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The review provides a detailed analysis of main trends in Russian economy in 2016. The paper contains 6 big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and budget spheres; financial markets; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts.

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4.5. Russian oil and gas sector in 2016[1]

The oil and gas sector is among principal sectors of the Russian economy and is the driving force in shaping the state budget revenues and the trade balance. In 2016, Russia's crude oil production hit an all-time peak since 1990, and crude oil exports were close to an all-time high. Under the so-called tax maneuver in force in the oil industry, refining depth went up noticeably, production and export of fuel oil moved down and export of crude oil, a highly lucrative source of the budget revenues, increased.

4.5.1. Dynamics of global crude oil and gas prices

The recent steady supply glut in the world oil market has led to a significant decline in crude oil prices. Growing production of shale oil in the U.S. owing both to introduction of new extraction technologies and to high crude prices were main factors for the world crude oversupply. In this context, OPEC opted not to cut its production quota and de facto launched a policy of retaining its global market share. Subsequently, the price of Russian Urals crude oil dropped to an average of $51.2, and to $41.9 per barrel in 2016 (*Table 21*). This being said, the price dipped to $28.8 per barrel in January 2016 (*Fig. 27*).

Table 21

World crude oil prices in 2010–2016, USD/bbl

	2010	2011	2012	2013	2014	2015	2016
Brent crude oil, Great Britain	79.6	111.0	112.0	108.8	98.9	52.4	44.0
Urals crude oil, Russia	78.3	109.1	110.3	107.7	97.7	51.2	41.9
Russian gas on European market, USD/thousand cub m	296.0	381.5	431.3	402.0	376.0	267.9	156.7

Sources: IMF, OECD/IEA, Rosstat.

Under the impact of low crude oil prices seen in 2016, the oil sector faced scaling back of oil production on cost-intensive deposits, first of all, on light tight oil deposits in the U.S. Investments in the most cost-intensive non-conventional deposits of oil in the U.S., tar sands in Canada and deepwater field in various parts of the world dipped significantly. At the same time, decrease of oil production in cost-intensive regions was actually offset by OPEC's growing production striving to widen its market share.

Low crude oil prices promote expansion of their global market share for those countries whose revenues decisively depend on crude oil exports. By increasing crude oil shipments, those countries try to offset contraction of the revenues due to price decline. Consequently, OPEC member states constantly exceed their production quota.

[1] Author of chapter: Yu. Bobylev – Gaidar Institute, RANEPA.

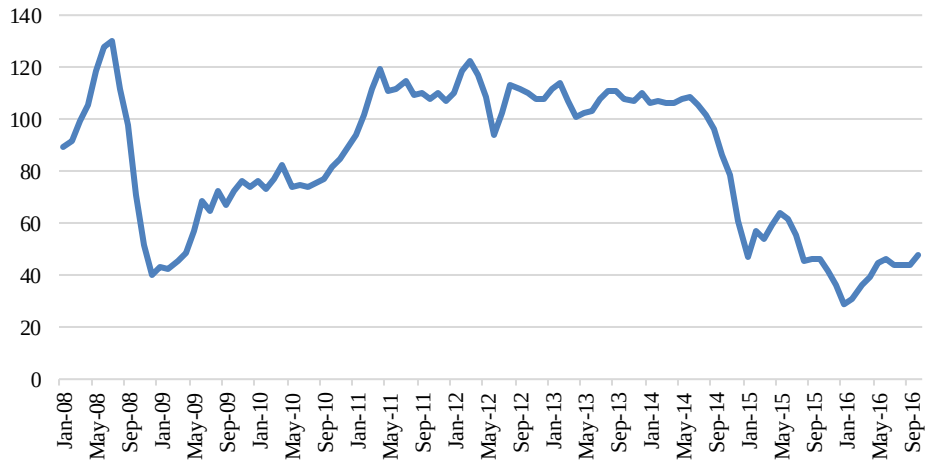

Fig. 27. Urals crude oil price in 2008–2016, USD/bbl.

Sources: OECD/IEA.

Saudi Arabia, the biggest OPEC producer, significantly built up crude oil production over the last two years. Main contribution in growing oil supply by OPEC in 2015 was attributed to Iraq, and in 2016 to Iran, which received an opportunity to increase oil shipments owing to lifting of sanctions. Consequently, growing oil production seen in Iran in 2016 totally offset decrease of oil production in the U.S.

Falling oil prices impelled oil-producing countries to curtail output volumes. In late 2016, OPEC and a number of non-OPEC producers, including Russia, reached a deal to cut oil output from January 1, 2017. According to the deal, OPEC producers (13 countries) were committed to slash their production by 1.2 mn barrels per day, and non-OPEC 11 producers – by 558 thousand barrels per day, including Russia - by 300,000 bbl/d.

Russian natural gas prices have also dropped on foreign market. Long-term contract prices, as a rule, are linked to petroleum products prices and follow with a certain lag global oil prices. At the same time, changes at the European gas market, which happened in recent years, which materialized in increased supply of gas by other gas producers and lower spot prices on gas in comparison with long-term contract prices offered by Gazprom exerts downward pressure on Russian gas selling prices. In 2015, Russian gas price declined by 29% on European market compared with the previous year and by 41.5% in 2016.

4.5.2. Dynamics and structure of production in oil and gas sector

Russia's crude oil output dynamics stood positive despite falling oil prices and enforcement of financial and technology-related sanctions (*Table 22*). In 2016, it hit an all-time high of 549 million tons since 1990. Crude oil extraction was positively affected by investment, ruble's devaluation, which reduced expenses of oil companies in dollar terms and ensured efficiency of their operations amid low oil prices. It was also positively influenced by putting into operation of several new large oilfields, as well as tax system updates, which facilitated the development of new oil producing areas and the upgrade of producing oilfields.[1] In the

[1] See: Yury Bobylev. Development of the Oil Sector in Russia. Voprosy Ekonomiki. 2015. No6, pp. 45–62; Bobylev Yu.N., Rasenko O.A. Russian Oil Sector: main trends. Moscow, Delo Publishers. RANEPA, 2016.

meantime, production conditions are deteriorating. Significant part of producing oilfields has entered a declining production stage and new oilfields in the majority of cases have inferior mining-and-geological and geographical factors. Their development required higher investment, exploitation and transportation costs. In order to offset oil output plunge at producing oilfields, it is necessary to develop both new oilfields in areas with underdeveloped or lacking infrastructure and in extracting reserves of inferior quality in developed areas.

Table 22

Production and refining of crude oil in Russia in 2010–2016

	2010	2011	2012	2013	2014	2015	2016
Extraction of crude oil including gas condensate, m t	505.1	511.4	518.0	523.3	526.7	534.0	547.6
Primary crude oil refining, m t	249.3	258.0	270.0	278.0	294.4	287.2	284.5
Share of crude oil refining in crude production, %	49.4	50.4	52.1	53.1	55.9	53.8	52.0
Crude oil refining depth, %	71.1	70.8	71.5	71.7	72.4	74.4	79.1

Sources: Federal State Statistics Service (Rosstat), Russian Energy Ministry.

2016 demonstrated that the so called tax maneuver in force in the oil industry – a structural tax reform in this sector envisages stepwise reduction of export duties on both crude oil and petroleum products, as well as a higher mineral extraction tax (MET).[1] According to adopted parameters of the so-called tax maneuver, marginal oil export duty rate was cut from 59% in 2014 to 30% in 2017, and fuel oil export duty rate was raised from 66% to 10% from the oil export duty rate.[2] This transformational change of the tax system has offered incentives for upgrading oil refining capacities and led to a change of a number of existing trends.

New trends emerged in 2015–2016, and some of them deserve to be mentioned here: first, oil refining depth increased notably as output and exports of fuel oil declined, second, crude oil exports growth more lucrative for state budget revenues than fuel oil exports, third, crude oil refining decline in volume terms owing to the two above factors (*Table 23*).

In 2016, oil refining depth hit Russia's all-time high of 79.1%. Note, that in the period of 2000–2014, that is, during a long period until the "tax maneuver" took force, depth of oil refining in Russia constituted 71–72%, while it stood at 75.0% in 2015 (by contrast, this indicator comes to 90–95% in leading industrial countries).

Table 23

Production of crude oil, petroleum products and natural gas in 2010–2016, in % to the previous year

	2010	2011	2012	2013	2014	2015	2016
Crude oil including gas condensate	102.1	100.8	101.3	100.9	100.7	101.4	102.5
Primary oil refining	105.5	103.3	104.9	102.7	104.9	97.3	98.7
Motor gasoline	100.5	102.0	104.3	101.3	98.8	102.3	101.9
Diesel fuel	104.2	100.3	98.7	103.1	107.4	98.9	100.2
Fuel oil	108.5	104.6	101.6	103.3	102.0	91.1	80.2
Natural gas	111.4	102.9	97.7	102.1	95.7	98.7	101.0

Sources: Federal State Statistics Service, Russian Energy Ministry.

2016 saw a consolidation of state assets in the oil sector resulting from a state-controlled oil firm Rosneft buying controlling stake in Bashneft, another state-controlled oil firm. Rosneft market share has significantly grown because of this deal. In 2016, the share of Rosneft (with

[1] See: Bobylev Yu. N., Idrisov G.I, Sinelnikov-Murylev S.G. Export Duties on Oil and Petroleum Products: Cancel Expediency and Scenario Analysis. Moscow, Gaidar Institute Publishers, 2012.
[2] See: Yu. Bobylev. Tax Maneuver in the Oil Sector. Russian Economic Development. 2015. No 8, pp. 45–49.

Bashneft) in the total Russian crude oil production hit 38.6%. Correspondingly, the portion of major Vertically Integrated Oil Companies on the market went up significantly: five major companies' (Rosneft, LUKOIL, Surgutneftegaz, Gazprom, and Tatneft) proportion accounted for 80.4% of crude oil output in 2016 (*Table 24*). Segment of small and medium-size oil companies remains relatively underdeveloped. Companies with 2.5 m t of crude oil production (roughly 50,000 barrels per day) account for solely 3.0% of Russia's crude oil output. (By contrast, in the U.S. the sector of small and medium-size oil companied demonstrated efficiently. The share of companies producing up to 50,000 barrels per day account for 46% of the overall crude oil output).

Table 24

Major Russian oil producing companies in 2010–2016

	Oil output in 2010, m t	Share in total output, %	Oil output in 2015, m t	Share in total output, %	Oil output in 2016, m t	Share in total output, %
Rosneft	112.4	22.3	189.2	35.4	211.1	38.6
LUKOIL	90.1	17.8	85.7	16.0	83.0	15.2
TNK-BP	71.7	14.2	-	-	-	-
Surgutneftegaz	59.5	11.8	61.6	11.5	61.8	11.3
Gazprom including Gazprom neft	43.3	8.6	51.3	9.6	55.2	10.1
including: Gazprom	13.5	2.7	17.0	3.2	17.4	3.2
Gazprom neft	29.8	5.9	34.3	6.4	37.8	6.9
Tatneft	26.1	5.2	27.2	5.1	28.7	5.2
Bashneft	14.1	2.8	19.9	3.7	-	-
Slavneft	18.4	3.6	15.5	2.9	15.0	2.7
RussNeft	13.0	2.6	7.4	1.4	7.0	1.3
NOVATEK	3.8	0.8	4.7	0.9	8.0	1.5
PSA operators	14.4	2.9	15.0	2.8	16.0	2.9
Other producers	38.2	7.6	56.5	10.6	61.7	11.3

Sources: Russian Energy Ministry, own calculations.

Economic sanctions enforced in 2014 remained in place in 2016. Besides enforced finance-related sanctions, which restrict access of Russian oil and gas companies to foreign sources of financing, a number of developed countries introduced sweeping restrictions on shipments of exploration and production equipment and technologies in connection with deepwater, Arctic shelf, and shale oil and gas projects in Russia. All these projects critically depend on foreign oil and gas related technologies. Regarding the implementation of Arctic shelf and deepwater projects with long-term investment cycle, the negative impact from imposed sanctions can pop up in long-term perspective. Implementation of the majority of these projects is being put off due to their economic failure in the wake of low crude oil prices.

Development of the majority of Russian shale-oil deposits is also unprofitable in the context of low crude oil prices. However, technologies for the development of shale formations (horizontal drilling, hydraulic fracturing) are used in the development of traditional producing oil deposits, first of all, on the deposits with high level of reserve depletion.

It should be noted that there is a rather significant potential for additional output on the producing oilfields due to their more intensive development. Russia's oil recovery factor comes roughly to 28%, which is significantly less than the average world rate (by contrast, in the U/S/ this rate is in the range of 35-43%, in Norway—46%). In the wake of low global crude oil prices and enforced technology related sanctions, the development of extensively depleted fields by

raising the production efficiency is of high importance for keeping oil production and export edge.

4.5.3. Dynamics and structure of oil and gas export

In 2016, Russia's exports of crude oil and petroleum products constituted 410.8 m tons, close to the all-time high of 2015. It should be noted that 2016 saw a notable growth of 4.2% of crude oil exports spurred by the so called tax maneuver and a 9.0% decline in exports of petroleum products mainly owing to a fall of fuel oil exports (*Tables 25* and *26*). The proportion of crude oil in the total oil exports constituted 62.0%, petroleum products—38.0%. This being said, the share of exports in the production came to 63.8%, in production of motor gasoline – 13.0% (by contrast, in 2010, the share of exports of motor gasoline in production of motor gasoline came to 8.2%, in 2015 – 12.1%).

Table 25

Ratio of production, consumption and exports of crude oil and natural gas in 2010–2016

	2010	2011	2012	2013	2014	2015	2016
Crude oil, m t							
Production	505.1	511.4	518.0	523.3	526.7	534.0	547.6
Exports, total	250.4	244.6	239.9	236.6	223.4	244.5	254.8
Exports to non-CIS countries	223.9	214.4	211.6	208.0	199.3	221.6	236.2
Exports to CIS countries	26.5	30.2	28.4	28.7	24.1	22.9	18.6
Net exports	249.3	243.5	239.1	235.8	222.6	241.6	254.0
Domestic consumption	125.9	140.7	142.1	137.5	141.3	122.2	138.3
Net exports as % of production	49.4	47.6	46.2	45.1	42.3	45.2	46.4
Petroleum products, m t							
Exports, total	132.2	130.6	138.1	151.4	164.8	171.5	156.0
Exports to non-CIS countries	126.6	120.0	121.2	141.1	155.2	163.3	148.1
Exports to CIS countries	5.6	10.6	16.9	10.3	9.6	8.3	8.0
Net exports	129.9	127.2	136.8	150.0	162.8	170.2	155.3
Crude oil and petroleum products, m t							
Net exports of crude oil and petroleum products	379.2	370.7	375.9	385.8	385.4	411.8	409.3
Net exports of crude oil and petroleum products as % of crude oil extraction	75.1	72.5	72.6	73.7	73.2	77.1	74.7
Natural gas, bn cu m							
Production	665.5	687.5	671.5	684.0	654.2	645.9	652.6
Exports, total	177.8	184.9	178.7	196.4	172.6	185.5	198.7
Exports to non-CIS countries	107.4	117.0	112.6	138.0	124.6	144.7	164.7
Exports to CIS countries	70.4	67.9	66.0	58.4	48.0	40.7	34.0
Net exports	173.5	179.2	171.6	189.3	165.5	178.4	189.8
Domestic consumption	492.0	508.3	499.9	494.7	488.7	467.5	462.8
Net exports as % of production	26.1	26.1	25.6	27.7	25.3	27.6	29.1

Sources: Federal State Statistics Service, Russian Energy Ministry, Federal Customs Service, own calculations.

Natural gas exports went up by 7.1% in comparison with the previous year. This being said, natural gas exports to far abroad countries hit an all-time record in 2016. However, due to a decline of gas shipments to CIS countries, the total gas exports failed to achieve the level of mid-2000s. Gas net export ratio in natural gas production came to 29.1% in 2016.

Analysis of Russia's crude oil exports over the course of a long period demonstrates a significant increase in the export-led component of oil industry compared to the pre-reform period.

Table 26

Dynamics of exports of crude oil, petroleum products and natural gas in 2010–2016, in % to previous year

	2010	2011	2012	2013	2014	2015	2016
Crude oil	101.2	97.6	98.2	98.6	94.4	109.4	104.2
Petroleum products	106.2	98.5	104.4	109.6	108.7	104.1	91.0
Natural gas	105.6	104.0	96.6	109.9	87.9	107.5	107.1

Sources: Federal State Statistics Service, Federal Customs Service.

The share of net exports of crude oil and petroleum products in crude oil production went up from 47.7% in 1990 to 74.6% in 2016. This, however, is due not only to the increase in absolute volumes of exports but to market transformation of the Russian economy, more efficient oil consumption and the replacement of petroleum products (fuel oil) by natural gas.

The share of fuel and energy products in Russian exports fell from 69.5% in 2014 to 62.9% in 2015, and 58.1% in 2016, in response to a plunge in global crude oil and natural gas prices. In the meantime, the share of crude oil and petroleum products in Russian exports contracted, from 54.2% in 2014 to 41.6% in 2016. The share of natural gas in Russian exports constituted 11.0% in 2016 (*Table 27*).

Table 27

Fuel and energy products export value and ratio in 2010–2016

	2010		2014		2015		2016	
	USD bn	%*	USD bn	%*	USD bn	%*	USD bn	%*
Fuel and energy products, total	267.7	67.5	345.4	69.5	216.1	62.9	166.0	58.1
Including crude oil	134.6	34.0	153.9	31.0	89.6	26.1	73.7	25.8
Natural gas	47.6	12.0	54.7	11.0	41.8	12.2	31.3	11.0

* In % to total volume of Russian exports.
Source: Federal State Statistics Service.

4.5.4. Domestic price dynamics on energy products

The pricing mechanism for crude oil in the Russian domestic market is based on equal-netback pricing, that is, prices are equal to the world price less export duty and export transportation costs. The domestic price went up due to growing global crude oil and petroleum products prices. However, in second half of 2014–2016, the domestic price in dollar terms declined too, owing to a tumbling global crude oil price (*Table 28*, *Fig. 28*). At the same time, there is still a wide gap between world and domestic oil price due to high export duty. In the meantime, a convergence of international and domestic prices is observed owing to a lower rate of export duty envisaged as part of the tax maneuver. In 2014, the domestic price constituted 42.0% of the global price, while it was 61.0% in 2016.

Table 28

Domestic prices on crude oil, petroleum products and natural gas in 2010–2016 (average producer price at year end, USD/t)

	2010	2011	2012	2013	2014	2015	2016
Crude oil	248.2	303.3	341.1	346.1	178.9	156.7	207.8
Motor gasoline	547.9	576.9	628.7	614.4	372.3	301.8	380.3
Diesel fuel	536.1	644.9	774.2	698.0	419.3	349.4	421.3
Fuel oil	246.3	274.6	275.3	235.8	128.7	49.5	129.7
Gas, USD/thousand cum	20.5	21.3	40.3	39.8	29.1	24.5	23.6

Sources: own calculations based on data released by Rosstat.

Domestic gas prices are under the state regulation. The government maintains a significantly lower level of domestic gas prices in order to preserve a competitive edge of the national

economy. At the same time, certain convergence between domestic and world price on gas was observed as a result of a significant reduction of global gas price in 2016. In 2015, domestic gas price (purchase price by industrial consumers less indirect taxes) averaged roughly 26% of Russian gas price on European market, while in 2016 – 40.8%.

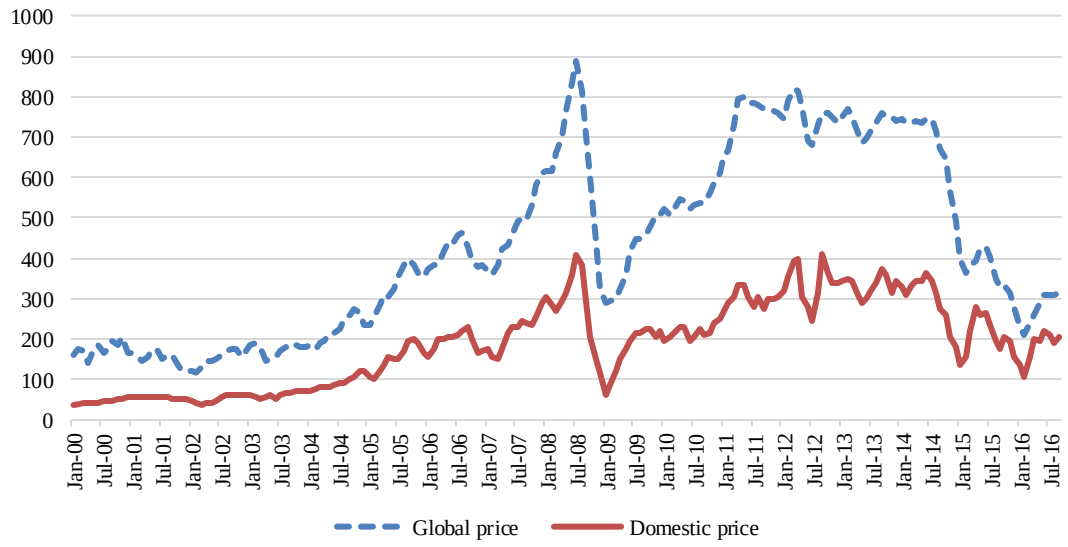

Fig. 28. Global and domestic oil prices in 2000–2016, USD/t

Sources: Rosstat, own calculations.

Motor gasoline prices continued the uptrend momentum in the domestic market despite a significant decline of global crude oil prices (*Table 29*). It primarily stemmed from the ruble's devaluation and increased excises on petroleum products. Producers price their petroleum products so that the price assures a profitability equal to that of exports: the global (tax-free) price on a given product less export duty and export transportation costs (netback price). Domestic consumer pricing for motor gasoline is based on producer prices (netback prices) adjusted for indirect taxes (excises, VAT) and trade increment. Russian producer gasoline prices in dollar terms tumbled, too, amid descending world oil prices. In the meantime, significant depreciation of the ruble against the dollar and growth of excises stemmed an increase in the ruble-denominated consumer price of motor gasoline (*Fig. 29*).

Table 29

Consumer prices on gasoline in Russia in 2014–2016 RUB/l

	2014 January	2015 January	2016 January	2016 July	2016 December
Regular unleaded gasoline	29.53	32.35	33.86	35.13	35.28
Gasoline 95 octane	32.64	35.16	36.81	38.14	38.34

Source: Rosstat.

Table 30

Excise rate on motor gasoline in 2014–2016 RUB/t

	2014	2015	2016 January-March	2016 April-December
Grade 4	9916	7300	10500	13100
Grade 5	6450	5530	7530	10130

Source: RF Tax Code (2014–2016 ed.).

Existing structure of gasoline consumer price against leading industrial countries is characterized by data given in *Table 31*. European countries have high gasoline prices and the highest tax burden on petroleum products. According to our calculations, the share of indirect taxes in the consumer price of gasoline is 35-43%[1] in Russia, whereas it is 65% in EU5 countries (Germany, France, Great Britain, Italy, and Spain), and 20% in the USA. Thus, regarding the tax burden on petroleum products, Russia ranks in the middle between EU5 and the USA, and it is close to Canada, another oil exporter.

Fig. 29. Consumer price in ruble and dollar terms on regular unleaded gasoline in 2008–2016

Sources: Rosstat, own calculations.

Table 32 provides data as of the beginning of 2014, which gives outlook prior to the fall of crude oil prices and ruble's devaluation. They represent a significant increase of the tax burden in gasoline price during recent two years. According to our calculations, the share of taxes in the consumer price of gasoline went up from 30–40% in 2014 to 35–43% in 2016. The share of taxes in the end consumer price went up on average across leading EU5 from 58 to 65%, and in the USA – from 13 to 20%. It is largely explained by that fact that amid lower gasoline price the share of taxes collected according to specific rates goes up.

Table 31

[1] See: Yu. Bobylev. Gasoline prices in Russia and other countries: comparative analysis. Russian Economic Development. 2016. No. 10, pp. 28-31.

Structure of consumer price on motor gasoline in Russia and other countries, July 2016

	Consumer price, USD/l	Taxes on consumers, USD/l	Prices less taxes, USD/l	Share of taxes in consumer price, %
Regular unleaded gasoline				
Russia	0.524	0.225	0.299	42.9
USA	0.583	0.119	0.464	20.4
Canada	0.791	0.294	0.497	37.2
Japan	1.191	0.634	0.557	53.2
Premium gasoline 95 octane				
Russia	0.569	0.199	0.370	35.0
Germany	1.471	0.962	0.509	65.4
Great Britain	1.472	1.009	0.463	68.5
France	1.454	0.963	0.491	66.2
Italy	1.616	1.100	0.516	68.1
Spain	1.291	0.738	0.553	57.2
Average across EU5	1.461	0.954	0.506	65.3

Sources: OECD/IEA; Rosstat; own calculations.

Table 32

Taxes on motor gasoline in Russian and other countries: share of taxes in gasoline consumer price, %

	2014 January	2016 July
Regular unleaded gasoline		
Russia	40.1	42.9
USA	12.7	20.4
Canada	31.7	37.2
Japan	40.0	53.2
Premium gasoline 95 octane		
Russia	29.9	35.0
Germany	58.7	65.4
Great Britain	61.3	68.5
France	57.5	66.2
Italy	60.3	68.1
Spain	50.7	57.2
Average across EU5	57.7	65.3

Sources: own calculations based on data released by OECD/IEA and Rosstat.

Gasoline prices in Russia are approaching the US prices, reaching 90% of the American level stemming from lower taxes in gasoline prices and such tax burden. Furthermore, they remain significantly lower than in other developed economies: 66% less than prices in Canada, 44% less than in Japan, and 39% less compared to EU5 countries (*Table 33*). One can note a somewhat decline in relative gasoline prices in Russia compared to developed economies during last two years. For example, Russian gasoline price declined from 96% in 2014 to 90% against the USA, and from 44% to 39% against leading EU5.

Table 33

Consumer prices on motor gasoline in Russia against other countries, %

	2014 January	2016 July
USA	95.8	89.9
Canada	72.9	66.2
Japan	55.0	44.0
Germany	44.4	38.7
Great Britain	43.3	38.7
France	45.3	39.1
Italy	39.5	35.2
Spain	48.7	44.1
EU5	44.1	38.9

Source: own calculation based on the data released by OECD/IEA and Rosstat.

Thus, current regime of export duties and taxes on petroleum products in Russia assure lower prices on motor fuel on the domestic market compared to developed countries.

4.5.5. Prospects for Russian oil and gas sector

Russia disposes of significant oil resources, which allow maintaining high levels of production and export in many years to come. There is a high potential for crude oil extraction owing to both undeveloped deposits in undeveloped areas and oilfields in new producing areas. At the same time, there is a rather significant potential for additional extraction on already producing oilfields thanks to an in-depth development. Moreover, Russia disposes of extensive currently undeveloped unconventional oil reserves including shale oil. The oil refining capacity is important. Upgrade of the oil refining depth allows satisfying domestic demand in motor gasoline with relatively lower volumes of oil consumption.

In future, global demand for oil will grow, which will allow Russia to retain and even to increase current volumes of crude oil exports. This being said, shifts in the regional structure of global oil demand prompt diversification of crude oil exports, expansion of shipments to the East.

Meanwhile, potential of the Russian oil sector development to a significant degree will rely on the world oil prices. The oil market outlook is marked by factors, which will be contributing to the retention of relatively low oil prices. The most important factors are extensive shale oil reserves in the U.S., which will be rapidly put into production and create oil glut with global oil price above USD 60 per barrel and slowdown of economic growth in China.

In the context of low crude oil prices, options for the development of new oilfields and unconventional reserves will be significantly restricted in Russia because investment in the cost demanding projects will be unprofitable (first of all, it is true to the implementation of the Arctic shelf projects). In the circumstances, conventional oil reserves located onshore will be the basis for further development of the Russian oil sector. In-depth development of producing oilfields and increase of the oil recovery rate are of major importance. Options for additional oil production at such oil fields will largely depend on technological progress, development of import substitution aimed at increasing the oil recovery index.

Further development of the oil sector will require necessary tax conditions.[1] First, it is necessary to accomplish structural reform of the taxation system in this sector, which includes a gradual reduction of export duties on crude oil and petroleum products (up to their total abolition) and increase of MET. This reform will reduce subsidizing of the downstream sector and create incentives for its upgrading and improve refining margin. Simultaneously, this will cut Russia's subsidies to other EAEU countries and will strengthen incentives for increasing efficiency of the domestic oil consumption.

It is expedient to introduce at the new oilfields Additional Profits Tax (APT), which will ensure both resource rent extraction and necessary conditions for investment. APT is based on net income and represents a more flexible taxation instrument by contrast with MET and export duty. APT automatically brings the tax burden in line with oil production conditions on each specific oilfield. In doing so, necessary conditions for investments are being created including in the development of high cost intensive oilfields.

[1] See: Yu. Bobylev, O. Rasenko. Options for tax incentives for the oil sector. Russian Economic Development. 2016. No 7, pp. 66–69.

It is expedient to develop the sector of medium- and small-scale oil producing companies, which can be efficient in the development of relatively small-scale low profit deposits and hard-to-recover reserves. This requires development of a corresponding organizational and legal regime including significant reduction of administrative barriers.