Russia considers oil export options

Shipping crude oil out of Russia to the US is no longer a pipedream. As the shifting sands of geopolitics blow in from the latest Iraq war, how is Russia's export system shaping up

Shipping million of barrels of Urals Blend crude oil to the US has become a reality as Russia fights to keep her taps switched on and politicians charm the sceptics that such trade can pay.

Playing the geopolitical game, Russia's president Vladimir Putin is keen on building a closer partnership with the US and forging economic links through the export of crude.

Although Russian companies do not need the US market - they can sell all the oil they want in neighbouring Europe - closer alliance with the US forms a key part of Putin's foreign policy.

To date, little Russian oil has reached US refineries - in 2001 Russia exported just 89,000 bpd of oil to the US according to the US Energy Information Administration (EIA), and all of this in the form of refined products. But in 2002, after a weak start with no imports in January or February the volume shot up to an April peak of an average 210,000 bpd to 220,000 bpd in October, according to the EIA.

Trans-Atlantic oil trade from Russia to the US is hampered by restrictions on the size of suitable tankers. Passage through the Bosphorus Strait is limited to vessels of 145,000 dwt (1.05m bbl), which makes exports to the US from Russia's Black Sea ports uneconomic for much of the time, says Julian Lee, a senior analyst at the London-based Centre for Global Energy Studies (CGES).

The situation is even worse in the Baltic Sea, where the depth of the Danish Straits linking the Baltic to the North Sea effectively restricts vessel size to 110,000 dwt (800,000 bbl), he adds.

Russian oil majors are very well aware of the physical constraints and are working on several deep-water port projects to ship Russian crude across the Atlantic Ocean at an economic rate. If supertankers could take the oil then the economics would look a lot healthier, says Lee.

Many market analysts in the West believe the recent shipping of Urals Blend crude oil into US refineries has more symbolic value than economic worth.

"Importing Russian oil has great symbolic value to the US," says Theodore Felder, regional manager, CIS for the influential Geneva-based consultancy IHS Energy. "It's an issue for the future. In the short term, shipping large volumes of Russian crude is not going to happen," he says.

But with billions of dollars of investment going into Sakhalin (ExxonMobil, Royal Dutch/Shell) and BP developing a close relationship with Russian oil major TNK and France's TotalFinaElf exploring in the Black Sea, reticence is slowing giving way to acceptance and understanding of the risks or operating in the Russia, says Felder.

Charles Meynell, Russia watcher and editor of Russia Briefing, takes a more sceptical view: "Many of the senior politicians in Washington have little time for Russia. Many are wary of the slow pace of economic reform and are wary of the increasing dependence of the Russian economy on petro-dollars".

US imports, currently standing on 9.1m bpd, with OPEC accounting for 51% of deliveries. Washington has often repeated its wish to reduce dependence on OPEC suppliers, opening the way for alternative producers. "The US sees diversification as a way of reducing risk," says Takayuki Nogami, a senior manage of the oil industry and markets division, International Energy Agency.

Predicted exports of Russian crude to China, which has based its 2001-2006 five year plan on increased energy imports from its westerly neighbour, suggests Chinese prime minister Zhu Rongli, could see the country source up to half its $25bn crude

imports from Russia over the coming 20 years. This route would provide much needed petro-dollars and offer less exposure to volatile marine shipping costs inherent in shipping crude to the US.
A senior group of Russian and US officials met in Houston late 2002 at the ground-breaking Commercial Energy Summit. US energy secretary Spencer Abraham discussed with a number of senior Russian politicians and oilmen including energy minister Igor Yusufov a wide range of subjects as politically sensitive as how to retain lucrative contracts in Iraq in any post-Saddam Hussein world.
But behind the scenes much of the discussion focussed on how Russia could raise oil exports to the US. The US consumes a mind boggling 20m barrels per day of crude oil, and is continually searching for ways to safeguard supply. A key memorandum signed at the meeting recorded the hope that Russia's share in oil supply in the US market will total 13% by 2010.
At the Houston event, Lukoil chairman Vagit Alekperov said that by 2010 Russia could supply at least 10% of the US' daily consumption.
Two years before the Houston gathering, an energy summit between the European Union (EU) and Russia took place at which the EU agreed to help Russia develop its oil and natural gas reserves in return for a long-term energy supply commitment.
Russian producers had become jaded by the continual disputes over payments from former Soviet Union countries and saw the EU as a strong market with money to pay the bills.
Speaking of the US/Russia rapport Laurent Ruseckas, analyst at the Cambridge Energy Research Associates (CERA) in Paris, France says that the "relationship will grow and develop. There is high political interest on both sides."
The move seems to realise not only president Putin's plan for an energy partnership, but Yukos chief Mikhail Khodorkovskii's often stated goal of greater trade with the US.
However, Ruseckas adds that it is misleading to equate too closely the flows out of Russia and into the US refineries. "It's a fungible market, with prices and supply/demand fundamentals dependent upon how much is in the global market".
Russia will never be a swing producer in the mould of Saudi Arabia that can increase production by 2m bpd almost in a very short time scale. But it will increase output steadily and will and if the US is seeking extra supplies it will be able to absorb new volumes of Russian crude supplies.
But it's not that simple just to say that any increase in Russian production will be shipped to thirsty US refiners. "The US has developed a hemispheric energy policy, but needs to expand its sources of energy. The near civil war in Venezuela that raged over the end of 2002 and into 2003 has highlighted the impact disruption of a major supplier can cause," says energy security and Caspian expert John Roberts
Psychologically it would be nice for the US to diversify and get Russian crude but it would be too expensive for the Americans to rely on Russian oil. It would be useful, but no more so than extra crude oil from Angola, says Roberts.
Yukos president, Nikolai Bychkov, said last July that his company would start shipping cargoes of 270,000 tonnes to the US each month. The planned amount is equal to about 66,000 barrels per day. The monthly deliveries, while still modest, are larger than the first shipment of 200,000 tonnes.
It is notable US oil companies with major investments in the former Soviet Union region have yet to start regular shipments to the United States. In 1998, US-based Chevron Corporation imported 448,000 barrels of oil from its operation at Kazakhstan's Tengiz oil field as an experiment, but concluded that closer European markets made more economic sense.
Russia is now jostling with Saudi Arabia to be recognised as the world's largest producer, at least on paper. Saudis Arabia is rightly recognised as the main swing producer, capable of increasing output rapidly. Russia holds around 5% of the world

oil supply and, after decades of intensive exploration by Soviet-era geologists, few experts predict major new reserve finds.

Billions of dollars will need to be invested, and quickly, in basic oil production and transport infrastructure if Russia is to become a significant, long term shipper of crude oil to the US. With thirsty markets on its doorstep in Europe and a huge potential market in China on its eastern flank, sending oil to the US refiners does not make economic sense, at least for now.

But then investing has never been a short-term game and if PSA legislation can be reformed and pipelines laid, then perhaps Urals Blend will help slake America's unquenchable thirst for gasoline.