Press Conference Background

GAZPROM IN EASTERN RUSSIA, ENTRY INTO ASIA-PACIFIC MARKETS

(June 18, 2014)

Gazprom continues implementing the projects under the state-run Development Program for an integrated gas production, transportation and supply system in Eastern Siberia and the Far East, taking into account potential gas exports to China and other Asia-Pacific countries (Eastern Gas Program).

Resource Base Buildup in Eastern Russia

At present, Gazprom carries out geological exploration offshore the Sakhalin Island, in the Republic of Sakha (Yakutia), the Irkutsk Region, the Krasnoyarsk and Kamchatka Territories.

Geological exploration was completed at the Kirinskoye field within the Sakhalin III project. In 2013, C1+C2 reserves of the Yuzhno-Kirinskoye field were significantly increased by 13 per cent – from 564 to 636.6 billion cubic meters through the drilling of two exploratory wells in the eastern part of the field. The recoverable reserves of gas condensate grew from 71.6 to 97.3 million tons. Besides, recoverable oil reserves in the amount of 6 million tons were discovered. The construction of two more exploratory wells is scheduled for 2014. Geological exploration goes on at the Mynginskoye field, the Vostochno-Odoptinsky and Ayashsky blocks of the project.

In 2013 the construction of exploratory wells at the Chayandinskoye field in the Republic of Sakha (Yakutia) was in progress. The geological exploration will be completed in 2015, and the final assessment of reserves will be carried out in 2016. 3D seismic survey at the Verkhnevilyuchanskoye Tas-Yuryakhskoye, Sobolokh-Nedzhelinskoye, and Srednetyungskoye licensed blocks will be conducted between 2014 and 2016.

Gazprom is developing the Kovyktinskoye and Chikanskoye fields as well as the Yuzhno-Ust-Kutsky licensed block in the Irkutsk Region. In 2013 the Kovyktinskoye Gas Condensate Field Development Plan was approved. In the same year one exploratory well was completed at the Chikanskoye field, the work is underway to determine efficient methods of hydrocarbons inflow stimulation. Exploratory wells construction and 3D seismic survey are scheduled at the fields from 2014 to 2016. Seismic survey is in progress at the Yuzhno-Ust-Kutsky licensed block.

Gazprom continues geological exploration of 16 licensed blocks at the Krasnoyarsk Territory.

3D seismic survey, design and preparation activities as well as drilling of prospecting and appraisal wells are planned within the Zapadno-Kamchatsky licensed block for the period until 2017.

Developing Production and Gas Transmission Capacities

The top-priority project of the Sakhalin gas production center is the development of the Kirinskoye field, where the first gas was produced in October 2013. Upon commissioning

of the second production well in 2014, the Primorye Territory and northern Sakhalin Region (Nogliki District) will receive gas supplies solely from this field starting from 2015.

Currently the Sakhalin – Khabarovsk – Vladivostok gas pipeline conveys gas from the Sakhalin II project (as a royalty) to the Primorye Territory customers and from the Sakhalin I project to the Khabarovsk customers.

On May 21, 2014 Gazprom and China National Petroleum Corporation signed a milestone contract for Russian pipeline gas supply to China. The 30-year contract stipulates that 38 billion cubic meters of Russian gas will be supplied annually. Natural gas will be delivered from the Yakutia and Irkutsk gas production centers via the Power of Siberia gas transmission system.

Design and survey activities are in progress as part of the Chayandinskoye field pre-development. Gas production is expected to start in 2018. In order to apply the membrane technology for the in-field helium extraction from natural gas at the fields of the Yakutia and Irkutsk gas production centers, the pilot testing of this technology is conducted at the Kovyktinskoye field.

Hydrocarbon Feedstock Processing

It is planned to create a gas processing and helium complex in the Amur Region, with gas from the Yakutia and Irkutsk gas production centers to become its resource base. The decision was made to implement the project using a project financing scheme. SIBUR Holding plans to set up a gas chemical facility near Gazprom's gas processing plant in the Amur Region. In November 2013 the companies signed a relevant memorandum in order to coordinate these projects.

Vladivostok LNG Project

In November 2013 Gazprom and the Primorye Territory Administration signed a Memorandum of Understanding and Cooperation within the project for an LNG plant construction in the Primorye Territory (Khasan District, Perevoznaya Bay). At present, project documents are being developed as part of Vladivostok LNG. In addition, design and survey operations are carried out at the proposed location of the LNG plant and surrounding infrastructure.

The Gazprom LNG Vladivostok project company (special-purpose company) was established in 2013 to implement the project.

Meanwhile, Gazprom is engaged in a dialogue on signing the relevant PSAs with potential LNG buyers.

Regional Gasification and Natural Gas Market Development

The gasification of the Primorye, Khabarovsk, Kamchatka Territories and the Sakhalin Region continues under the approved programs for gas supply to and gasification of the Far Eastern Federal District areas.

In the Primorye Territory the design and estimate documents are under development for four gas pipeline branches, a gas distribution station (GDS) and four inter-settlement gas pipelines.

In the Khabarovsk Territory investments will be made into the construction of two gas pipeline branches, a GDS and six inter-settlement gas pipelines as well as into the possible start of construction and installation activities for three inter-settlement gas pipelines. In addition, design operations were initiated for three gas pipeline branches, a GDS and six inter-settlement gas pipelines; plans were made to start designing two gas pipeline branches, a GDS and three inter-settlement gas pipelines.

Gazprom allocated investments for constructing in the Sakhalin Region a gas pipeline branch, a GDS, three inter-settlement gas pipelines and possibly launching the construction and installation activities at one gas pipeline branch, a GDS and three inter-settlement gas pipelines. Design and estimate documents are being developed for two gas pipeline branches, a GDS and five inter-settlement gas pipelines.

Investments are provided for the Kamchatka Territory to construct one gas pipeline branch, a GDS and three inter-settlement gas pipelines. In addition, it is planned to develop design and estimate documents for two gas pipeline branches, a GDS and five inter-settlement gas pipelines.

Sakhalin II Project

As of 2013 year-end, gas, oil and condensate production within the Sakhalin II project totaled 17.6 billion cubic meters, 3.72 million tons and 1.56 million tons respectively. 54 standard oil cargoes (5.41 million tons) and 166 standard LNG cargoes (10.76 million tons) were offloaded.

In 2013 LNG from the Sakhalin II project was supplied to Japan (8.67 million tons, with 0.45 million tons supplied by Gazprom Group), Korea (1.98 million tons / 0.13 million tons) and Taiwan (0.066 million tons).

In Q1 2014 a total of 4.9 billion cubic meters of gas, 1.0 million tons of oil and 0.43 million tons of condensate were produced; 15 standard oil cargoes (1.48 million tons) and 45 standard LNG cargoes (2.94 million tons) were offloaded.

In Q1 2014 LNG from the Sakhalin II project was supplied to Japan (2.27 million tons, with 0.064 million tons supplied by Gazprom Group), Korea (0.65 million tons) and China (0.064 million tons / 0.064 million tons).

The volume of gas supplied from the Sakhalin II project to consumers in the Primorye Territory and the Sakhalin Region in 2013 totaled 1.45 billion cubic meters, and in Q1 2014 – 0.51 billion cubic meters.

On February 23, 2014 Gazprom and Shell signed the Memorandum (roadmap) for the construction of the third LNG production train in Prigorodnoye settlement on the Sakhalin Island. The Memorandum envisages step-by-step decision making on the preparation of FEED and PDD documents.

Other LNG Projects

Rosneft jointly with the Sakhalin I project consortium declared the construction of another LNG plant in Sakhalin – Far East LNG with the annual capacity of 5 million tons of LNG.

In this context, attention should be given to the possibility of reaching certain synergies from using gas of the Sakhalin I Phase 2 in the Sakhalin II project through Gazprom's acquisition of this gas on an arm's length basis.

In addition, a certain amount of gas from the Sakhalin I Phase 2 may be channeled under the gas transmission contract with Rosneft via the Sakhalin – Khabarovsk – Vladivostok gas trunkline to supply the Eastern Petrochemical Complex of Rosneft in the Primorye Territory (currently Rosneft requests gas from Gazprom to implement this project).

This comprehensive decision will duly meet the interests of the Russian Federation as the party to the Production Sharing Agreement, as it mitigates the aggregate recoverable costs for the Sakhalin I project.

Measures of State Support for Eastern Gas Program

Gazprom goes on cooperating with the Russian Government with a view to develop the practical measures of state support for projects in Eastern Siberia and the Far East in terms of tax incentives and customs & tariff benefits as well as building external infrastructure ahead of schedule.

Some of the required laws have already been adopted. Thus, Federal Laws No. 263-FZ and 268-FZ dated September 30, 2013 secure severance tax benefits for gas and gas condensate from the fields of the Irkutsk Region, the Krasnoyarsk Territory, the Far Eastern Federal District and the Sea of Okhotsk. In addition, Federal Law 268-FZ stipulates tax exemption for certain types of corporate property located in the Russian continental shelf as well as exclusion of offshore stationary and floating platforms, mobile offshore drilling rigs and drilling vessels from the list of assets subject to transport tax.

However, the provided tax incentives do not fully consider the specifics of development operations in Eastern Siberia and the Sea of Okhotsk. Gazprom is taking further steps in this direction.

Additional state support is required in the tax and customs & tariff regulation area (primarily profit tax relief and corporate property tax relief) that would make it possible to reduce the tax burden on major projects of oil and gas producing companies in Eastern Russia, as well as increase the investment attractiveness of the region.

Gazprom also plans to go on working with the Russian Federal Tariff Service on improving natural gas pricing mechanisms in Russia's eastern regions.

State support is also important to ensure outstripping creation and financing of external infrastructure facilities in Eastern Siberia and the Far East.

Thus, the Russian Federation Government Directive No. 308 dated April 15, 2014 approved the state-run Program for Socioeconomic Development of the Far East and the Baikal Region. The relevant special federal programs and a subprogram were devised within the said Program. However, the current version of the document leaves out a whole range of measures required for creating the efficient external environment of the macroregion. For example, it is vitally important to timely finance the Vilyui motor road planned to be completed by late 2016 and the M-58 Amur and M-60 Ussuri motor roads should be kept in good condition.

The timely implementation of the Vladivostok LNG project also requires an upgrade and expansion of the A-189 motor road at the Ussuriysk – Slavyanka section to be used for supplying cargoes during the plant construction to the Perevoznaya Bay (Lomonosov Peninsula, Khasan District, Primorye Territory). These measures are to be included into the state-run Program.

In addition, state incentives are required for:

- establishing the national carrier fleet for hauling liquid helium (tank trucks), R&D activities to design railway tanks for shipping liquid helium;
- developing innovative helium-consuming plants in Russia;
- developing Far East shipyards producing marine vessels of different classes, including LNG carriers as well as offshore oil production equipment, offshore platforms and subsea production systems.

It is also necessary:

- to maintain the unified channel for Russian gas export via pipelines;
- for Gazprom to achieve a single gas balance for the Sakhalin projects with the account of supply to the domestic and international market, inter alia, through acquisition of gas from Phase 2 of the Sakhalin I project on an arm's length basis;
- to work out the helium export mechanism aimed at ruling out the competition among Russian producers in helium sales from international markets by means of granting Gazprom the status of an authorized special-purpose company.

The constituent entities of the Far Eastern Federal District of the Russian Federation also require state financial support in order to fulfill their obligations on preparing consumers for gas supply within regional gasification programs to the full extent and in due time.

Gas Export in Eastern Russia

Maintaining the unified channel of Russian gas export via gas pipelines both westwards and eastwards meets the long-term objectives of Russia's socio-economic development, as it rules out the competition among Russian suppliers in the international markets and provides for maximum export revenues and tax returns.

Arranging Russian natural gas supply to the Asia-Pacific via gas pipelines in the first place consists in implementing projects for natural gas export to the People's Republic of China via the eastern (contract signed in May 2014) and western (Gazprom is to start negotiations in the near future) routes. All in all, LNG supply dominates the Asia-Pacific Region and accounts for 87 per cent of the market.

The arguments of independent gas producers in favor of liberalizing pipeline export to the Asia-Pacific are based on improperly overestimated forecasts of the gas demand growth in China and unfounded forecasts of production opportunities in the region disregarding profitability indices of developments and gas transportation from certain fields to the target markets.

Nowadays, the countries of Northeast Asia also largely favor the implementation of numerous separate projects for pipeline gas and LNG supply to the Asia-Pacific region with a view to exert the price pressure on suppliers in future. In the Asian importers' opinion, this process will lead to equalizing the level of gas prices for Europe and Asia.

In this context, the main factor for launching the supplies and providing well-founded forecasts of gas supply volumes to China is the gas price.

Due regard should also be paid to the high capital capacity of future projects for developing the fields of Yakutia and Eastern Siberia, regarded as the basis for arranging gas supply to China via the eastern route. It concerns the high gas production cost, the necessity of concurrently creating gas processing capacities as well as considerable construction costs of gas transmission infrastructure facilities.

In addition, it should be kept in mind that the natural gas market of Northeast China is currently at its initial stage of development. This means that the Chinese party has to make substantial investments into setting up gas distribution and use infrastructure facilities there. Consequently, this determines China's stage-by-stage approach to reaching the contracted gas supply volume.

In case China is ready to increase the purchase of Russian natural gas at fair prices, Gazprom's resource base provides an opportunity to considerably raise supply both via the eastern route and also arrange the supply of required gas volumes via the western route. It should also be pointed out that the Chinese party has chosen a single importer of Russian gas via pipelines.

At present, there is no adequate estimate of possible gas volumes produced by independent companies as they do not have the approved project documents for developing such fields.

Unlike Gazprom's fields in the Yakutia and Irkutsk gas production centers, the fields of independent producers are much less prolific, have lower density of reserves, low exploration degree and require full-scale geological exploration, which poses certain risks to meeting their commercial development schedules and possibly including them into the mid-term gas balance.

The volumes of gas from independent producers may be considered as possible export supplies only when full-scale geological exploration is completed at these fields. Reserves should be converted to the commercial category and project documents for field development should be approved. Integrated feasibility study should be completed with the account of costs for field pre-development, gas treatment in compliance with the existing regulatory documents and for the construction of extensive pipeline connectors to gas trunklines.

Gazprom is ready to purchase third-party APG volumes to deliver them to the eastern part of the Unified Gas Supply System, which is currently under construction. In addition, being the Eastern Gas Program coordinator, Gazprom will maintain interaction with independent producers to consider the possibilities of purchasing natural gas as part of the efforts aimed at creating a single long-term balance of the region.