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R95 **Russian Economy in 2019. Trends and outlooks. (Issue 41)** / [V. Mau et al; scientific editing by Kudrin A.L., Doctor of sciences (economics), Radygin A.D., Doctor of sciences (economics), Sinelnikov-Murylev S.G., Doctor of sciences (economics)]; Gaidar Institute. – Moscow: Gaidar Institute Publishers, 2020. – 596 pp.: illust.

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The review "Russian Economy. Trends and Outlooks" has been published by the Gaidar Institute since 1991. This is the 41th issue. This publication provides a detailed analysis of main trends in Russian economy, global trends in social and economic development. The paper contains 6 big sections that highlight different aspects of Russia's economic development, which allow to monitor all angles of ongoing events over a prolonged period: global economic and political challenges and national responses, economic growth and economic crisis; the monetary and budget spheres; financial markets and institutions; the real sector; social sphere; institutional changes. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts confirming the conclusions.

By contrast to the previous publications the present issue includes also a short analysis of the first three months of 2020 from the perspective of the COVID-19 pandemic impact on the Russian economy development.

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Yuri Bobylev

4.5. The Oil and gas sector in Russia 2019[1]

The oil and gas sector is among the basic ones of the Russian economy and is playing an important role in the income generation for the state budget and Russia's trade balance. Implementation of the OPE, Russia and a number of other countries agreement on the production cut with a simultaneous global crude oil demand growth in 2019 has resulted in the world crude oil prices stabilization in the range of $60–70 per barrel. In 2019, the volumes of crude oil production peaked for the entire post-Soviet period and the extraction of the natural gas hit an all-time high. Under the effect the tax maneuver in force in the oil industry, the crude oil refining volumes have stabilized and significantly increased the refining depth, production of fuel oil and its exports have contracted. March 2020 revealed a crucial discrepancy between the positions taken by Russia and the OPEC member states regarding the deal parameters for the subsequent period. Hence, there were no new agreements, the current deal was not extended and Saudi Arabia notified about the intention to ramp up production. In the wake of coronavirus pandemic and a plunge of the global oil demand the crude oil prices have collapsed.

4.5.1. Dynamic of global oil and gas prices

Over recent years the world crude oil market was marked by fundamental changes. Following the prolonged period of exceptionally high world crude oil prices (in 2011-H1 2014 they stood at USD 107–112 per barrel) the rapid growth of global crude oil production resulted in a substantial excess of crude oil supply over production and a plunge of crude oil prices. The main factor for the oil glut was the development of U.S.'s shale oil-fields bolstered by advanced drilling methods. Facing this context, OPEC countries refused to cut their oil production quota and in fact switched to a policy of retaining their market share on the global oil market, seeking to ramp up the supply volumes and thus offset contraction of revenues. Subsequently, the price of the Russian Urals crude oil on the world market dropped from USD 107.1 per barrel registered in H1 2014 to USD 51.2 per barrel in 2015 and to USD 41.9 per barrel in 2016, that said in January 2016 the price plummeted to USD 28.8 bpd. (*Table 18, Fig. 23*).

Table 18

World crude oil and natural gas prices in 2014–2019, USD/bbl.

	2014	2015	2016	2017	2018	Q12019	Q22019	Q32019	Q42019	2019
Brent crude price, Great Britain	98.9	52.4	44.0	54.4	71.1	63.3	68.3	61.9	62.7	64.0
Urals crude price, Russia	97.7	51.2	41.9	53.1	69.8	63.3	68.1	61.3	62.1	63.7
Average export price on Russian gas, USD/thousand cubic m.	314	225	157	179	223.3	226.2	183.6	162.7	174.8	186.8

Источник: OECD/IEA; World Bank; Росстат.

[1] This section was written by *Bobylev Yu.N.*, Candidate of science (Economics), Head of Mineral Sector Economics Department, Gaidar Institute.

The decline in oil prices spurred oil-producing countries into taking decisive actions on output cuts. At the end of 2016, OPEC and a group of oil producing countries from outside OPEC, including Russia, (OPEC+) concluded a production cut agreement for 6 months period in effect since 1 January 2017. In compliance with this agreement OPEC+ obligated to reduce its oil production by 1.8 million barrel per day, including OPEC member states – by 1.2 million barrels per day and 11 non-OPEC countries, agree to cut output by 558,000 barrels per day, of which Russia by 300,000 barrel per day. In an effort to decrease further the oil supply glut, the OPEC+ parties to the agreement decided in May 2017 to extend the agreement for another nine months, that is, between July 2017 and March 2018, and in late November 2017 the deal was extended till the end of 2018. Meanwhile, some of the parties to the agreement (Venezuela, etc.), for various reasons, experienced a steep downfall in oil production. As a result, the real cut in oil production by OPEC+ has turned out to be a considerably higher target than envisaged by the agreement.

Fig. 23. Urals crude oil price in 2008–2019, USD/bbl.

Source: Rosstat.

In this context, in June 2018 OPEK+ decide to raise production from early July by 1 million barrels per day compared to May. That said, a provision was envisaged for switching from the previous per-country control over the agreed output targets to a control over total crude oil output (by 1.8 million barrels per day below the level of October 2016) of the parties to the agreement. Hence, countries with spare potential had the opportunity to boost their production in H2 2018. Saudi Arabia (representing nearly 70 percent of OPEC's available capacities) and Russia were the first to do this. However, production ramp up by major crude oil producers (USA, Saudi Arabia, and Russia) and some other factors resulted in the crude price drop over last months of 2018 (to USD 57–58 per barrel).

In this context, in December 2018 OPEC+ members agreed to cut oil production by 1.2 million barrels per day from early 2019 onwards from the output seen in October 2018. This deal was effective over 6 months (January-June 2019). Under the deal the cut of crude oil production by OPEC members was in the amount of 800 thousand bpd, and by non-OPEC major crude oil producers by 400 thousand bpd, with Russia taking on 228 thousand bpd. However, the output cut commitments did not apply to Iran, Venezuela and Libya where oil production was already low, plus Iran was facing the risk of reducing further its output in case

of tougher U.S. sanctions against purchases of Iranian crude, which really occurred. By late 2019 compared to Q1 2018, oil output in Iran under the burden of sanctions dropped by 47%. Similar situation was observed in Venezuela: over that period oil production decreased by 57.5%. In early July 2019, the deal was extended for next 9 months (July 2019 – March 2020).

Implementation of OPEC+ agreements with simultaneous growth of the global oil demand resulted in the noticeable rise of the global oil prices and their stabilization in the range of USD 60–70 per barrel. In 2018, the price of the Russian crude oil on the world market averaged USD 69.8 per barrel, in 2019 – USD 63.7 per barrel. In 2019, the price dropped by 8.7% against 2018. That said, in H2 the oil price declined to USD 61–61 per barrel and in some months decreased still further (for example, in October 2019 it stood at USD 58.5 per barrel).

Reason for the 2019 oil price drop was a slowdown of the global oil demand and ramp up production in countries outside of the deal, first of all, in the US (*Table 19*). Technological advancement and cost effectiveness allowed the U.S. oil industry to adapt to lower prices: in 2018 the US produced 10.99 million bpd (up by 17.5 percent against 2017), and in 2019– 12.24 million bpd (up by 11.4 percent against 2018).

Table 19

Oil production in US and OPEC members in 2016–2019, mn bpd.

	2016	2017	2018	Q12019	Q22019	Q32019	Q42019	2019
USA	8.86	9.35	10.99	11.81	12.10	12.23	12.82	12.24
OPEC, total	32.68	32.68	31.96	30.47	30.00	29.20	29.48	29.78
Saudi Arabia	10.42	10.09	10.38	10.00	9.92	9.38	9.83	9.78
Iraq	4.43	4.44	4.60	4.75	4.70	4.70	4.65	4.70
Iran	3.57	3.82	3.52	2.63	2.33	2.10	2.03	2.27
Venezuela	2.18	1.92	1.43	1.05	0.79	0.73	0.68	0.81

Source: US EIA.

In the context of growing oil supply by producers outside of the deal, in December 2019 the OPEC+ members agreed on additional cut of crude oil production from January 1, 2020 by another 503 thousand bpd (in addition to the effective commitments in the amount of 1.2 million bpd). That said, the OPEC members have to additionally cut production by 372 thousand bpd and other countries outside of the deal – by 131 thousand bpd. Taking into account this reduction, which had to stay in force over Q1 2020 the aggregate reduction by OPEC+ members compared to October 2018 should come to 1.7 million bpd.

Saudi Arabia accounted for a major cut: under effective commitments cut production totaling 322 thousand bpd it had to cut production by another 167 thousand bpd. Russia according to December agreement has to cut another 70 thousand bpd. As a result, taking into account effective commitments to the tune of 228 thousand bpd Russia's total production cut should be 298 thousand bpd. Moreover, on the insistence of the Russian party from 2020 the Russian quota will not include condensate, which corresponds the effective OPEC methodology applied to countries members of OPEC. This fact will allow Russia not to limit condensate production.

It should be noted that the effect of Russia's adherence to the OPEC+ agreements on the crude oil production in the country was rather limited: in 2017 compared to 2016, the annual oil output declined by 0.15 percent, and in 2018 and 2019, went up by 1.7 and 0.9 percent, respectively. With regard to the 2017 situation, we should point out two aspects. Firstly, the OPEC+ countries took production level of October 2016 as a benchmark for the oil production cut. During 2016, the oil production in Russia was growing and in October hit maximum (above the average level posted in 2016). Moreover, by virtue of technological and climatic features

Russia was cutting production gradually in the curse of several months. Ultimately, the annual production in 2017 against the previous year decreased relatively insignificantly.

In 2018, Russia jumped at the opened within the framework of the agreement opportunity to raise production in the second half which led to an increase of annual production. In 2019, the annual oil production growth was triggered both by a relatively high benchmark level of October 2018 and by the relatively slow reduction of production due to technological and climatic factors.

As a result of Russia's 3-year adherence to the OPEC+ agreements (2017–2019), the annual oil production in the country went up by 2.4 percent.

Accordingly, the OPEC+ agreements on joint efforts aimed at the oil production cut were a substantial factor severely affecting global oil prices. The three-year experience of their implementation has demonstrated that such agreements allow to reduce risks of price crises and contribute to maintain a certain level of the global oil prices.

Whereas the effective agreement covered solely Q1 2020 in early March 2020 next meeting of the OPEC+ representatives took place where the issue of further joint actions on the production cut were to be taken. However, the meeting revealed a crucial discrepancy between the positions taken by Russia and the OPEC member states regarding the deal parameters for the subsequent period. The OPEC members considered necessary to additionally cut oil production by 1.5 mn bpd from April 1, 2020, the Russian position resided in retaining parameters of the ongoing agreement for the next quarter. Hence, the new agreement collapsed and the effective deal was not extended.

Starting from April 1, 2020 the agreement participants got a chance to exit from the restrictions regime and Saudi Arabia has notified about its intention to boost its production. In the second half of March 2020 the futures price on Brent crude declined to USD 25–28 per barrel.

Prices on Russian natural gas exported abroad on long-term contracts, as a rule, are tied to the prices of petroleum products and owing to this factor follow the world crude oil prices with a certain lag. Meanwhile changes that took place on the European market over recent years – increased supply of gas by other natural gas producers and lower spot prices on natural gas compared to the prices of long-term contracts signed by Gazprom produce downward pressure on the Russian natural gas. In 2019, the average export price on Russian gas stood at USD 186.8 per cub m or declined by 16.3 percent compared to 2018 and by 40.5 percent against 2014 (*Table 18*, *Fig. 24*).

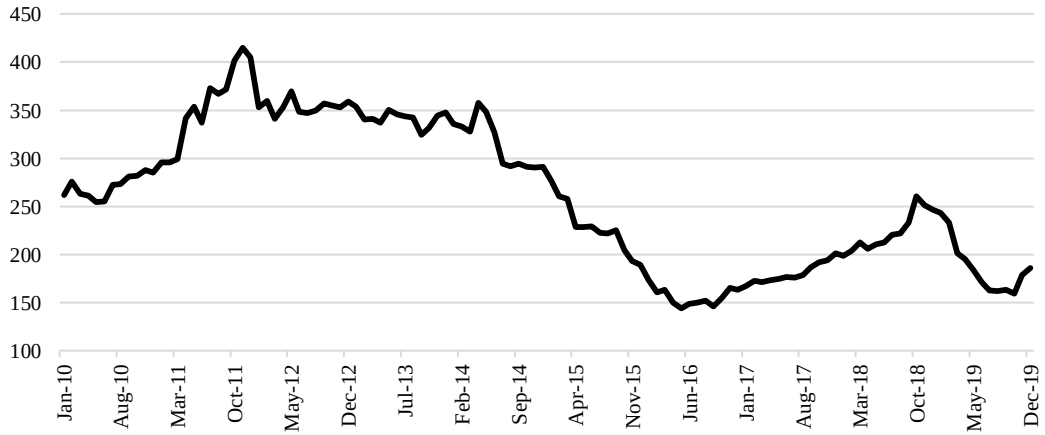

Fig. 24. Average price of Russian gas on external markets in 2010–2019, USD/thousand cub m

Source: Rosstat.

4.5.2. Production dynamic in the oil and gas sector

Volumes of crude oil output in 2019 were governed by Russia's compliance with her commitments taken within OPEC+ agreements. Along with this, in 2019 oil production in Russia hit 560.8 million t or went up by 0.9 percent compared to 2018 (*Table 20, Fig. 25*). This was an all-time high since 1989 (Russia peaked its oil output in 1987 by 569.4 million tons). Extraction of natural gas in 2019 increased to 758.1 billion cubic meters (Up by 2.3 percent against 2018), which is an all-time high. In recent years, production of liquefied gas has surged (from 10.9 million t in 2016 to 29.5 million t in 2019). Russia boasts of a substantial potential in order to maintain and ramp up current volumes of oil and gas output. At the same time, the oil sector faces objectively deteriorated production conditions. Considerable share of producing fields demonstrate a downward trend of extraction and the new deposits in the majority of cases are marked with not as good mining-and-geological and geographic parameters, their development requires higher investment, running and transportation costs. In order to offset falling production on the brown fields, it is necessary to develop both new oil deposits in regions with underdeveloped infrastructure or in those regions that lack infrastructure altogether, and to develop low quality deposits in developed regions.[1]

Table 20

Production of crude oil and natural gas and oil refining in Russia in 2010–2019

	2010	2014	2015	2016	2017	2018	2019
Crude oil including condensate, million tons	505,1	526,7	534,0	547,6	546,8	556,0	560,8
Natural gas, billion cubic meters	665,5	654,2	645,9	652,6	704,1	741,1	758,1
Natural liquefied gas, million tons	10,0	10,7	10,8	10,9	11,8	20,0	29,5
Primary crude oil refining, million tons	249,3	294,4	287,2	284,5	284,3	290,7	290,0
Share of crude oil refining in crude production, percent	49,4	55,9	53,8	52,0	51,9	52,3	51,7
Crude oil refining depth, percent	71,1	72,4	74,4	79,1	81,0	82,1	82,7

Sources: Rosstat, Ministry of Energy of the Russian Federation.

[1] See Yu. Bobylev, O. Rasenko. Russia Oil Sector: main trends. Moscow, Delo Publishers, RANEPA, 2016.

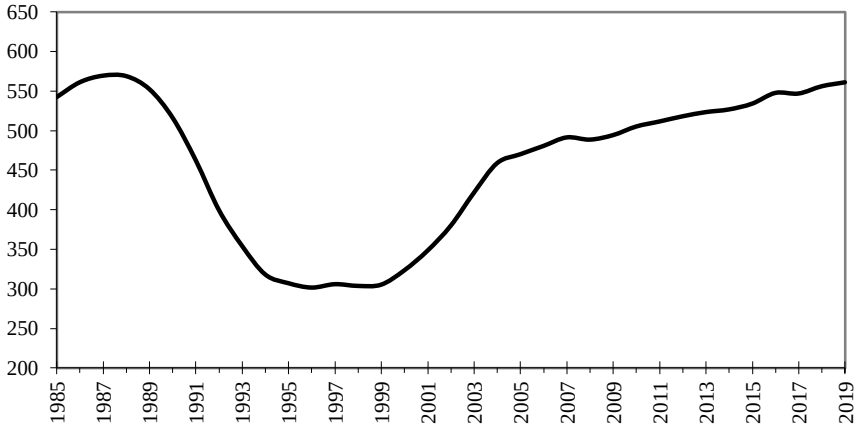

Fig. 25. Crude oil production, including condensate in 1985–2019, mn t

Sources: Rosstat, Ministry of energy of Russia.

Year 2018 demonstrates that the tax maneuver has delivered positive results from the first phase of the tax maneuver in force in the oil industry from 2015: a structural tax reform in this sector envisages gradual reduction of export duties on both crude oil and petroleum products, as well as higher mineral extraction tax (MET).[1] Such restructuring of the tax system has created incentives for upgrading of oil refining capacities and has resulted in current trend changes.

In 2000–2014, the Russian oil sector saw growing volumes of both oil refining and exports of petroleum products owing to the increase of production and exports of fuel oil (the least valuable refining product which in Europe is used for further refining and obtaining light petroleum products). The oil refining depth was not growing at that and constituted solely 71–72 percent (while, in the leading industrial countries it came to 90–95 percent). Then tax system actually conserved technological backwardness of Russia's oil refining sector and led to marked losses for the state budget as a result of hidden subsidizing of the oil refining sector and other EAEU member states owing to lower compared to the world oil prices as well as lower export duties on petroleum products against the oil export duties.

Implementation of the tax maneuver resulted in the turnaround of existing trends. Among the new trends emerged in 2015–2019, and some of them deserve to be mentioned here: firstly, the oil refining depth increased notably as production of fuel oil declined, secondly, owing to the contraction of exports of fuel oil more lucrative crude oil exports moved up, thirdly, crude oil refining declined in volume terms due to the above two factors. The oil refining depth in Russia increased from 72.4 percent in 2014 to 82.7 percent in 2019 which is the all-time high (*Fig. 26*). Production of gasoline and diesel fuel went up while production of fuel oil declined by 39.6 percent. The share of refined oil in its production decreased from 55.9 percent to 51.7 percent. Petroleum products exports contracted by 13.3 percent

In view of this, thanks to the implementation of the tax maneuver previously observed trends which demonstrated growth of refined oil volumes and growing exports of petroleum products due to increasing production and exports of fuel oil were phased out by trends which show contraction of production and export of fuel oil and as a result contraction of the oil refined

[1] See Yu. Bobylev. Tax Maneuver in Oil Industry. Russian Economic Developments. 2015. No. 8, pp. 45–49.

volumes and petroleum products exports. Meanwhile, depth of the oil refining increased notably.

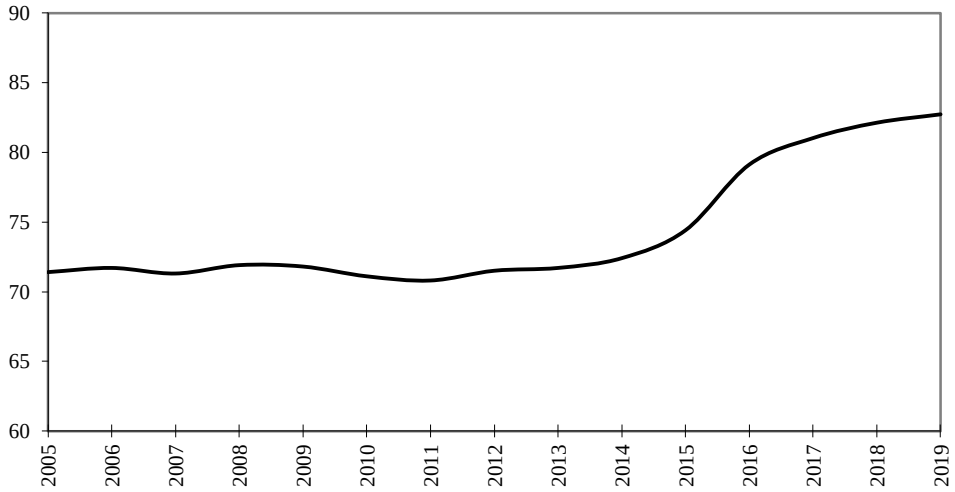

Fig. 26. Crude oil refining depth in 2005–2019, percent

Sources: Ministry of Energy of Russia, Rosstat.

4.5.3. Dynamic and structure of oil and gas export

In 2019, the total Russia's exports of crude oil and petroleum products constituted 409.7 million tons, up by 6.7 percent against 2014 or by 0.1 percent against 2018. This index is close to an all-time high achieved in 2015 (411.8 million t). The share of net exports of crude oil and petroleum products in 2019 came to 73.1 percent (*Table 21*). It should be noted that 2015–2019 saw a notable growth of 19.7 percent of crude oil exports spurred by the tax maneuver and 13.3 percent decline in exports of petroleum products mainly owing to a steep fall of the fuel oil exports (by 34.7 percent). As a result, the share of crude oil in total oil exports went up from 57.5 percent in 2014 to 65.2 percent in 2019, and that of petroleum products – declined from 42.5 to 34.8 percent. Meanwhile, exports of diesel fuel and motor gasoline went up. The share of exports in diesel fuel production in 2019 made up 65.6 percent, and in motor gasoline production – 13 percent. The share of fuel oil in petroleum products exports declined from 52.9 percent in 2014 to 39.9 percent in 2019.

Table 21

Ratio of production, consumption and exports of crude oil and natural gas in 2010–2019

	2010	2014	2015	2016	2017	2018	2019
Crude oil, mn t							
Production	505.1	526.7	534.0	547.6	546.8	556.0	560.8
Exports, total	250.4	223.4	244.5	254.8	252.6	260.2	267.5
Exports to - non-CIS countries	223.9	199.3	221.6	236.2	234.5	241.7	249.1
Exports to CIS countries	26.5	24.1	22.9	18.6	18.1	18.5	18.3
Net exports	249.3	222.6	241.6	254.0	252.0	259.7	267.5
Domestic consumption	125.9	141.3	122.2	138.3	147.1	146.7	151.1
Net exports as percent of production	49.4	42.3	45.2	46.4	46.1	46.7	47.7
Petroleum products, mn t							
Export	132.2	164.8	171.5	156.0	148.4	150.1	142.8
Net export	129.9	162.8	170.2	155.3	147.7	149.6	142.2

	2010	2014	2015	2016	2017	2018	2019
Crude oil and petroleum products, mn t							
Net exports of crude oil and petroleum products	379.2	385.4	411.8	409.3	399.7	409.3	409.7
Net exports of crude oil and petroleum products as percent of crude oil production	75.1	73.2	77.1	74.7	73.1	73.6	73.1
Natural gas, billion cubic meters							
Production	665.5	654.2	645.9	652.6	704.1	741.1	758.1
Exports	177.8	172.6	185.5	198.7	210.2	220.6	219.9
Net exports	173.5	165.5	178.4	189.8	201.4	211.2	210.8
Domestic consumption	492.0	488.7	467.5	462.8	502.7	529.9	547.3
Net exports in percent to production	26.1	25.3	27.6	29.1	28.6	28.5	27.8

Sources: Rosstat, Russian Ministry of Energy, Federal Customs Service, own calculations.

Analysis of Russia's crude oil exports over the course of a long period demonstrates a marked increase in the export-led component of oil industry. The share of net exports of crude oil and petroleum products in crude oil production went up from 47.7 percent in 1990 to 73.1 percent 2019. This, however, is due not only to the increase in absolute volumes of exports but to a crucial contraction of domestic oil consumption against the Soviet period on the back of the market reform of the Russian economy and more efficient oil consumption and the replacement of petroleum products (fuel oil) by natural gas.

Exports of natural gas in 2019 amounted to 219.9 billion cubic meters and was close to the previous year's level of 220.6 billion cubic meters, which was an all-time high. The share of net exports in the natural gas production in 2019 constituted 27.8 percent. We should note a spike in exports of liquefied natural gas which over the recent years surged by over 3-fold: from 21.4 million cubic meters in 2015 to 65.4 million cubic meters in 2019.

Owing to the plunge of global prices on crude oil and natural gas, the share of oil and gas sector products in Russian exports amounts to over a half (*Table 22*). In 2019, the oil and gas sector accounts for 56.0 percent of Russia's exports. The oil sector accounts for the major part of exports. Nevertheless, its proportion in the Russia's exports over recent years declined from 54.2 percent in 2014 to 44.3 percent in 2019. The share of the natural gas sector in the Russia's exports amounted to 11.7 percent. Furthermore, the proportion of the liquefied gas went up (from 0.9 percent in 2017 to 1.9 percent in 2019).

Table 22

Cost and share of export of oil and gas sector products in Russian exports in 2017–2019

	Exports in 2017, billion USD	In percent to total volume of Russia's exports	Exports in 2018, billion USD	In percent to total volume of Russia's exports	Exports in 2019, billion USD	In percent to total volume of Russia's exports
Oil and gas sector, total	192.87	53.7	261.5	57.9	237.9	56.0
Crude oil and petroleum products	151.55	42.2	207.1	45.8	188.3	44.3
Crude oil	93.31	26.0	129.0	28.5	121.4	28.6
Petroleum products	58.24	16.2	78.1	17.3	66.9	15.8
Natural gas	38.15	10.6	49.1	10.9	41.6	9.8
Liquefied natural gas	3.17	0.9	5.3	1.2	7.9	1.9

Sources: Federal Customs Service, own calculations.

4.5.4. Dynamic of domestic prices on energy products

The pricing mechanism for crude oil and petroleum products on the Russian domestic market is based on equal-netback pricing, that is, prices are equal to the world price less export duty

and transportation costs. On the back of this, domestic prices on crude oil and petroleum products in dollar terms actually follow the world market prices (*Table 23*, *Fig. 27*). Having said that, there is still a wide gap between world and domestic oil prices due to the export duty. Along with this, 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 oil price (the producers' price) came to 42 percent of the global price (Urals crude price on the European market), while in 2018 – 66 percent, and in 2019 – 71 percent.

Table 23

Domestic prices on crude oil, petroleum products and natural gas in dollar terms in 2010–2019 (average producers' prices at year-end, USD/ton)

	2010	2013	2014	2015	2016	2017	2018	2019
Crude oil	248.2	346.1	178.9	156.7	207.8	302.4	320.8	329.1
Motor gasoline	547.9	614.4	372.3	301.8	380.3	460.0	423.3	393.2
Diesel fuel	536.1	698.0	419.3	349.4	421.3	515.2	550.7	540.1
Fuel oil	246.3	235.8	128.7	49.5	129.7	166.1	186.0	116.1
Gas, USD/thousand cubic m	20.5	39.8	29.1	24.5	23.6	34.2	28.9	27.7

Source: own calculations based on data released by Rosstat.

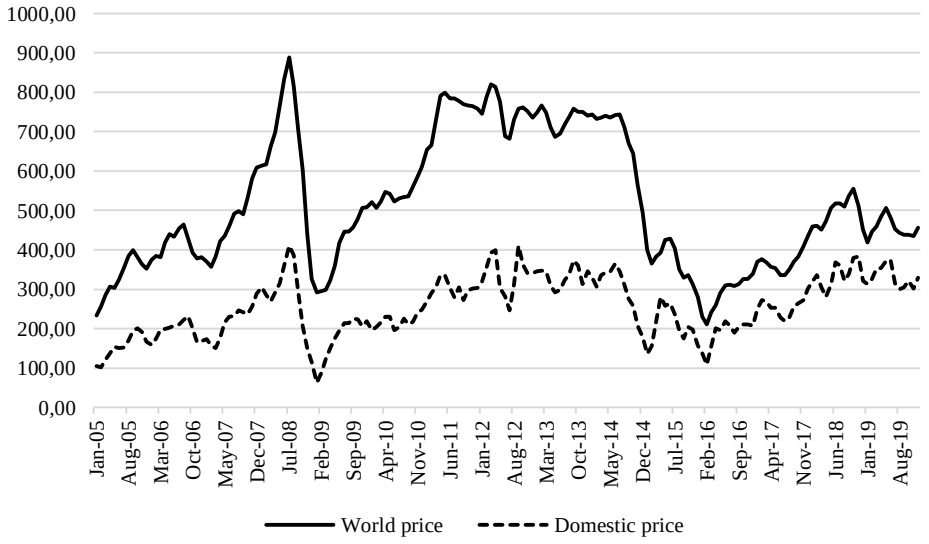

Fig. 27. Global and domestic crude oil prices in 2005–2019, USD/t

Sources: Rosstat, own calculations.

End-user (consumer) prices on motor gasoline (*Table 24* are set on net-back prices taking into account indirect taxes (excises, VAT) and markup. Russia regarding the share of indirect tax burden in the final motor gasoline price ranks in the middle between leading EU countries where this share is the highest (65 percent) and the USA where it is relatively low (20 percent).[1]

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

With lower non-tax gasoline prices and such level of tax burden the consumer prices on motor gasoline in Russia are approaching the US prices, but remain significantly lower than in other developed countries. According to our calculations, in 2020 the consumer price on motor gasoline in Russia came to the level of the USA 100 percent, Canada – 75 percent, Japan – 49 percent and regarding the average level of leading EU-5 – 45 percent (*Table 25*).

Table 24

Consumer prices on motor gasoline in Russia 2014–2018, RUB/liter (in January y-o-y)

	2014	2015	2016	2017	2018	2019	2020
Regular unleaded gasoline	29.53	32.35	33.86	35.57	38.12	41.87	42.46
Premium 95 octane and plus	32.64	35.16	36.81	38.69	41.05	45.14	45.85

Source: Rosstat.

Accordingly, in the wake of the tax maneuver the relative level of end-user prices on motor gasoline in Russia went up insignificantly. The effective system of export duties and the level of tax burden on petroleum products in Russia ensures lower price level on motor gasoline on domestic market in comparison with the majority of developed countries. At the same time, prices on motor gasoline in Russia have arrived at the USA level which boasts of a lower tax burden on petroleum products.

Table 25

Consumer prices on motor gasoline in Russia relative to other countries, percent

	2014, January	2020, January
USA	95.8	100.1
Canada	72.9	75.2
Japan	55.0	48.8
Germany	44.4	46.6
Great Britain	43.3	43.8
France	45.3	42.5
Italy	39.5	41.2
Spain	48.7	49.5
EU-5	44.1	44.7

Source: own calculations of data released by OECD/IEA and Rosstat.

Domestic prices on the natural gas are under the state regulation. In order to ensure competitiveness of the national economy, the government maintains significantly lower level of domestic prices on gas compared to the world gas prices. Meanwhile, owing to a regulated increase of the domestic gas prices and a significant decrease of the world prices on natural gas there is a gradual convergence of domestic and world gas prices. In 2019, domestic gas price (corporate consumers' price less indirect taxes) averaged 36 percent of the export price on Russian gas in 2018 – 31 percent).

4.5.5. Prospects for development of the Russian oil industry

Russia disposes of the vast oil reserves, which are enough to maintain high levels of crude oil extraction and exports for many years to come. There is a substantial potential for crude oil extraction owing to both undeveloped deposits in the developed areas and oilfields in the 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, and ramping up the oil recovery index. Moreover, Russia disposes of extensive currently undeveloped unconventional oil reserves including shale oil. Russia's oil refining potential is high and ramping up the

refining depth rate to the level of industrial states allows to satisfy domestic need in motor fuel amid relatively lower volumes of oil consumption.

Global demand for oil will allow Russia to retain and even to increase current volumes of crude oil exports, first of all, by increasing shipments to China and other countries of Asia. 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. Against this backdrop enforced technological sanctions against Russia, which ban exports to Russia of equipment and technologies for the development of deposits located on the Arctic shelf, deep-water oil fields and shale oil deposits will negatively affect the oil industry development.

There is a significant uncertainty regarding the world crude oil prices in 2020 due to the effect of such factors as coronavirus pandemic, economic recession, oil demand plunge, decline of shale oil production in the US as well as behavior of major oil producing stakeholders and first of all Saudi Arabia. In Q2–Q4 2020 the most feasible projection of the crude oil price to stay in the range of USD15–40 per barrel. That said, in Q2 2020, the oil prices may stay in the range of USD15–25 per barrel. Renewal of negotiations within OPEC+ and conclusion of a new deal on the production cut would have triggered stabilization and rise of the world oil prices in H2 2020.

In this context, the backbone of the further development of the Russian oil sector should become the conventional oil reserves on land. Having said that, particular significance will have deepened development of the producing fields, raising the oil refining rate. Capacities for additional crude oil output will depend on the technological progress in the sector, development of import substitution technologies, ramping up the oil recovery rate and development of unconventional reserves including shale oil deposits.

The future economic policy regarding the oil industry aimed at the creation of necessary conditions for its further development and at the government obtaining oil-related fiscal revenues should include the implementation of the following measures:

- continuation of the tax system reform: raising the MET role, reduce and abolish export duty on crude and petroleum products. This will contribute to a more efficient tax system structure, reduce subsidization of the refining sector, provide incentives for its further modernization, stepping up the oil refining depth; decrease subsidization by Russia of EAEU members; strengthen incentives for raising energy efficiency;
- expand the application of the additional profits tax on the new deposits with a progressive tax rate depending of the profitability of deposits development. This tax will ensure a wider differentiation of tax burden depending on the production conditions, complete resource rent extraction to the state and create favorable conditions for investment into the oil production, including the development of high-cost deposits;
- continuation of the tax burden differentiation policy applied to the producing oil fields: putting in place reduced MET rates and export duty for high-cost deposits. Reduction of tax burden on extensively depleted deposits: additional reduction of the MET rate for such deposits will provide incentives for their deep development, raising the oil extraction index;
- development of small and medium-sized companies: development of corresponding organizational and legal regime including a significant reduction of administrative barriers to entry for the development of mineral resource blocks. This will contribute to the deep development of producing oil fields, development of small-scale and low-income deposits and hard-to-recover reserves. It seems expedient to renew cooperation with OPEC+ and

rearrange coordination of activities regarding oil production with OPEC members and other oil producing countries in an effort to maintain an acceptable level of world crude oil prices.