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2010 Russian Oil & Gas Outlook Survey

Introduction

2009, a year of recession, has come to an end and it is high time to sum up the results and identify perspectives for further development in the oil and gas sector.

Deloitte performs its Oil & Gas Outlook Survey annually in order to pool the opinions of oil & gas sector managers regarding the current issues of industry development. This year, the questionnaire was prepared based on the changes that have taken place in the global economy. Many of these questions deal with the crisis and the possible ways of ending it. As in previous years, we have interviewed the managers of companies operating in the hydrocarbon exploration, production and processing markets in Russia. The scope of our survey encompassed both large national and international vertically integrated companies, as well as independent small and mid-sized enterprises. The questionnaire was completed by the managers of both state owned and private oil and gas companies.

The survey was intended to review whether the oil and gas companies' market position was sustainable in the current economic environment and to identify their expectations for the future. As a result, we have concluded that this sector's companies possess the essential degree of stability that allows them to define the sector as sustainable and the least affected by the crisis. However, investments toward increasing production were reduced with no reduction of investments in social initiatives, environmental issues and personnel training. What is more, no reductions were made to occupational safety.

Half of the survey participants feel that the sources of their competitive advantage are efficient asset management and minimization of administrative and production costs, as well as control over strategy and efficiency management program implementation. A third of the respondents give preference to the introduction of new technologies and innovations and risk management.

The growth of the oil and gas sector seen last year implies not only an increase in the development of new fields', but also the efficient development of existing fields, as well as an increase in the depth of crude oil processing and development of oil products marketing and related services networks. The focus is not currently on quantitative but qualitative indicators, which characterizes the sector as innovative and intent on improving efficiency. Companies are making efforts to concentrate on core assets only, continue optimizing costs by improving contractor efficiency, reduce transportation costs and implement new, energy-saving technologies.

Thus, the crisis is characterized not only by negative events, but also includes some positive trends such as increased attention to quality and efficiency, risk management and the introduction of new technologies.

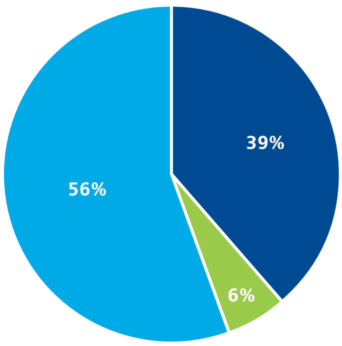
Below are the details of our survey. We would like to thank everyone who took part and wish you every success in 2010!

Elena Lazko
Partner in Charge
CIS Oil and Gas Practice

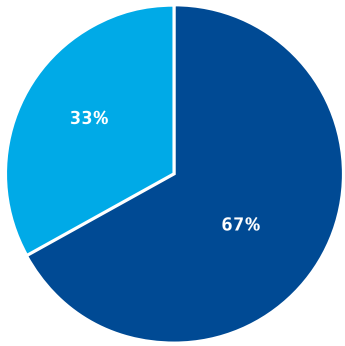
2010 Russian Oil & Gas Outlook Survey

How do you see domestic and global oil and gas demand changing over the next 5 years?

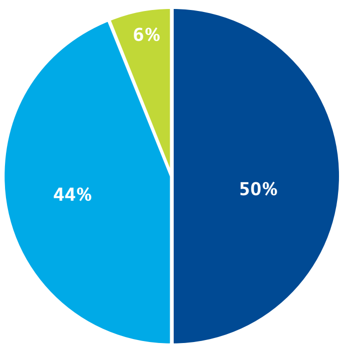
Domestic demand for oil over the next 5 years will:



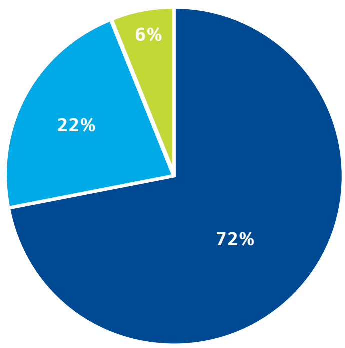
Domestic demand for gas over the next 5 years will:



Global demand for oil over the next 5 years will:



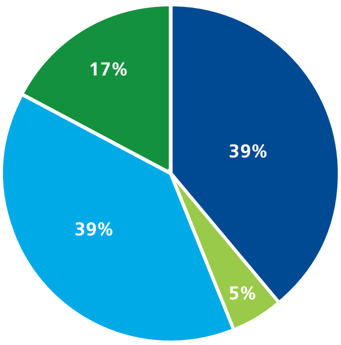
Global demand for gas over the next 5 years will:



- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don't know

Respondents are conservative in their outlook for both domestic and global demand for oil and oil products. However, many respondents are positive in their estimates for gas demand growth. This increase can be explained by a gradual recovery of the Russian and global economies, mainly driven by Chinese and Indian demand.

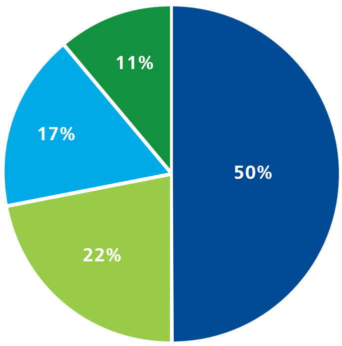
Compared with current prices, oil prices in 2010 will:



- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don't know

As a result of the sharp drop in prices in 2008 and subtle growth in 2009, respondents are divided in their views, with almost 40% answering that prices will increase, and another 40% saying prices will generally remain the same. A number of respondents (17%) believe that 2010 will see prices decrease compared with current levels. Analysts discouraged by incorrect predictions in the past also avoid offering clear-cut estimates. On the one hand, against the backdrop of a depreciating US dollar, growing stock markets and increased demand for raw materials, prices are expected to follow suit. On the other hand, many still remain doubtful that the crisis is over, pointing to "overheated" prices. The next year may show who is right.

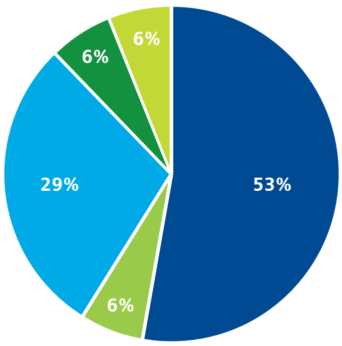
Over the next 5 years, the demand for capital in the Russian oil and gas industry will:



- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don't know

50% of respondents expect to see growth in the demand for capital over the next 5 years, with another 22% expecting a significant increase. Such expectations appear quite reasonable, given that many respondents predict growth in the demand for hydrocarbon stock, which could only be realized by further investment in both existing and new assets.

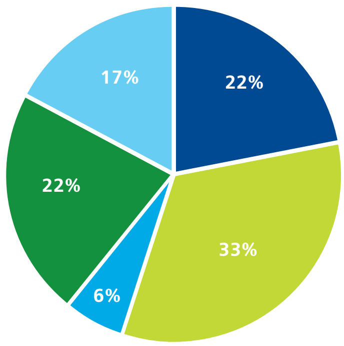
Over the next 5 years, the inflow of capital in the Russian oil and gas industry will:



- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don't know

Just over 50% of respondents suggest that investment inflow will grow over the next 5 years. Even if they do not correspond to the real situation, such responses seem to signal the industry's need for investment. Bringing about actual growth in investment would require addressing many issues, including those connected with improving the investing environment, creating a flexible taxation regime and reducing investment risks in Russia.

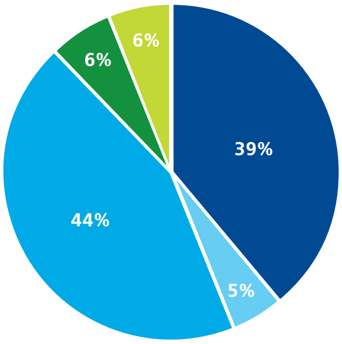
Over the next 5 years, the primary source of capital for the Russian oil and gas industry will become:



- Private capital (including foreign companies)
- Public offerings
- Third party loans
- Internal funds
- I don't know

Public offerings (33%) and private capital (22%) have been named by respondents as the most popular sources of capital. 17% of respondents have named internal funds instead. The survey results demonstrate a more balanced approach to lending as compared with previous years. Having accumulated a large debt, companies are considering employing their internal reserves.

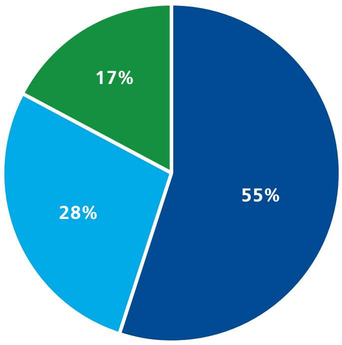
Over the next 5 years, the M&A and restructuring activities in the oil and gas industry will:



- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don’t know

44% of respondents are convinced that the volume of the M&A market will generally remain the same. However, 39% believe that M&A activities will increase. The fact that so many respondents expect activities to intensify can be explained by the global trend towards consolidation, as well as by the expectations of further consolidation among state owned oil and gas companies.

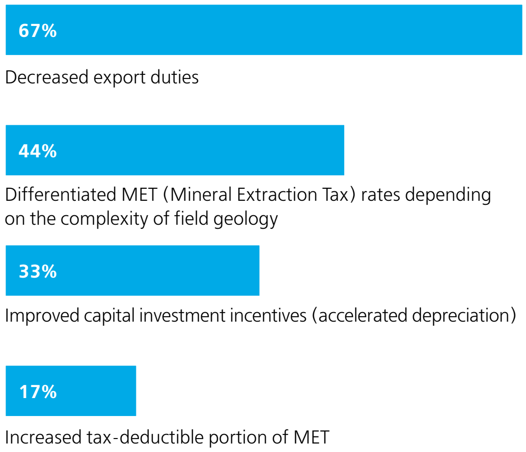
Over the next 5 years, state regulation of the Russian oil and gas industry will:



- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don’t know

As in previous years, respondents have pointed out that the already common presence of state institutions in the industry will continue to grow. When should we expect a reversal of this trend? Only time will tell.

The tax benefits and tax adjustments the industry can most benefit from are (please select):



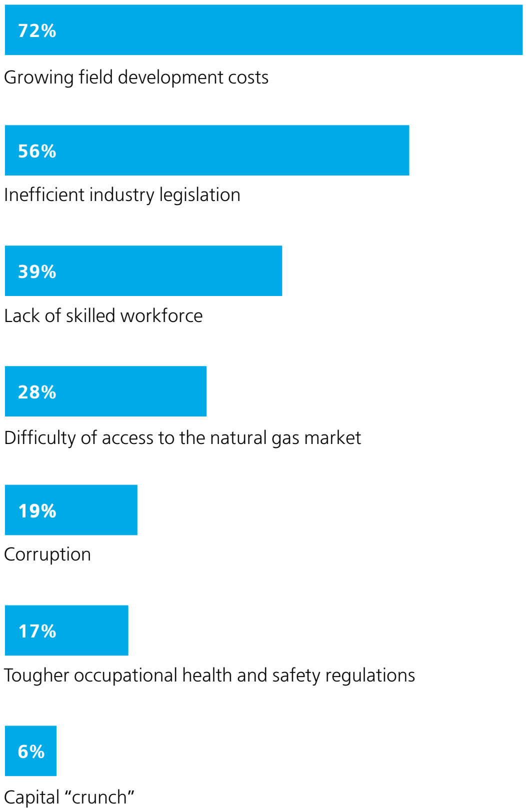
Decreased export duties and differentiated MET are named by respondents as the most beneficial incentives for the industry.

Reserves are getting harder to reach and extract

For more information please read our survey "Oil & gas reality check" in the "Energy & Resources" section at our site www.deloitte.ru

In your view, which of the problems facing oil and gas companies are the most challenging?

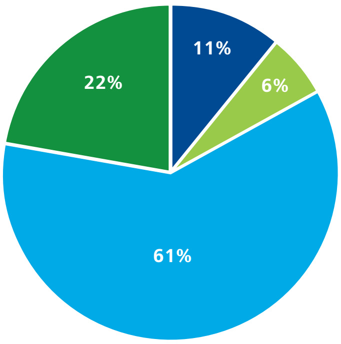
As in previous surveys, the most popular reply given by respondents is "growing field development costs". "Inefficient industry regulation" follows in second and "lack of skilled workforce" comes third. Such a wide range of responses provides a fairly clear picture of the industry, and given the unresolved problem of how difficult it is to access the gas market, these opinions indicate that despite the apparent prosperity of the oil and gas industry, there is a tangle of problems which companies will need to address to stay successful.



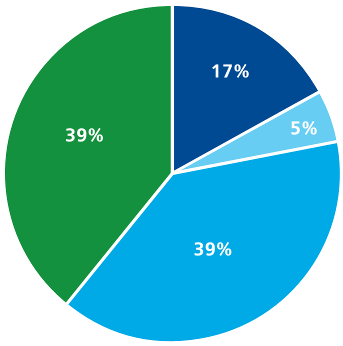
Your headcount in 2009 has:

Head office

Management

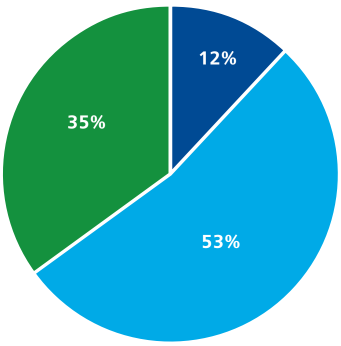


Professional and administrative staff

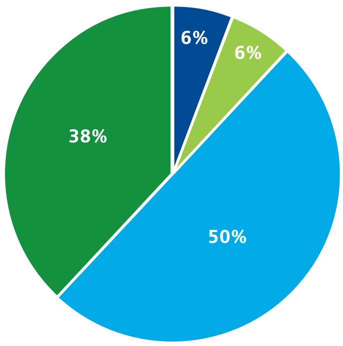


Production units

Management, professional and administrative staff



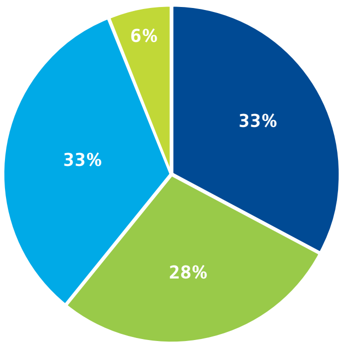
Blue collar workers



- Increased
- Increased significantly
- Generally remained the same
- Decreased
- Decreased significantly
- I don't know

Like others during the crisis, oil and gas companies have cut their operational costs by reducing headcount. The survey has shown that staff reductions have affected various categories of employees. However, some respondents reported a headcount increase, with results ranging from 6% to 17% for various employee categories. Companies therefore demonstrated a balanced HR approach in adjusting their headcount, rather than attempting across-the-board staff cuts.

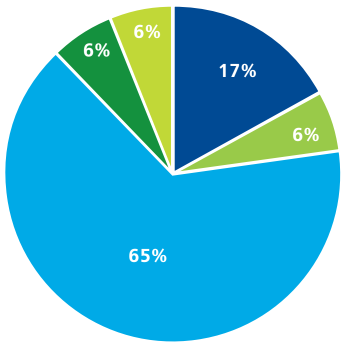
How would you describe the impact of the global crisis on your company?



- Our business has suffered from the crisis
- The crisis has benefited our business; we have emerged even stronger than before
- Our business remains unaffected by the crisis
- I don't know

Respondents are divided in their opinions, with 33% replying that they are "unaffected by the crisis" and another 33% saying that the crisis has had a negative impact on their business. A remarkable 28% of respondents say that they have benefitted from the crisis. This is because adverse market conditions have successfully spurred such companies to improve their operational and financial performance in order to emerge stronger from the crisis.

In 2009, you have seen your production assets:

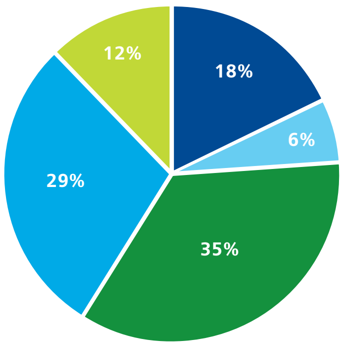


- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don't know

The production asset portfolios of most of the companies have not changed significantly during the crisis in 2009. However, 17% of respondents have said that their asset portfolio has grown, which may actually mean that during the period of instability, companies were keen to preserve their existing business, only taking the risk to increase their asset portfolio in some cases, including acquiring assets in other countries.

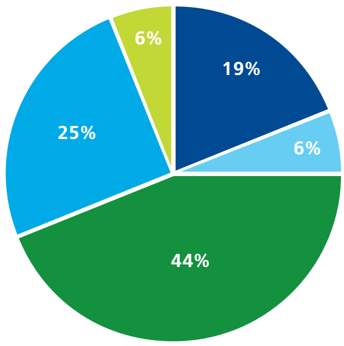
In 2009, your company's spending in the areas specified below has:

R&D in oil and gas



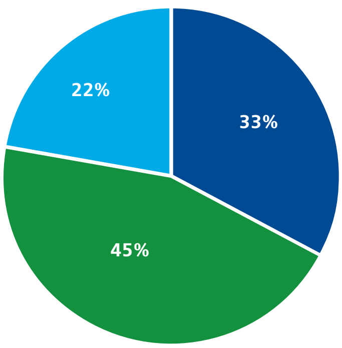
35% of respondents have reduced R&D investments, and 29% kept their R&D investments at the same level.

Capital construction



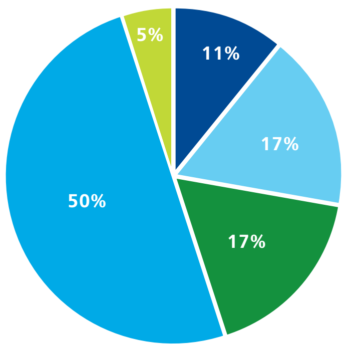
Capital construction experienced a more pronounced cut. 44% of respondents say they have reduced spending on capital construction.

Operational activities



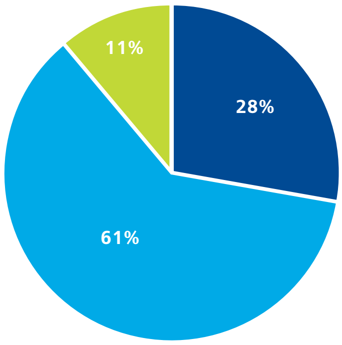
Cutting operational expenses was expected during the crisis and is what 45% of respondents chose to do.

Personnel training



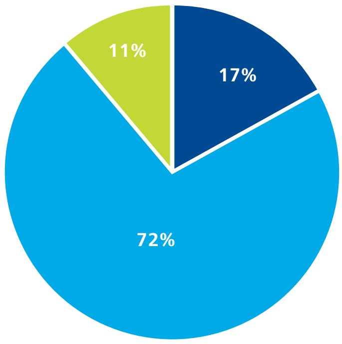
A company's success depends largely on its personnel. Even against the backdrop of the crisis, 50% of respondents chose not to reduce their spending on training.

Environmental safety, including oil well gas utilization



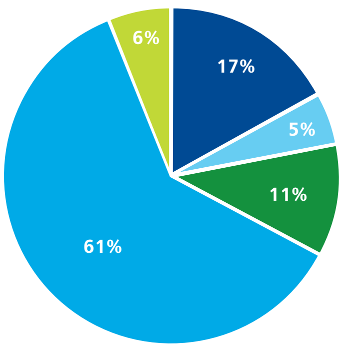
Oil and gas companies continue to invest in environmental safety and oil well gas utilization. Over 60% of respondents reported retaining their spending level, and 28% said they had increased their spending.

Occupational health and safety



An overwhelming majority of the companies surveyed (72%) kept the same level of spending on occupational safety, and 17% increased such spending.

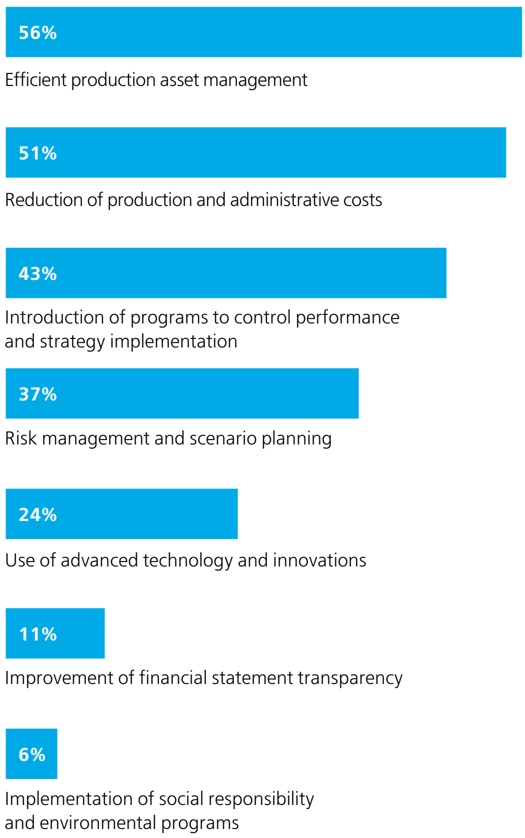
Social programs



Spending on social programs generally remained the same, although some companies managed to find the resources to increase it.

- Increased
- Increased significantly
- Generally remained the same
- Decreased
- Decreased significantly
- I don’t know

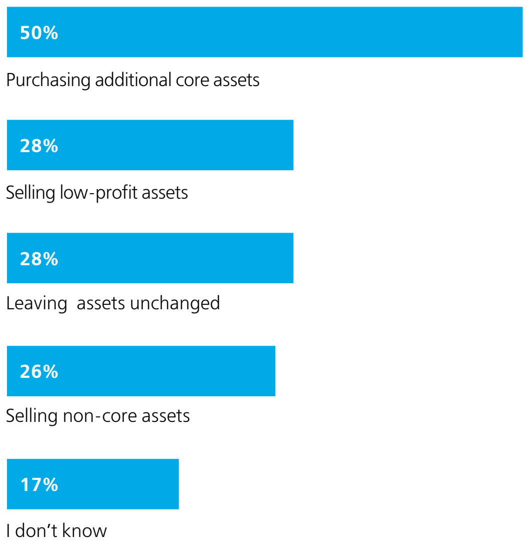
Which of the strategic initiatives listed below would you name as the most important for your company to stay competitive?



Survey participants named asset management, cost reduction measures and programs to control performance and strategy implementation as the most important sources of competitive advantages. Next was risk management and scenario planning (37%), followed by advanced and innovative technology (24%). Improvement of financial statement transparency was specified by 11% of respondents, demonstrating that, although undoubtedly important, this measure is not seen by the companies as a core competence.

What will be your company's approach to managing its assets in 2010? From the options below, please select all that are relevant.

50% of respondents plan to purchase additional core assets in 2010. Moreover, about 30% have plans to restructure their current asset portfolios by disposing of non-core and low-profit assets (28%). In 2009, companies were rather checked in their M&A activities, saving their efforts for a major leap in 2010.



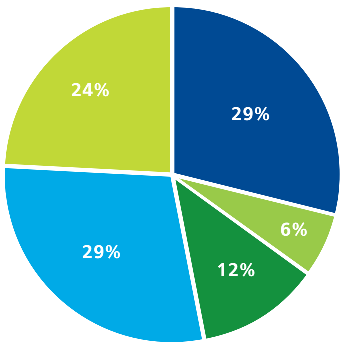
The pace of mergers and acquisitions accelerates

For more information please read our survey "Oil & gas reality check" in the "Energy & Resources" section at our site www.deloitte.ru

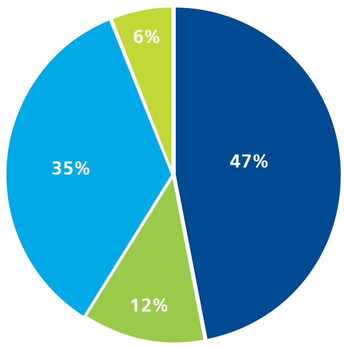
Compared with 2009, which of the operational areas specified below does your company plan to expand or cut back in 2010?

Upstream

Drilling

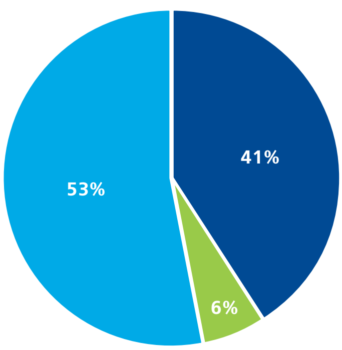


Efficient field development

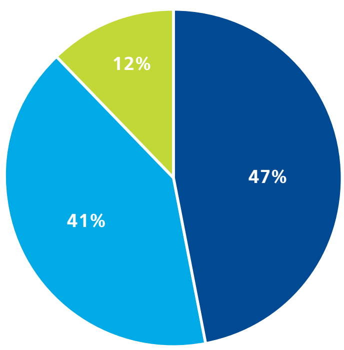


Midstream

Total processing capacity

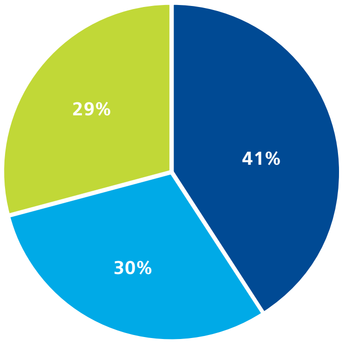


Processing efficiency

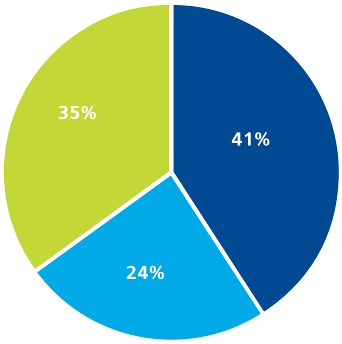


Downstream

Number of filling stations



Products and services offered



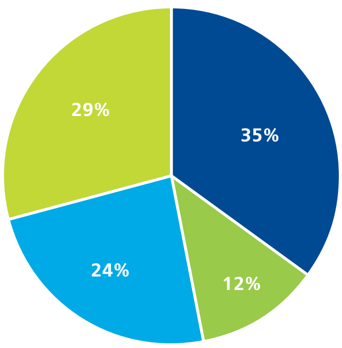
- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don't know

These answers clearly demonstrate the shift from quantitative to qualitative measures. Companies are planning to improve field development efficiency (47%), invest in improving processing efficiency (47%) and expand the number of products and services they offer at filling stations (41%).

Compared with 2009, for which of the operational areas specified below does your company plan to increase or cut back in capital investments in 2010?

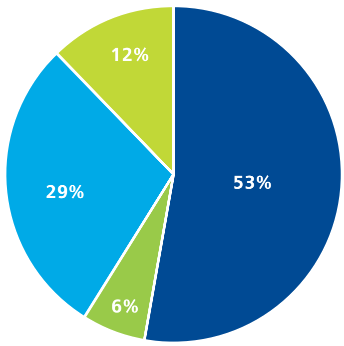
Most respondents are quite optimistic in their views and plan to increase capital investments across the value chain. Such an optimistic outlook on business development issues is partially driven by anticipated growth in hydrocarbon prices and demand, as well as by the need to compensate for lost opportunities in 2009.

Oilfield purchasing



35% of respondents plan a general increase of capital investments in purchasing oilfields, with another 12% planning a major increase.

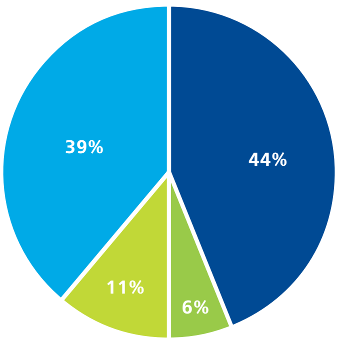
Field development



53% of respondents plan to increase their investments in field development to compensate for lost opportunities in 2009.

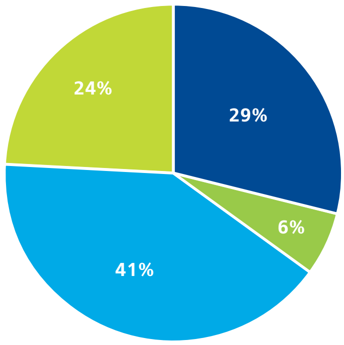
- Increase
- Increase significantly
- Generally remain the same
- Decrease
- Decrease significantly
- I don't know

Upstream



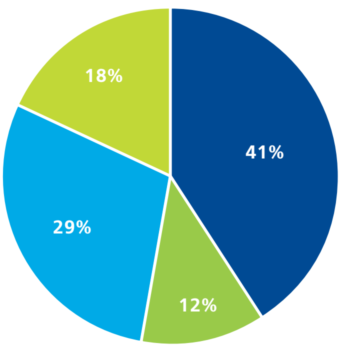
Respondents are divided on the issue of investments in operational activities, with 39% planning to leave the level of capital investments unchanged and 44% planning a general increase.

Midstream



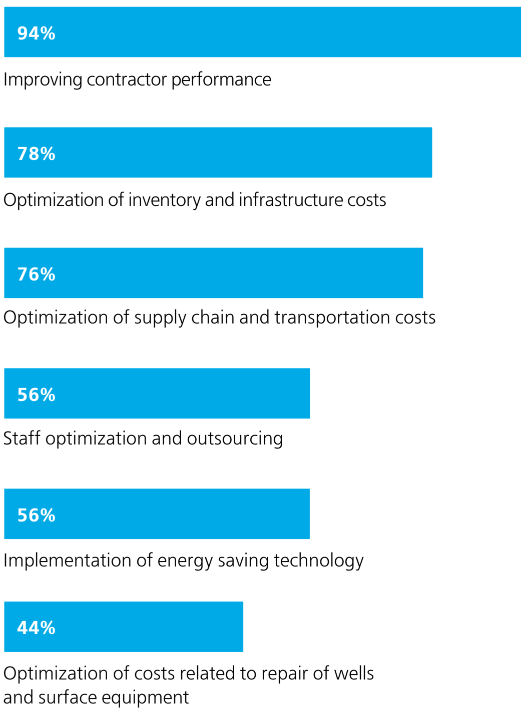
Most respondents (41%) plan to leave the level of midstream investments unchanged, and 29% have plans for a general increase in investment.

Downstream



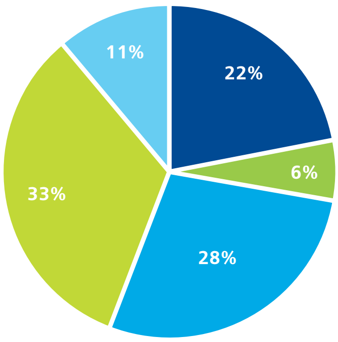
Over 50% of respondents have plans for either a general or major increase in capital investments in downstream assets, and 29% will leave these levels unchanged.

In 2010, what will be your company's approach to controlling/reducing operational costs? From the options below, please select all that are relevant:



Respondents have been unanimous in specifying that cost optimization would first of all require improving control of contractor performance, as well as optimizing costs related to inventory, infrastructure and supply chain. It is interesting to note that companies achieved significant success adopting such measures in 2009.

Do you invest in the alternative energy research and development?



- Yes we do, and we also have plans to expand the investments
- Yes we do, and we will maintain investment at the current level
- I don't know
- No, we don't
- No, we don't, but we are planning to do so

The existing global trends have lead businesses to consider investments in alternative energy sources. However, 33% of respondents replied that their companies have not been investing in alternative energy and do not have plans to do so in the coming years. In the absence of a real alternative to oil and gas, hydrocarbons remain the major focus, which is undoubtedly understood by the surveyed executives at oil and gas companies.

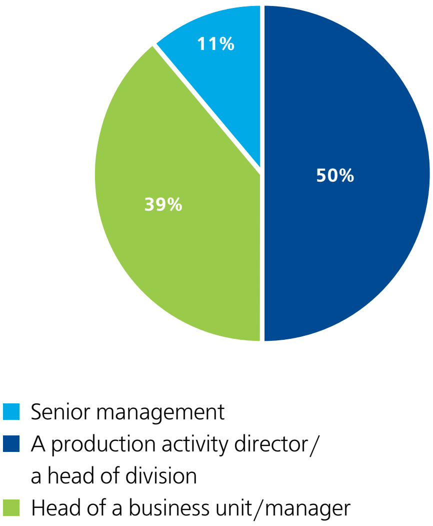
An alternative energy strategy is mandatory

For more information please read our survey "Oil & gas reality check" in the "Energy & Resources" section at our site www.deloitte.ru

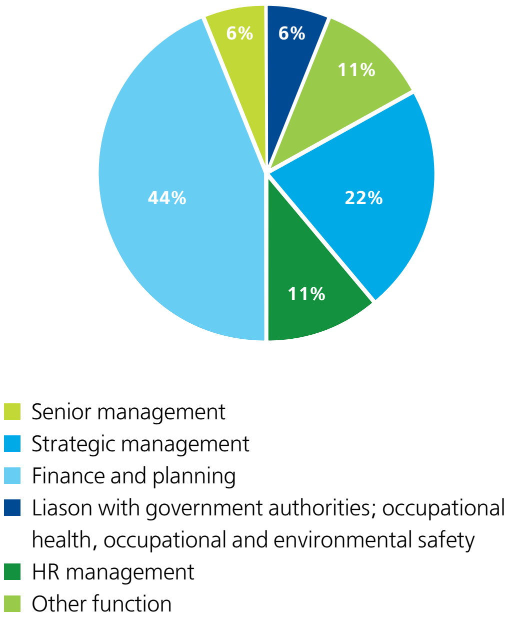
Our respondents

Our survey was conducted among executives at the companies operating in Russia and engaged in hydrocarbon exploration, production and processing. The survey covers both local and international vertically integrated companies, as well as independent small and mid-size businesses. Among the participants of the survey were both state owned and private companies operating in the Russian oil and gas market.

Survey participants' positions within their companies:



Functional area:



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