



2012 Russian Oil & Gas Outlook Survey



Introduction



In 2011, the oil and gas industry saw high oil prices and a steady increase in global energy demand. Global energy demand is still growing and the results of Exxon Mobil's survey revealed that, by 2040, demand would increase by 30 per cent from countries in the Organization for Economic Cooperation and Development (OECD), including North America and Europe, and by 60 per cent from other countries. The share of unconventional hydrocarbon sources (such as shale formations) will increase. Oil and gas will account for 60 per cent of all energy sources.

At the end of each year, we conduct a survey given to oil and gas company executives to find out their views on the prospects of business development in the upcoming year. The respondents were asked their opinions on industry processes and their expectations during the period from September to November. Both private and state oil and gas company executives took part in the survey.

Given the favourable outlook for hydrocarbon demand, most oil and gas companies plan to expand their core asset portfolios and are preparing to invest in the resources and field development mainly using their own funds for financing.

For most oil and gas companies, the main operational priorities are to improve contractors' performance and optimize logistics.

The companies' expectations of tax regulations are clear – nearly 40 per cent of all respondents said Mineral Extraction Tax (MET) differentiation is the main factor that will favourably affect industry development.

The results of the Deloitte survey can be found below. We hope that the results of our survey are interesting and useful for you.

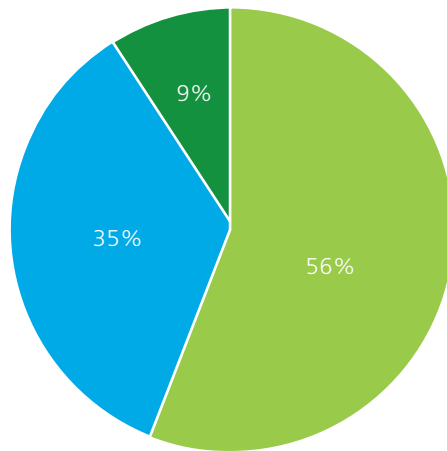
We would like to thank all those who shared their thoughts on the future of the oil and gas industry with us and we wish our readers all the best for 2012.

Elena Lazko
Partner
Oil & Gas Leader

2012 Russian Oil & Gas Outlook Survey

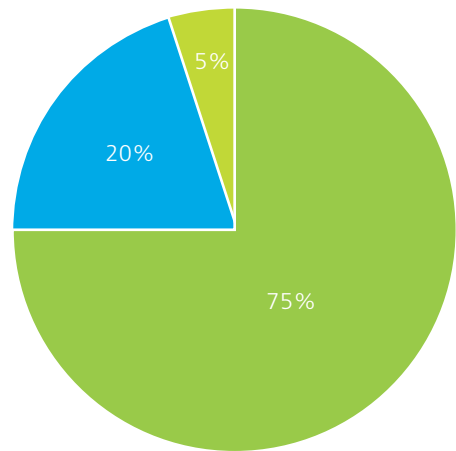
How do you think the demand for oil will change over the next 5 years in both the Russian domestic and global markets?

Domestic demand for oil



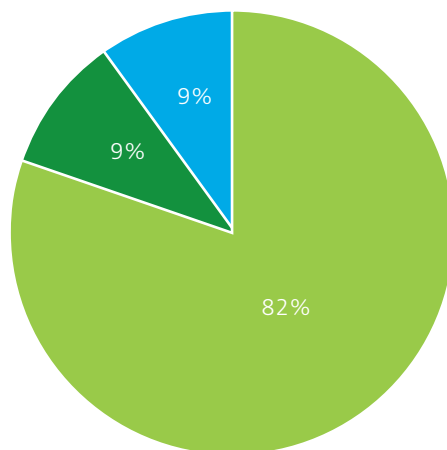
■ Remain the same
■ Increase
■ Significantly increase

Domestic demand for gas



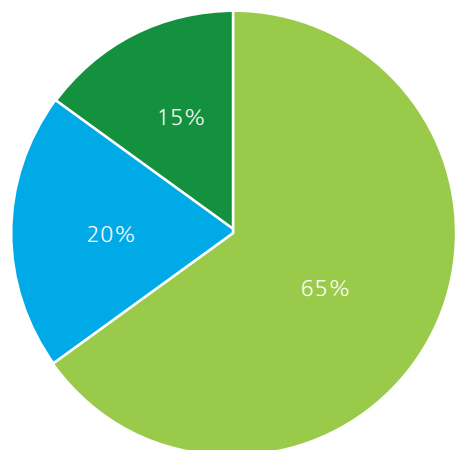
■ Remain the same
■ Increase
■ Decrease

Global demand for oil



■ Remain the same
■ Increase
■ Significantly increase

Global demand for gas

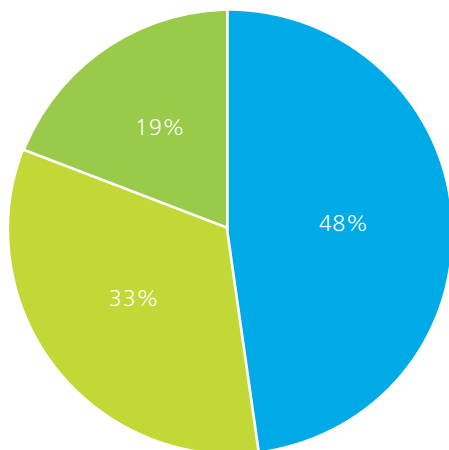


■ Remain the same
■ Increase
■ Significantly increase

The respondents are as optimistic about the demand for oil and gas as they were last year. 56 per cent of survey respondents believe that the demand for oil in Russia will keep growing, and 9 per cent of respondents expect the demand for oil and gas to increase considerably in the next five years. Such an increase will mainly be driven by increasing consumption in the Asia-Pacific,

which is fuelling discussions on the future development of the nuclear power industry and new discoveries of shale deposits. 91 per cent of the respondents also think the global oil market will grow. The proportion of respondents who expect domestic and global gas demand to increase was up compared with last year (75 per cent and 80 per cent respectively).

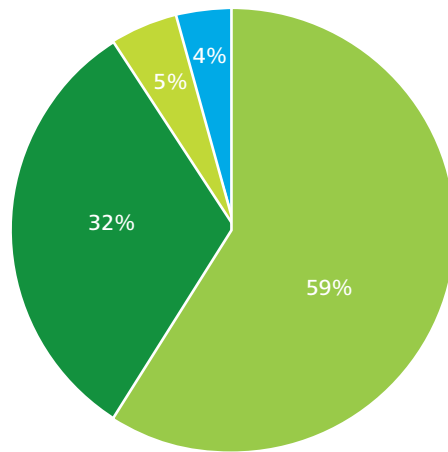
Compared with current prices, oil prices in 2012 will:



- Remain the same
- Increase
- Decrease

Oil prices increased in 2011, as the majority of the respondents (46 per cent) predicted the previous year. Prices have remained in the USD 94–125 per barrel range. They have reached pre-crisis level, although almost half of the respondents (48 per cent) do not expect any further changes in prices, while one third anticipate a decline. Only 19 per cent said that oil prices might rise.

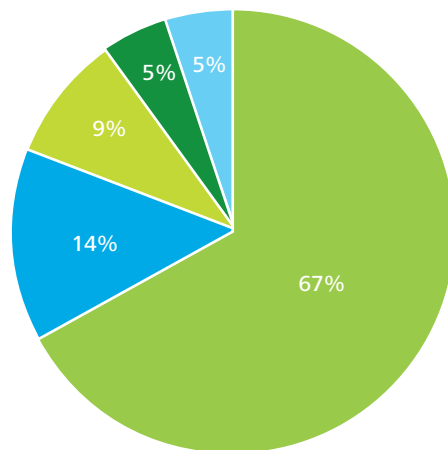
Over the next 5 years, capital demand in the oil and gas industry will:



- Remain the same
- Increase
- Decrease
- Significantly increase

As many as 91 per cent of respondents expect to see capital expenditure on oil and gas to grow over the next five years, with 32 per cent anticipating a significant increase. The reason may lie in the projected growth of demand for hydrocarbons: to meet such demands, new fields will have to be developed, and this will mean greater exploration of the Arctic shelf, which has been limited up until now. The cost of developing Arctic exploration in particular will be higher in terms of cost per unit of geological exploration and infrastructure development (cost will probably be 1.5-2 times higher) and the period between capital investment and peak production will be longer (approximately 10 to 12 years from the start of the exploration process). Besides, upstream and downstream equipment is in need of renovation, so significant investment will be required to upgrade or fully replace such equipment.

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

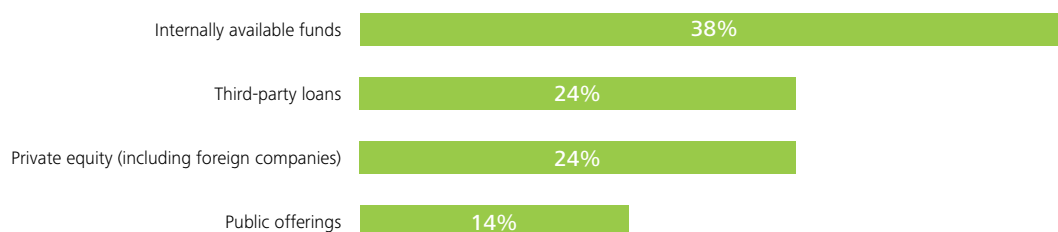


- Remain the same
- Increase
- Decrease
- Significantly increase
- Don't know

Given that current energy prices have reached pre-crisis price levels, 72 per cent of survey respondents believe that capital inflow into the oil and gas sector will grow, with 5 per cent of them expecting a significant increase in investment. Less than 10 per cent of respondents suggested a decline in capital inflow, which is likely to be related to the unstable investment climate in Russia.



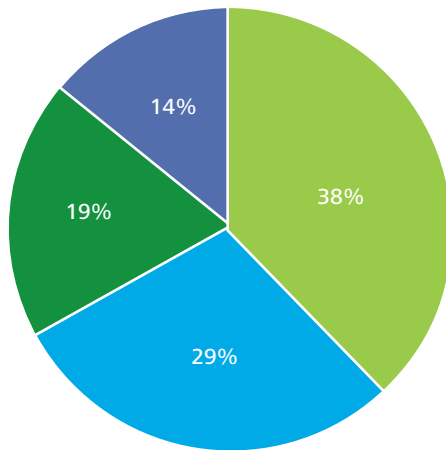
Over the next 5 years, the primary source of capital for the Russian oil and gas industry will be:



The nature of capital sources changed considerably compared with the previous year. While almost half the respondents (45 per cent) were prepared to consider third-party loans as a source of capital in 2011, internally available funds will be the main source in 2012, according to 38 per cent of respondents (last year, the

percentage of respondents with the same view was no higher than 9 per cent). Rumours and expectations of a second crisis, along with the elections expected to be held in 2012, might have led respondents to believe a more careful approach towards obtaining capital funding would be taken.

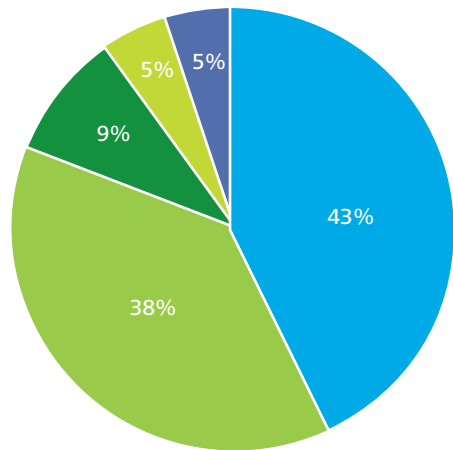
Over the next 5 years, participation by state companies in the industry will:



- Remain the same
- Increase
- Significantly decrease
- Significantly increase

Respondents' views were split almost evenly: 47 per cent expected state influence over the industry to increase, while a similar proportion said it would remain unchanged. 57 per cent of respondents believe that the state still has significant influence and participation by state companies will increase. While last year a significant number of respondents expected the influence of state companies to decrease, this year,

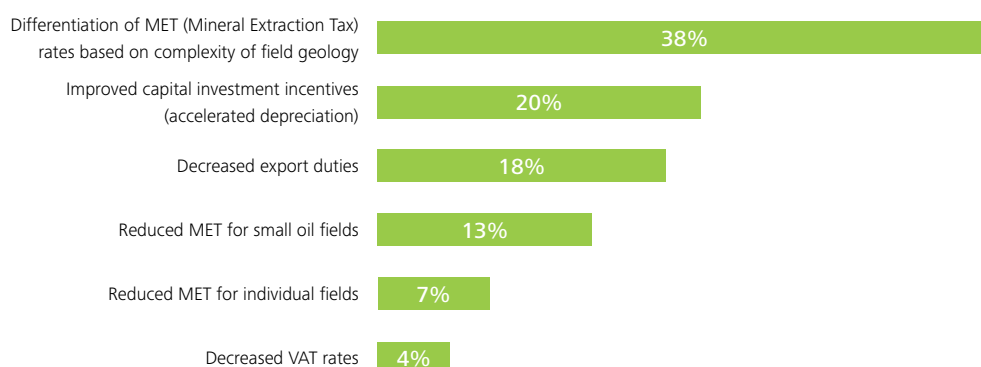
Over the next 5 years, state regulation of the oil and gas industry will:



- Remain the same
- Increase
- Decrease
- Significantly decrease
- Significantly increase

almost 20 per cent believe it will grow significantly. For example, technical regulations were amended in September 2011 to permit production and sales of Euro-2, Euro-3, and Euro-4 petrol and diesel fuels until the end of 2012, 2014, and 2015, respectively. It turned out that large state company refineries were not prepared for producing the required volumes of higher-quality fuel.

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



Differentiated MET rates (38 per cent), improved capital investment incentives (20 per cent), and reduced export duties (18 per cent) remain the most cited tax incentives for the industry.

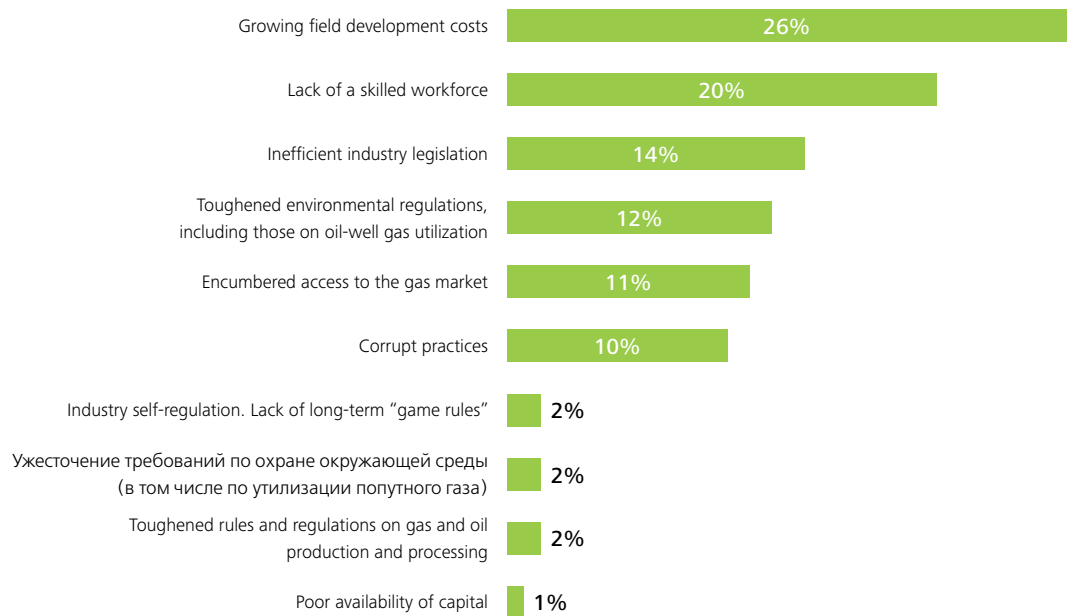
The state is taking certain steps to address these proposals.

In July 2011, a decree was signed to reduce the tax burden for the national gas and oil industry. A decision was made to cut MET on oil to zero for shelf production in the Black Sea and the Sea of Okhotsk. A zero rate of MET rate was also introduced for gas produced through the Yamal LNG production projects. Additionally, MET rates were reduced for small oil fields with initial recoverable reserves not exceeding 5 million tonnes.

The Russian Ministry of Energy's project stipulates, among other things, a rate of zero on export duty and MET for oil, gas and condensate produced in the Caspian Sea and on the Arctic shelf.

Another example is a reduction in the preferential export duty rate for oil produced in the fields in Eastern Siberia and LUKOIL's two Caspian fields as of January 2012. Moreover, a new "60/66" methodology for calculating export duties on oil and petroleum products became effective on 1 October 2011. The export duty rate for light and heavy petroleum products has been unified and calculated at 66% of the duty on oil. Export duty on oil has also been reduced.

In your view, what could be the most serious problems facing oil and gas companies?

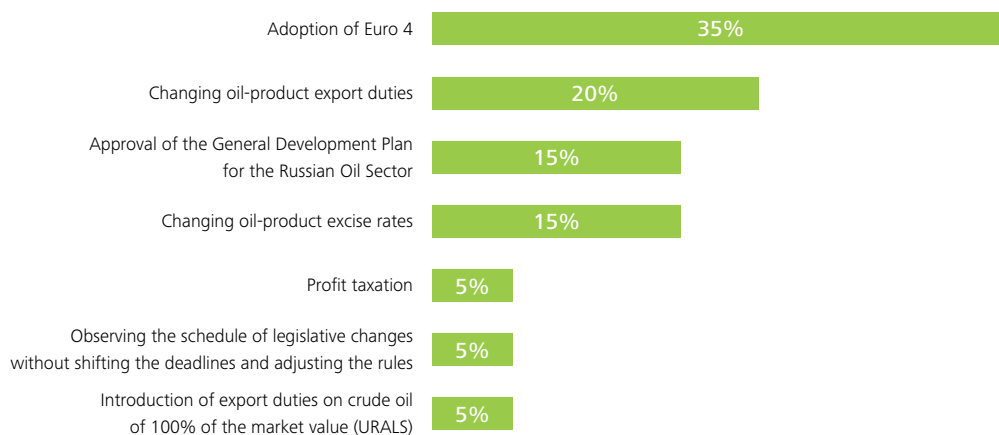


As it has in the past two years, increased oil development costs lead the list of the most significant issues faced by oil and gas companies (chosen by 26 per cent of respondents). Costs associated with developing new fields geologically challenging locations and significant investments in infrastructure are still seen as serious problems. The global issue of applying new technologies and developing new approaches to the production and refining of hydrocarbons is present

in, among others, the Russian market. As you can see from the chart, the second most important problem for companies is lack of a skilled workforce (20 per cent).

As many as 14 per cent of respondents suggested that insufficient industry legislation will be a major problem. Another 12 per cent highlighted toughened environmental regulations.

Which of these events do you think will have the greatest impact on the oil processing industry?



Respondents' opinions have changed in comparison to last year. While 35 per cent of respondents this year cited the introduction of Euro 4 technical regulations as having the most significant impact on the oil refining industry, last year the Master Plan for Development of the Oil Industry was regarded as being the most important.

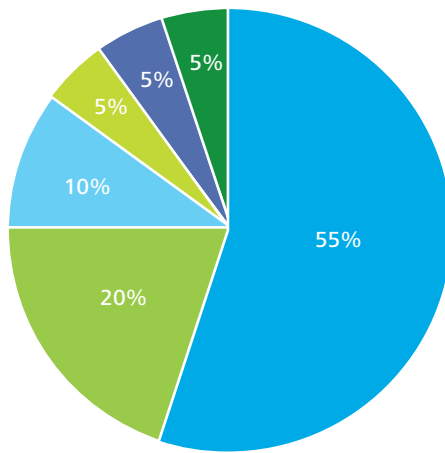
The introduction of Euro 4 regulations and tight restrictions on production will motivate companies to upgrade the equipment and processes required for production of high-quality fuel and higher refining-rate products. Also, 20 per cent of respondents believe that changes to petroleum product export duties is going to greatly impact the refining sector. Last year, respondents did not cite this as an influential factor for the industry.

Your headcount in 2010 has:

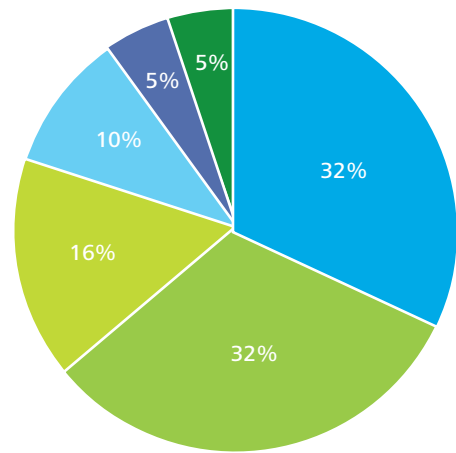
Headquarters

Management

- Remained the same
- Increased
- Decreased
- Significantly decreased
- Significantly increased
- Don't know



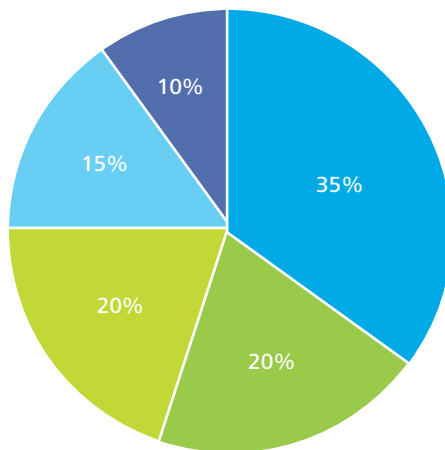
Professional and administrative staff



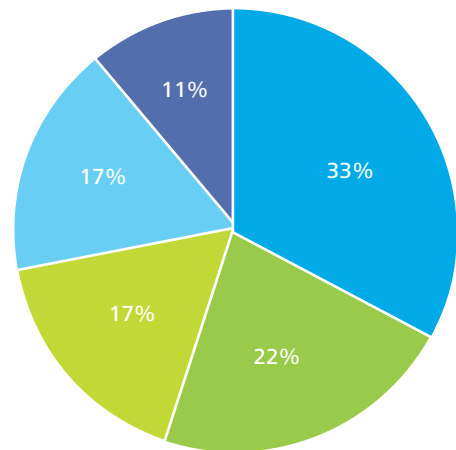
Production units

Management, professional and administrative staff

- Remained the same
- Increased
- Decreased
- Significantly decreased
- Significantly increased
- Don't know



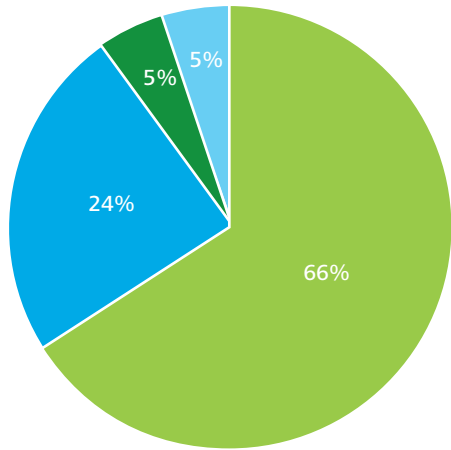
Skilled and unskilled worker



25 per cent of respondents reported an increase in management personnel at their headquarters (compared with 37 per cent in 2010), and 37 per cent reported a higher headcount for professionals and office workers (compared with 46 per cent in 2010). As for production

units, 28 to 30 per cent of survey respondents reported decreased headcounts (as compared with 9 per cent in 2010), with only 20 to 22 per cent indicating an increase (compared with 27 to 36 per cent in 2010).

In 2011, your production assets:

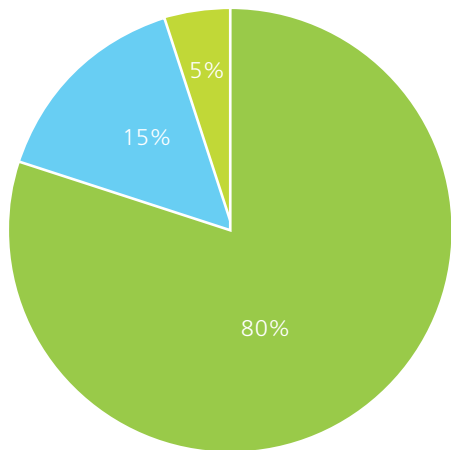


- Remained the same
- Increased
- Significantly increased
- Don't know

Companies have been building up their assets for a second year running after the 2009 crisis. As many as 71 per cent of survey respondents indicated that their portfolios had increased, while almost one quarter of the companies surveyed (24 per cent) did not acquire any new assets.

In 2011, your company's spending in the following areas has:

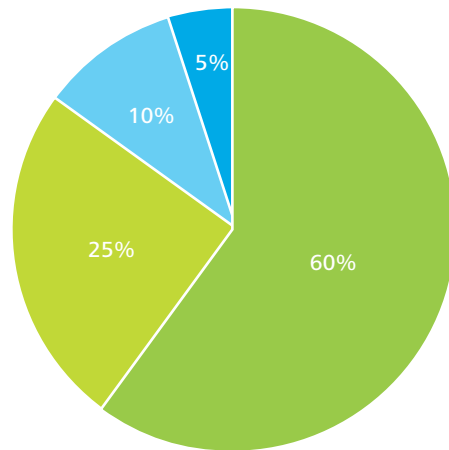
Capital construction



- Increased
- Decreased
- Don't know

80 per cent of companies increased and five per cent decreased capital construction.

Operational activities



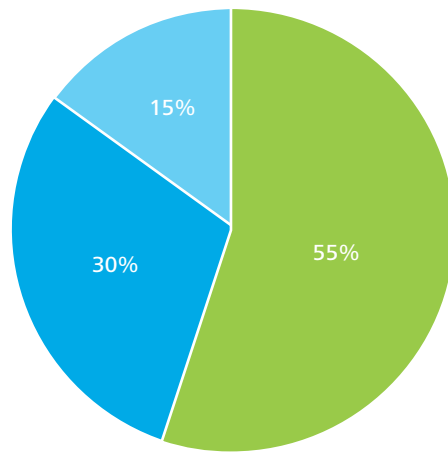
- Increased
- Remained the same
- Don't know
- Decreased

60 per cent of respondents reported increased spending on operational activities, while 25 per cent cut down their spending.

High oil prices (above USD 100 per barrel) have persuaded companies to invest in capital construction and current operations, new developments, and innovations. The share of companies with increased

spending on capital construction grew from 55 per cent in 2010 to 80 per cent in 2011. Fewer companies (60 per cent in comparison to 73 per cent last year) increased their spending on current operations in 2011.

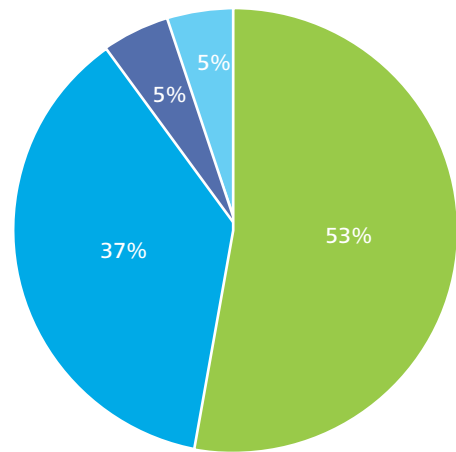
R&D in oil and gas



■ Increased ■ Don't know
■ Remained the same

As in the previous year, 55 per cent of companies increased their spending on research and innovations, while 30 per cent did not change their spending budget. More challenging production conditions and increasing costs for refining motivated companies to carry out development activities, in order to reduce production time and costs, and to increase their refining efficiency.

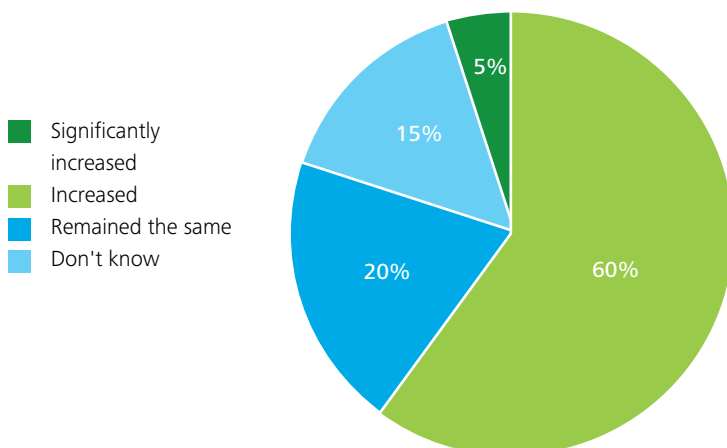
Personnel training



■ Increased
■ Remained the same
■ Significantly decreased
■ Don't know

In 2011, spending on personnel training increased significantly: from 27 to 53 per cent. This trend was driven by the increasing share of companies which introduced new technologies and upgraded their production. Only 5 per cent of companies reduced their spending.

Environmental safety, including utilization of gas from oil wells



■ Significantly increased
■ Increased
■ Remained the same
■ Don't know

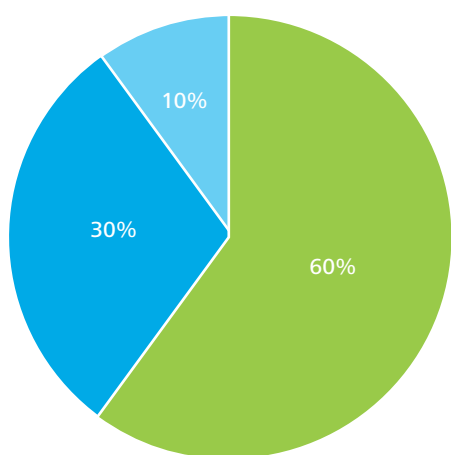
More than 60 per cent of companies increased their environmental spending, while 20 per cent kept it steady.

The requirement to utilize 95 per cent of associated petroleum gas (APG) will come into effect in 2012. Large oil companies have already approved target programs for bringing APG utilization to the required level. Therefore, more companies still are expected to increase their spending on APG utilization.

At present, the percentage of flared APG in Russia is much higher than the global percentage, making up 26 per cent of total volumes; 76 per cent of APG is utilized.



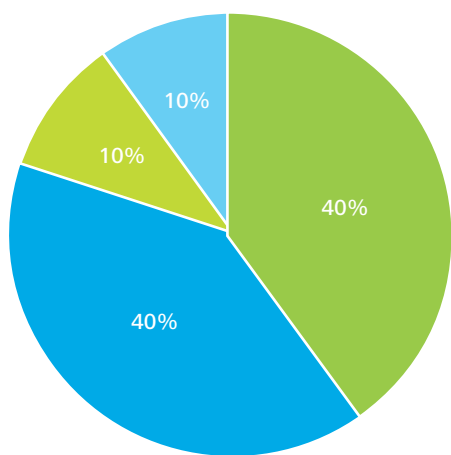
Occupational health and safety



- Increased
- Remained the same
- Don't know

60 per cent of companies increased their spending on occupational health and safety, while 30 per cent of respondents kept levels of investment in occupational health and safety the same as last year.

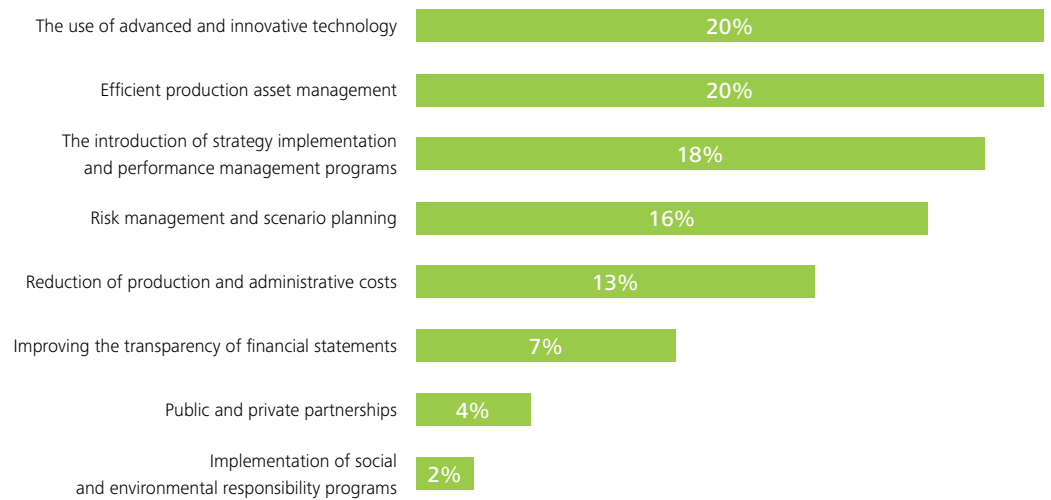
Social programs



- Increased
- Decreased
- Remained the same
- Don't know

Spending on social programs remained almost unchanged compared with the previous year. 40 per cent of companies increased their social spending; another 40 per cent kept it steady; and only 10 per cent of respondents reduced spending on social programs.

In your view, which of the strategic initiatives listed below are the most important so that your company remains competitive?



According to respondents, the most important strategic initiatives for companies to stay competitive are implementing cutting-edge technologies and innovations, and efficient asset portfolio management (20 per cent each). These are followed by introducing performance management programs and strategy

implementation control (18 per cent, as compared with 7 per cent in the previous year). The share of respondents who indicated that cutting-down on production and administrative expenses was important for their companies fell from 21 to 13 per cent.

Compared with 2011, which of the operational areas specified below are you planning to expand or cut back on in 2012?

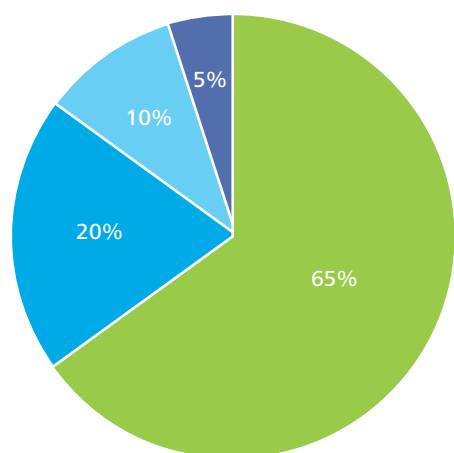
The surveyed companies plan to improve their quantity and quality indicators across the value chain. This trend was observed in the previous year as well. However, 25 per cent of the surveyed companies lack well-defined

plans for 2012 for developing their refining operations, and more than 25 per cent do not have any plans to expand sales networks.

Upstream

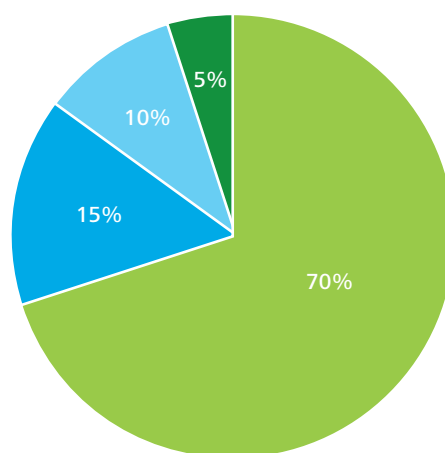
Drilling

Improving efficient use of fields



- General expansion
- Unchanged
- Major cut-backs
- Don't know

The share of respondents planning to increase their drilling expenditure grew by 15 per cent in comparison to the previous year, amounting to 65 per cent. 75 per

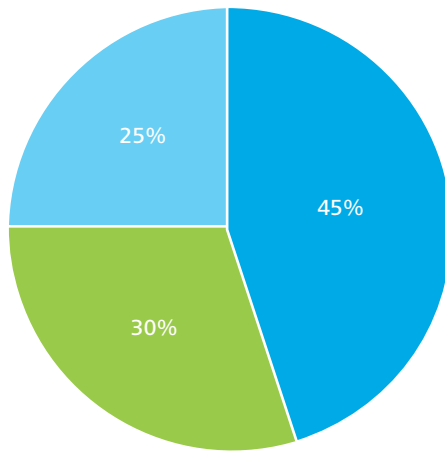


- Major expansion
- General expansion
- Unchanged
- Don't know

cent of companies plan to enhance the development efficiency.

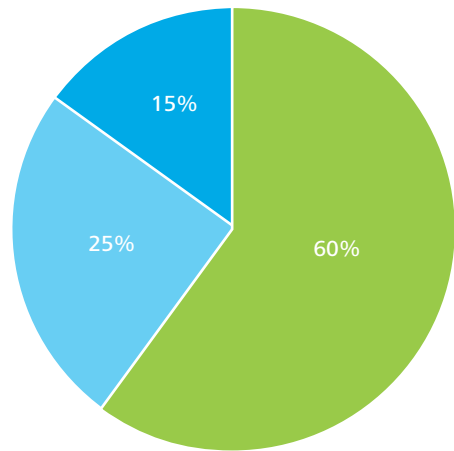
Midstream

Total processing capacity



- General expansion
- Unchanged
- Don't know

Processing efficiency



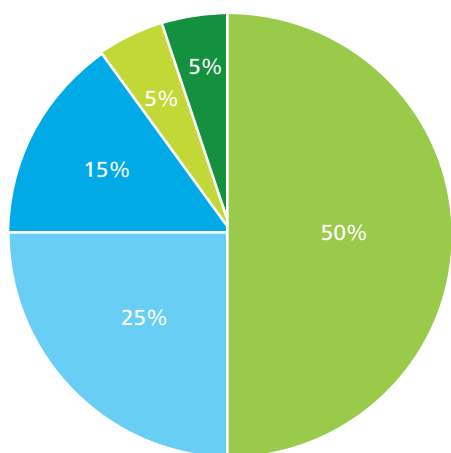
- General expansion
- Unchanged
- Don't know

Russian oil refineries have an average refining efficiency of 72 per cent, compared to between 85 and 95 per cent in other countries globally. As many as 60 per cent of companies plan to increase their refining efficiency, which shows that Russian businesses are eager to improve in this respect. Until recently, average

capacity utilization for refineries was around 80 per cent, which may be one of the reasons why almost half of respondents (45 per cent) do not plan to increase expenditure on increasing their aggregate production capacity.

Downstream

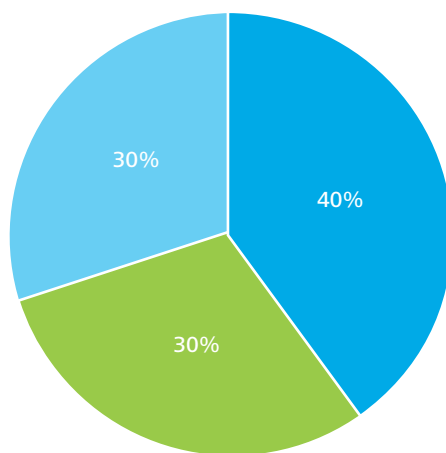
Number of fuel stations



- General expansion
- Unchanged
- General cut-backs
- Don't know
- Major expansion

As many as 55 per cent of companies intend to increase expenditure on constructing new filling stations in 2012, while only 30 per cent plan to expand their product and service offerings.

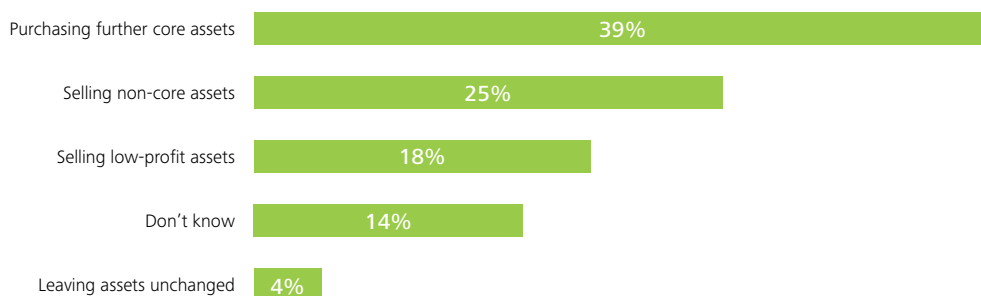
Product and service offerings



- General expansion
- Unchanged
- Don't know

In general, the majority of companies plan to invest in production, improved efficiency of field use and greater refining efficiency.

What plans do your company have for asset management in 2012?



Compared with the previous year, responses to the question of how the existing asset portfolio would be managed have changed significantly. While only 22 per cent of companies planned to acquire new core assets in 2011, the proportion is 39 per cent in 2012. Only 25 per cent of companies are going to sell their non-core

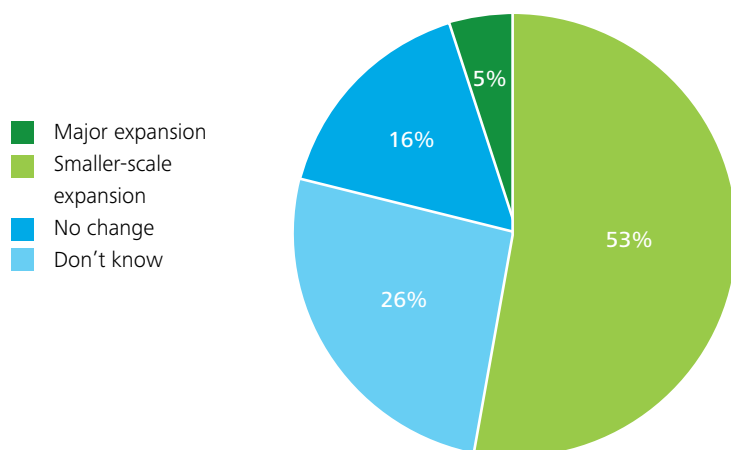
assets, which is considerably less than in 2011 (67 per cent of surveyed companies). Such a trend may suggest that many companies have already sold their non-core assets, and high oil prices and the expected increase in demand for hydrocarbons is driving M&A activity in the industry.

Compared with 2011, which of the operational areas specified below are you planning to expand or cut back capital investments on in 2012?

The majority of companies responded that they would increase capital investment in all areas of their activities. The share of the respondents who did not give a definite

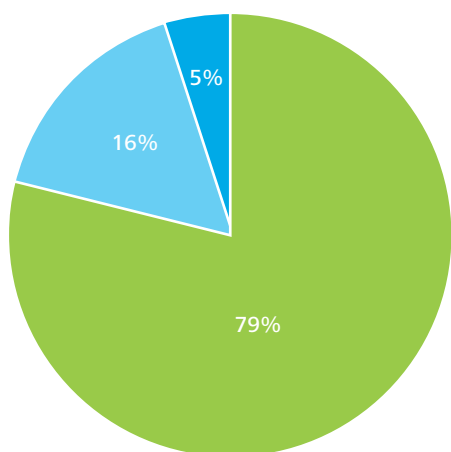
answer about their plans for the upcoming year is smaller than the equivalent share for the previous year.

Purchasing inventory



A considerable share of respondents (58 per cent) said they would increase expenditure on purchasing inventory. Growth from the previous year was 18 per cent. Slightly more than a quarter of companies (26 per cent) may be expected to take a "wait-and-see" stance with regard to long-term investment until the 2012 elections. The results of the elections should allow companies to confirm their long-term investment plans and enable such plans to withstand the risks from a possible second wave from the crisis. On the whole, however, the share of companies which plan to increase expenditure on purchasing inventories has gradually increased over the last three years.

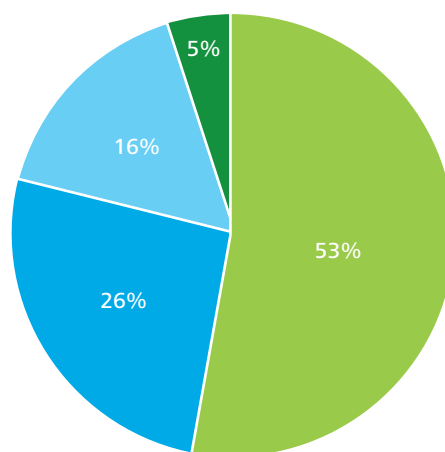
Field development



- Smaller-scale expansion
- No change
- Don't know

Compared with the previous year, the share of companies planning to increase investment in field development soared to 79 per cent, compared to 45 per cent in 2010. Only 5 per cent of respondents indicated that they had no plans to increase their spending on development. To comply with license obligations to the state, companies must invest in field development.

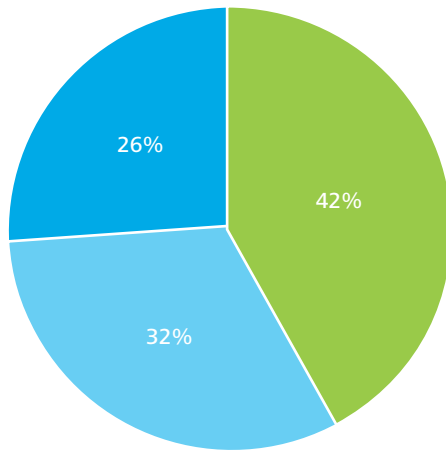
Up-stream



- Major expansion
- Smaller-scale expansion
- No change
- Don't know

As many as 58 per cent of companies are keen to increase spending on production, and 26 per cent plan to maintain spending levels from the year before.

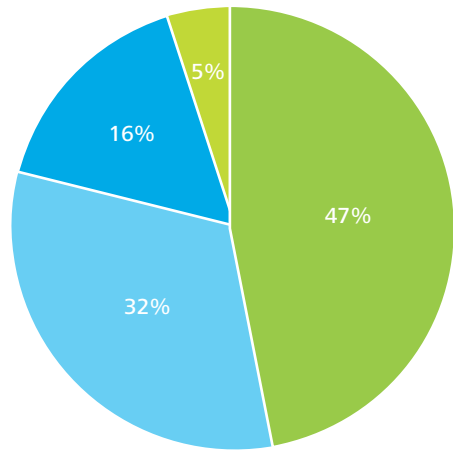
Mid-stream



- Smaller-scale expansion
- No change
- Don't know

Only 42 per cent of companies plan to invest more in refining, despite toughened quality requirements for petroleum products. As many as 32 per cent did not give a definite answer about their plans for the upcoming year, while 26 per cent are going to keep their spending on refining unchanged.

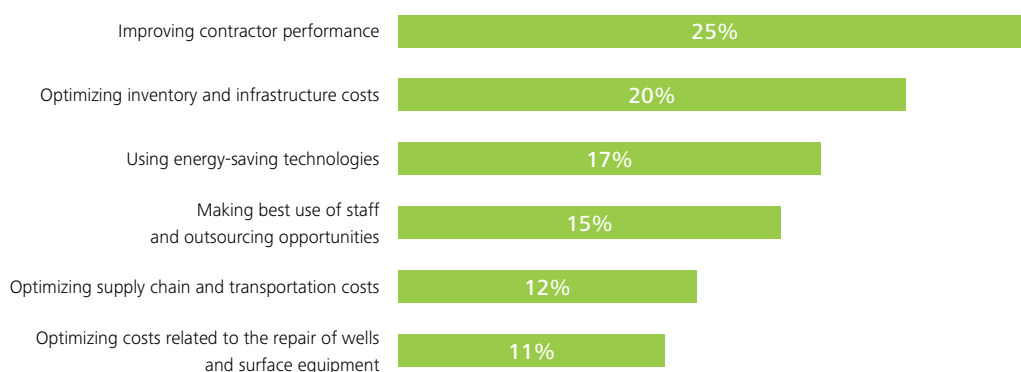
Down-stream



- Smaller-scale cutbacks
- Smaller-scale expansion
- No change
- Don't know

47 per cent of companies plan to invest more in developing their market sales, compared to 60 per cent the year before. 32 per cent of respondents did not give a definite answer on their sales expenditure for the upcoming year.

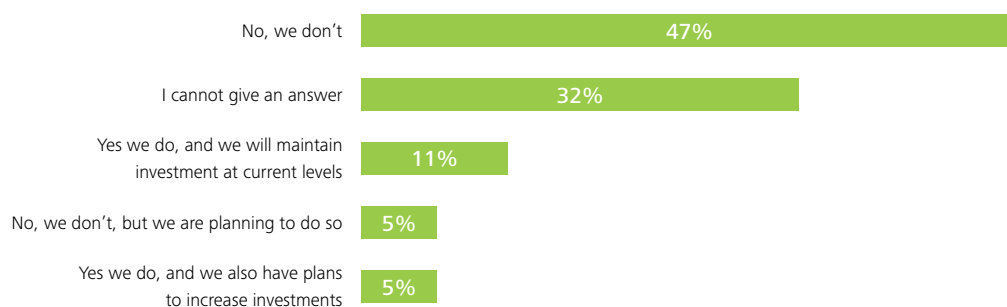
In 2012, what will be your company's approach to controlling/reducing operating expenses?



A quarter of respondents believe that improving contractor performance is the most effective measure for controlling and reducing operating expenses. Other popular methods include optimization of costs for logistics and infrastructure, and using energy-saving technologies (20 per cent and 17 per cent respectively). Making the most of internal staff and outsourcing

opportunities became less popular in comparison to the previous year (a decrease from 22 to 15 per cent), because many companies have already implemented projects for outsourcing certain functions to shared service centers, which allow for optimized headcount and staff and management costs.

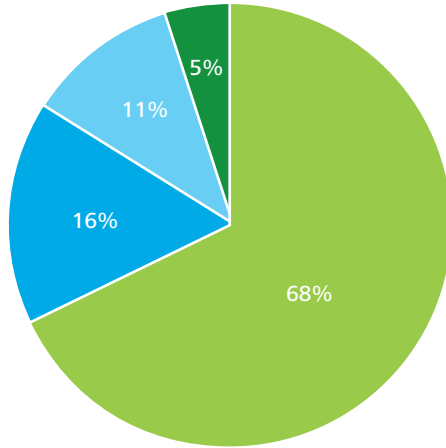
Do you invest in alternative energy research and development?



Depletion of resources, the increasing complexity of mineral extraction, and new environmental requirements are leading western energy companies to make considerable investments in alternative energy research and development. No such trend is observed among Russian companies, however. More than half of respondents are not making any such investments. Only

16 per cent of respondents spend funds on developing alternative energy resources (this figure decreased by almost one-half compared with the previous year), and 5 per cent plan to increase their spending. 32% per cent of respondents did not give an answer to this question.

How will the volume for exploration work change within the next 5 years?



- Significantly increase
- Increase
- Remain the same
- Don't know

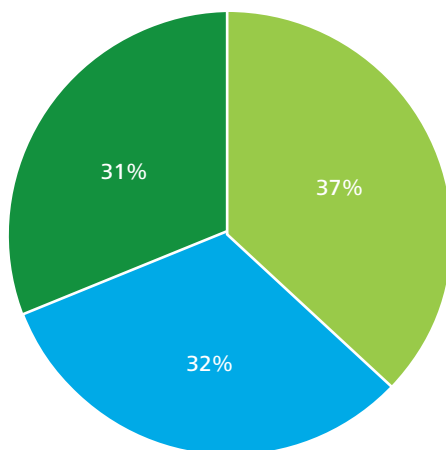
A considerable number of respondents (73 per cent) indicated an increase in the volume for geological exploration. The main reasons are the gradual decline in already discovered hydrocarbon sources and the necessity to fulfil license obligations. Relatively high oil prices and support initiatives from the state also provide incentives for companies to expand exploration activities.

Our respondents

We surveyed executives at various levels of seniority (senior executives, heads of divisions and departmental heads) who are engaged in hydrocarbon exploration, production and processing. The survey covers both

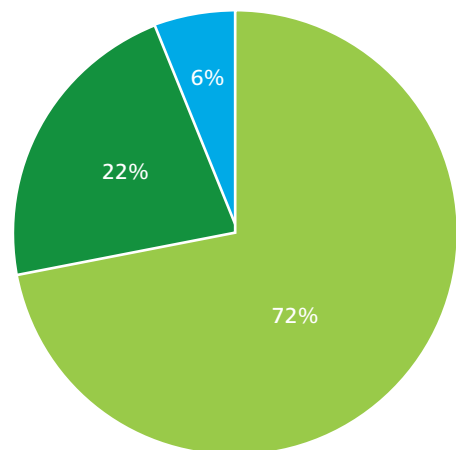
local and international vertically integrated companies of a large size and independent small and medium-size businesses.

Your company is:



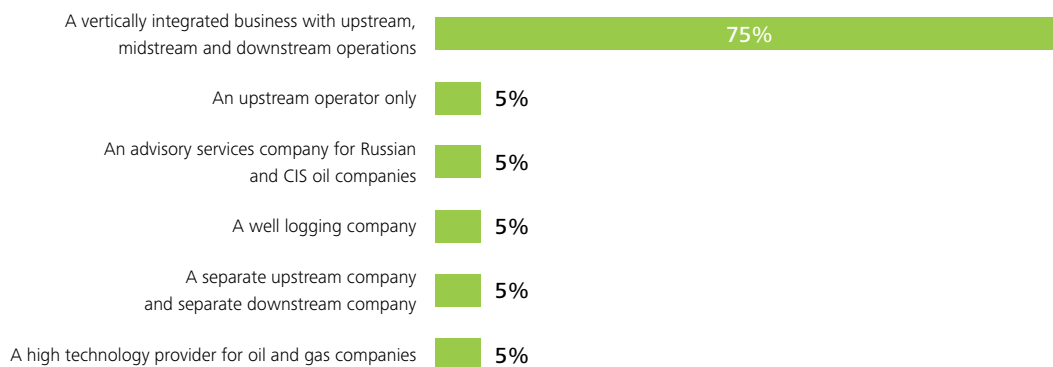
- A private company
- A public company
- A state-owned company

The consolidated annual revenue of your company is:

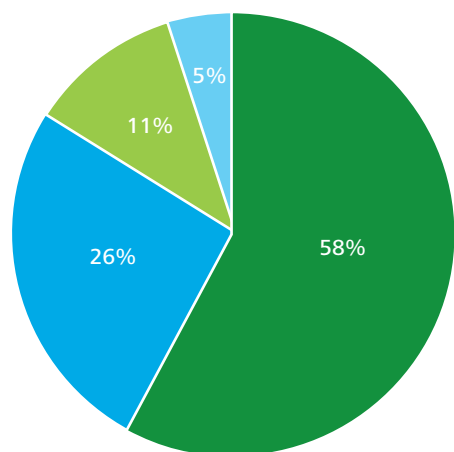


- Above USD 15 billion
- Between USD 1 billion and 15 billion
- Between USD 500 million and 1 billion

Which of the following business models applies to your company?

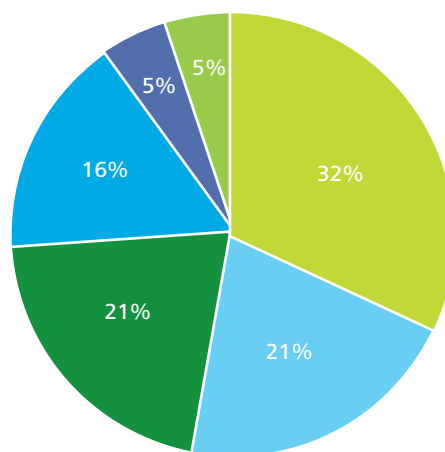


What is your position within the company?



- Senior management
- Managing director/head of division
- Head of business unit/manager
- Head of Russian branch

Your function within the company is:



- Senior management
- Strategic management
- Finance and planning
- Production operations (upstream, midstream, downstream)
- Business development
- IR

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2012 Russian Oil & Gas Outlook
Survey in the Energy & Resources
section at our site www.deloitte.ru.

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