic investors (oil and gas majors)
- Investment funds (limited scope)
- IFI's (EBRD, IFC)

- **Debt Financing**

- IFI's (EBRD, IFC) (own funds)
- EIB (European portion)
- Commercial banks (participating in IFI B Loans)
- ECAs (Hermes, Coface, JBIC, Exim...)

- **Capital Markets**

- Equity (IPO's)
- Bonds



Debt as Financing Source

- Loans
 - Tailor made instruments with negotiated conditions
 - Bank lenders familiar with different structures
- Bonds
 - Relatively rapid issuance process
 - No covenants for straight instruments
 - Tradable instruments
 - But lack of flexibility



Pure Project Finance is no longer an option

- Lenders and Sponsors will have to structure projects that go beyond funding project cost Sustainability + Good Governance are high on the agenda
 - International Financial Institutions (Extractive Industry Review)
 - Commercial Banks (Equator Principles)
 - Socially Responsible Investors
 - NGOs and civil society
 - Governments (EITI)



EBRD NGO involvement

- Committed to dialogue with NGOs from an early stage
- Addressing NGO issues with Sponsors
- Acting as “catalyst” to facilitate dialogue between Governments, independent experts and Sponsors
- **Multi-Stakeholder-Forums** seeking dialogue with directly affected people to verify ‘mood on the ground’
- Continue dialogue with NGOs during project implementation

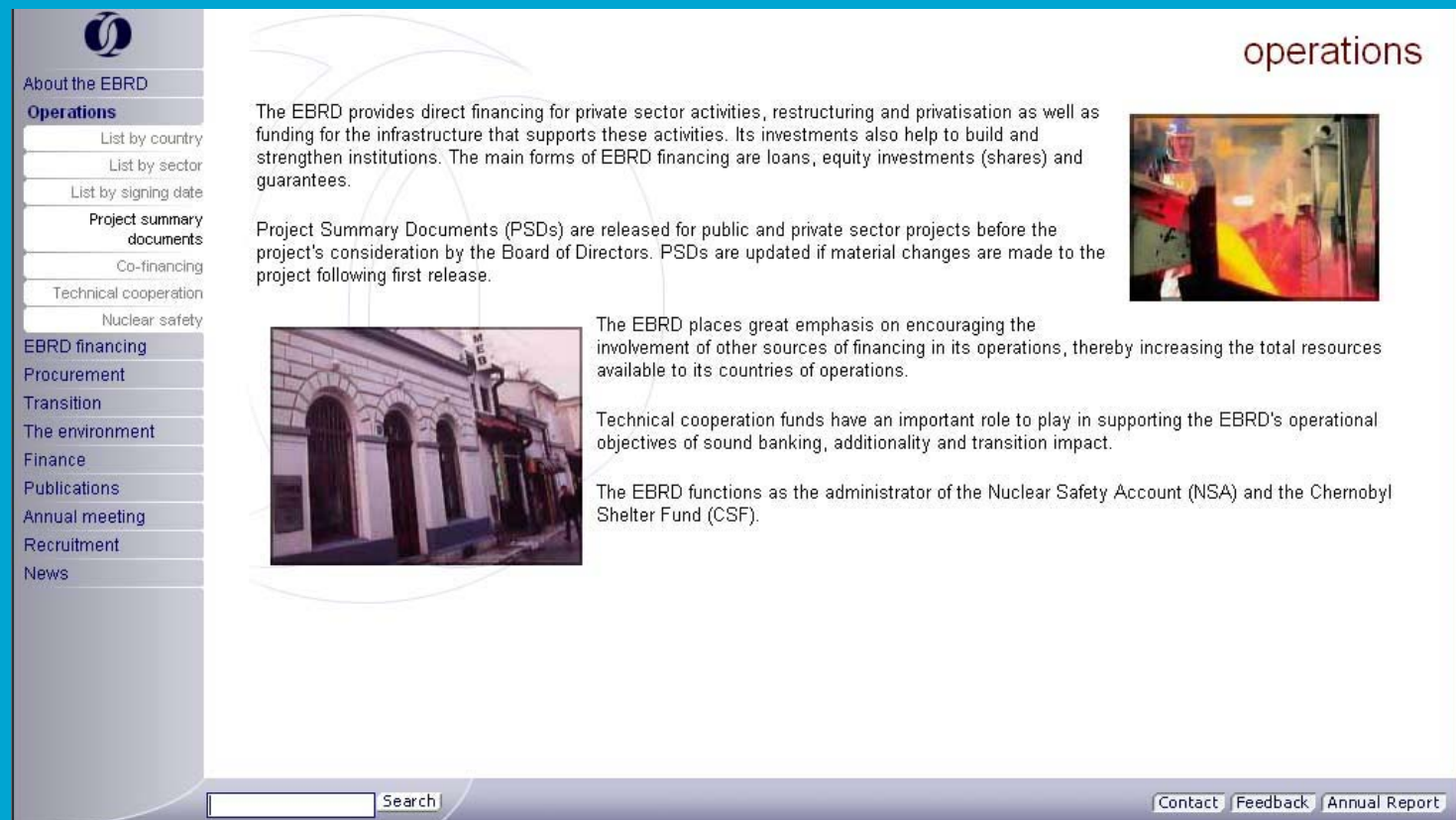


Contact Details

Paul Shapiro
Senior Banker
Natural Resources Team
European Bank for Reconstruction and
Development
1 Exchange Sq.
London, EC2A 2JN
Tel. 44 (0) 207 338 6244
Fax 44 (0) 207 338 6101
Mob. 44 (0) 7764 230 775



More information: www.ebrd.com



The screenshot displays the EBRD website's 'operations' section. On the left is a vertical navigation menu with the EBRD logo at the top, followed by 'About the EBRD', 'Operations' (highlighted), and a list of sub-topics: 'List by country', 'List by sector', 'List by signing date', 'Project summary documents', 'Co-financing', 'Technical cooperation', 'Nuclear safety', 'EBRD financing', 'Procurement', 'Transition', 'The environment', 'Finance', 'Publications', 'Annual meeting', 'Recruitment', and 'News'. The main content area is titled 'operations' and contains three text blocks. The first block describes the EBRD's role in providing direct financing for private sector activities, restructuring, and privatisation, as well as funding for infrastructure. The second block explains that Project Summary Documents (PSDs) are released for public and private sector projects before Board of Directors consideration and are updated if material changes occur. The third block states that the EBRD encourages the involvement of other financing sources to increase total resources. To the right of the first text block is an image of a person in a red protective suit. Below the second text block is an image of a classical building facade. To the right of the third text block is an image of a person in a white protective suit. At the bottom of the main content area is a search bar with the word 'Search' and three links: 'Contact', 'Feedback', and 'Annual Report'.

operations

The EBRD provides direct financing for private sector activities, restructuring and privatisation as well as funding for the infrastructure that supports these activities. Its investments also help to build and strengthen institutions. The main forms of EBRD financing are loans, equity investments (shares) and guarantees.

Project Summary Documents (PSDs) are released for public and private sector projects before the project's consideration by the Board of Directors. PSDs are updated if material changes are made to the project following first release.

The EBRD places great emphasis on encouraging the involvement of other sources of financing in its operations, thereby increasing the total resources available to its countries of operations.

Technical cooperation funds have an important role to play in supporting the EBRD's operational objectives of sound banking, additionality and transition impact.

The EBRD functions as the administrator of the Nuclear Safety Account (NSA) and the Chernobyl Shelter Fund (CSF).

Search

Contact Feedback Annual Report



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