

In the Name of God

Iran's Views
on
Energy Transit
Problems and Risks

Madam Secretary General, Mr. Chairman, Distinguished Guests, Ladies and Gentlemen:

I would like to begin by extending my sincere thanks to Dr. Kemper for inviting me to this conference. I hope this conference will succeed in defining the existing challenges of energy transit from the standpoint of energy consumers, suppliers and transit host countries and set the stage for prospective cooperation among all.

In my speech today, I would like to first touch on global oil and gas demand in the coming decades as well as Iran's current position in and future plans for playing a role in the global oil and gas industry. I will then discuss some of the major international challenges facing oil and natural gas transportation after which I will conclude by highlighting the role of the ECT in the quest for a stable energy market.

Figures show that the demand for natural gas has grown much faster than that of other primary energy resources. It is, therefore, expected that the share of natural gas in the primary energy basket will increase. The annual growth rate of world demand for natural gas will average 3.1%. European countries will be more dependent on natural gas in the coming decades. It is projected that by 2030, more than 65% of the natural gas consumed by the EU will be imported because the increase in demand will have greatly exceeded that of production in Europe. An evaluation of the projected natural gas supply and demand for 2020 and 2030 reveal that European countries will have to find new sources of supply to satisfy their additional demand. Russia, currently the main supplier of natural gas to Europe, may not be able to meet the increasing demand by OECD countries since it will have to meet the growing demand for natural gas in FSU countries and domestic markets.

Iran, located in the vicinity of Russia, the CIS and Caucasian countries, as well as on the eastern borders of Europe, has the potential to export

natural gas both to EU markets in the West and emerging markets with huge demand in the East such as Pakistan, India, China, and even Japan.

Iran's unique geo-economic features distinguish it from other gas-rich countries in the region. It is located in southwestern Asia where the world's major oil and gas reserves are concentrated. Iran, the biggest natural gas producer and consumer in the Middle East, with the second largest proven natural gas and oil reserves, is emerging as a major supplier of natural gas to world markets.

We have plans to increase our oil production capacity from the present 4.2 mb/d to around 6 mb/d in 2015 in order to maintain our current share in OPEC's production. We also have plans to increase our gas production capacity from 130 bcm/y to 300 bcm/y in the next 10 years and to 400 bcm/y in the next 20 years. This will position Iran as the second or the third largest natural gas producer in the world.

Most investments in Iran's oil and gas development projects are made through finance and buy-back contracts. We are planning to invest some \$100 billion in oil and gas by the year 2015. During the past 7 years, more than \$46 billion have been invested in this sector, 65% of which have come from foreign investors. Buy-back contracts account for 63% of these investments.

In pursuance of our policy to develop a natural gas downstream sector, studies on two separate GTL projects are in process and four LNG projects namely, Persian LNG, Iran LNG, Pars LNG, and NIOC LNG are in the different phases of FEED design to EPC tendering process. Iran is planning to develop its natural gas pipeline network and extend it to its eastern and western borders and become a center for natural gas transactions. Iran's LNG target markets are China, India, Europe, Japan, and East Asia.

Presently, we are exporting gas to Turkey and very soon we will start exports to Armenia and Nakhjavan and the UAE.

There are some other pipeline projects for exporting Iranian natural gas to our neighbors and beyond to the UAE, Kuwait, Pakistan, India and Europe.

Iran's adjacency to major natural gas producing and consuming countries has brought about several different alternatives as regards to international gas transactions. Unique geopolitics and efficient domestic network of

natural gas transport enable us to play an important role in natural gas transport or swaps in the region. As an example, some of our neighbors in the north receive around 10 bcm /y gas from Gasprom with a long distance delivery. We can deliver this amount of gas to these countries, if Gasprom agrees to deliver the same amount of gas on our behalf to Europe.

Transmission of Caspian sea oil to the Persian Gulf via Iran is another viable project which will enhance regional cooperation and economic prosperity. Regrettably, the interference of outsiders with economically disastrous political agendas, has delayed this project.

We already have a swap agreement with some Caspian states whereby their oil is delivered to Neka on Iran's Caspian coast. The delivery capacity of this arrangement is currently around 120000 b/d which is expected to rise to 350.000 b/d within 10 months. Another project, KTI (Kazakhstan -Turkmenistan- Iran) oil pipeline which will transfer oil from Kazakhstan to Turkmenistan and Iran is currently under study by Total.

Madam Secretary General, Mr. chairman, Ladies and Gentlemen:

I would now like to return to the theme of the conference and elaborate on some of the major problems and risks gas export projects are facing today.

Briefly speaking the major problems and risks for gas export projects are as follows:

- 1- Capital intensiveness of the projects and need for financing.
- 2- Low prices of gas
- 3- The necessity for pre determined customers
- 4- High transport costs
- 5- Crossing several different countries and political risks of each one
- 6- Disputes among transit countries
- 7- The right for transit

Now I will elaborate some of these items.

Capital-intensiveness and high capital risks are two inextricable features of natural gas transit projects. Project financing is, therefore, considered to be a crucial factor in floating such projects. Under current conditions, there is a great deal of competition for attracting investment for costly

energy projects. International financiers and investors consider a wide range of political, legal, geopolitical, and security issues as well as economic viability when deciding whether or not to finance a natural gas export project.

There are an increasing number of natural gas export projects that require large amounts of investment and involve a degree of risk. It would therefore be in the interest of major finance organizations to join with similar organizations in or the governments of producing countries to jointly finance or invest in such projects. It would seem most unlikely for any natural gas export project to be realized unless several international organizations or major oil and gas companies participate in it.

On the issue of gas price I believe that the current high oil prices resulting partly from insufficient supplies should signal a warning to gas consumers, particularly the EU countries. In the past few years low oil prices hampered investment in production projects which resulted in the current undesirable situation. The same scenario can happen to natural gas, given the current low gas sales prices.

Natural gas pricing mechanisms have always been a controversial issue between suppliers and customers. The question of whether the positive externalities of natural gas, especially its environmentally sound nature should be a determining factor in pricing mechanisms, have always been a problematic issue. In general, reaching an agreement over the price is the most important prerequisite of implementing an export project.

Ladies and Gentlemen:

One of the crucial issues regarding natural gas production and export is how to transfer it to the market. Unlike oil, gas storage is also difficult and expensive. With such constraints the duration of gas contracts will have to be sufficiently long to mitigate risks and be economically sound. Transfer of natural gas over long distances usually results in higher transport costs and increases delivery risks. Political risks are among the factors affecting security of supply over long distances especially in projects where natural gas pipelines cross several different countries. Unfortunately, these issues have always had adverse effects on projects related to Middle East natural gas transfer to Europe. Multilateral cooperation and supervision by international organizations are the only ways to alleviate concerns and minimize risks. Therefore, for expediting EU gas supply projects, we suggest European countries form multilateral international bodies like NUBOCO, comprising natural gas producers,

international companies, consumers, transit host countries and relevant international organizations. These bodies could then work on contracts to transfer natural gas to consuming countries. Since the reliance of European countries on oil and gas import is projected to be higher in the future, the matter should be given serious consideration.

As I mentioned dispute among the transit or producer countries is one of the real obstacles. Iran – Pakistan – India gas pipe line project is a good example of it. The Caspian region is another example. Existing hydrocarbon resources in the Caspian region could be of some significance, but due to a number of obstacles, it is unlikely that the region's oil and gas reserves will have considerable impact on global markets, at least for the next decade. Exploitation of Caspian oil and gas reserves has been delayed by both technical and political problems. There is no consensus among the littoral states over an appropriate legal regime for the Caspian Sea. The high sulfur content of the region's oil and gas in addition to the land-locked nature of the Caspian region are also important problems. Iran and Russia are the only Caspian countries that have access to the open seas.

Clearly, cooperation between the countries of the region will be to the benefit of all .

The last issue I would like to touch upon is the transit right. Some transit countries, who do not have any gas, are interested to be a gas trader instead of a gas transiter. This attitude is also an important factor for delaying projects. Transit costs are also considered a main factor in natural gas transit projects. In some cases, the host government unilaterally raises the transit fees, adversely affecting the viability of projects.

Ladies and Gentlemen:

Stability and an absence of frequent political turmoil are deciding factors for countries involved, to secure natural gas contracts. It is notable that investors take into account such factors as the type of government and the stability of a country or the region in their investment decision making process. Although the geopolitical and political situation of the Middle East has, to some extent, driven away potential investors in oil and gas projects, the political stability of Iran, despite the existing regional tensions, justifies more foreign investments in its oil and gas industries.

Mr. Chairman, Dear friends, Ladies and Gentlemen;

In an attempt to alleviate worries over the secure flow of oil and gas to Europe in the post-Soviet era, ECT was formed in the early 1990s to help maintain energy security in Europe. Although ECT, with over 51 member states and observers, has developed into an international organization carrying considerable weight, the results of a decade of long negotiations clearly demonstrate the continued complexity of its mission. This mission covers a wide range of national interests, territorial disputes, complex geopolitics, geostrategy and petropolitics. This is especially so in an era experiencing dramatic challenges and changes effecting and affected by the political economy of energy which in turn is reshaping the geopolitics of Eurasia.

Thus the ECT must play a more active role in focusing on the real challenges facing the energy market and pave the way for further long-term and multilateral cooperation among all players.

Thank you ladies and gentlemen for your patience.