

Interview Vagit Alekperov, ceo Lukoil

‘We view ourselves as much a European as a Russian company’



Vagit Alekperov, chief executive officer of Lukoil, the largest private oil producer in Russia, recently visited Brussels for the first time in his life. He called for improved dialogue between Russia and Europe, but added that Lukoil, which has invested \$5 billion in the EU in recent years, felt no constraint about operating in the EU. ‘We consider ourselves as much a European as a Russian company.’

| by Karel Beckman

Of all Russian oil and gas companies, Lukoil is by far the most internationally oriented. The company has extensive international operations, upstream in Kazakhstan, Egypt, Azerbaijan, Saudi Arabia, Venezuela, Colombia, Ghana and Iraq, downstream (including petrol stations) in the US and Belgium, as well as most Eastern European countries. Founded on 25 November 1991, it was the first company to come out of the collapse of the Soviet Oil Ministry. It was privatised in 1993 – before the controversial privatisation programmes of the mid-1990s.

By now the company has survived 20 years of upheaval in the Russian oil and gas industry. Through its good relations with the Kremlin, it escaped the fate of its great rival Yukos, which was nationalised in 2006. Yet, Lukoil is still under pressure from the continuing encroachment of the State. State-owned gas producer Gazprom has recently expanded into oil production by

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acquiring Sibneft, whereas state-owned oil company Rosneft has surpassed Lukoil as largest oil producer by acquiring parts of dismantled Yukos. Most observers, however, believe that Lukoil, with its American shareownership (ConocoPhillips owns 20%) is in a good position to survive. It has risen to the challenge of competition from Gazprom and Rosneft by expanding into gas, petrochemicals and electricity production in Russia and by further expanding its international activities. As Financial Times-writer Isabel Gorst points out in an article for the James A. Baker III Institute for Public Policy (“Lukoil: Russia’s Largest Oil Company”), the company is ‘highly adaptive’ and may even serve as a ‘model for private western oil companies operating in Russia’.

For all its international scope, Lukoil’s co-founder, co-owner and chief executive officer Vagit Alekperov visited Brussels for the first time in his life in March of this year. He came to the EU capital to address the European Business Summit. In an

exclusive interview with European Energy Review, Alekperov expressed a desire for good relations between Russia and the EU. He said it was time for experts to come up with a proposal for a document to improve the Energy Charter Treaty, so as to ‘ensure stable and predictable development of the world energy sector’. In a voice more typical perhaps of the Russian view of things, he also issued a call to limit speculation in oil and to reduce spot market trading volumes.

How do you look back on your first visit to Brussels?

I have visited many countries of the world, but, surprisingly enough, this is indeed my first visit to Brussels. During my short stay, I have held a series of meetings to discuss matters concerning energy security, in particular with Mr. Andris Piebalgs, EU Commissioner for Energy, Mr. Nobuo Tanaka, Executive Director of the International Energy Agency, Mr. Robert S. Franklin, Vice President Production of ExxonMobil and other representatives of the European institutions and business circles. In my view, the more contacts there are between business and political leaders, the better it is. You may be aware that Lukoil is now a large investor in the EU, we have invested \$ 5 billion in the EU by now, so it is important for the leader of such a large Russian company to be present at the European Business Summit.

Do you have a specific message for the European Commission and the European Union?

We would like to see more serious and substantial consultations with energy producers regarding decisions and legislation adopted at the EU level. The good intentions to fight climate change, to increase the use of renewable energy sources, and so on, should not have negative effects on the existing production capacities. In the current conditions of the world crisis, we should intensify the dialogue between legislators and producers.

EU-Russia relations have been strained over the last few years; how do you think they could be improved?

For Lukoil, the topic of energy cooperation between Russia and the EU is of particular importance. Europe represents the main

market for our production. Three out of our 8 refineries and nearly one third of our filling stations are located in 14 EU states. (Since then Lukoil has acquired a 45% stake in a Dutch refinery, ed.) Today, Lukoil's investments in the eurozone economy represent more than \$5 billion. We work according to the EU legislation and consider ourselves to be as much a European as a Russian company. Lukoil does not experience any obstacles as regards our activities in the EU countries, even though we do feel the negative impact of the financial and economic crisis and the decline in demand for petroleum products.

Do you believe in the usefulness of the Energy Charter Treaty?

I was part of the Russian delegation when the Energy Charter was signed 16 years ago in Lisbon. I am persuaded that the world oil industry needs a framework regulatory document based on principles reflecting both the interests of hydrocarbon producers and consumers. The troubled existence of the Energy Charter and its Protocols is largely due to the pre-eminence given by the Charter to the interests of hydrocarbon consumers. I am sure that experts should and must prepare proposals for a document which will ensure stable and predictable development of the world energy sector.

The theme of the European Business Summit is “financing, staffing, greening”. Which has priority for you at this moment?

All three are important.

How important is greening the economy to you? Do you believe in the dangers of climate change?

Of course we can't help noticing the impact of climate change. Yet I have fresh in my memory the problem of the millennium bug. Everybody was scared to death. How much money has been spent in preventing this? But nothing happened. There are cycles in the climate, there are warm periods and cold periods. I think that too often environmental slogans become politicised.

So the risk may be exaggerated?

(He laughs). I leave you to figure that out. It's demonised.

In your speech in Brussels you suggested limiting the use of oil quotes in speculative financial transactions and to reduce spot market trade volumes.

Yes. Because of the enormous growth in the trade of financial instruments, the oil price no longer reflects the actual supply-demand balance. We have seen a lot of unpredictable, dramatic price fluctuations, which are in no one's interest. The crisis is an appropriate time for introducing new mechanisms of price setting. We can now take measures aiming at fixing a fair price of oil, including limitations of the use of oil quotes in speculative financial operations, the reduction of the volumes of trade on the spot markets and the conclusion of direct long-term contracts between oil producers and consumers. In my opinion, this crisis should bring closer the interests of the producers and the consumers.

But how could this be accomplished?

The activities of financial and commodity stock exchanges are subject of strict regulation from the competent state authorities in all countries of the world. It seems to me that regulating the forms and volumes of speculative transactions using oil quotes is a more realistic project that regulating commodity and service markets.

What do you think is a “fair price” for oil?

I think that \$70 a barrel is a fair price. At this level, it is possible to cover the costs, to make a reasonable profit and to invest in long-term projects, both in the production and refining.

Where do you see the oil price going this year?

It is a well-known fact that oil prices are influenced by a series of factors, some of which are difficult to predict. However, from the point of view of today, the oil price this year could be between \$50-60.

You were at the OPEC meeting in Vienna recently. Do you think Russia should join OPEC in limiting production?

Russia has a long-standing cooperation with OPEC and enjoys an observer status with this esteemed organization. The decisions regarding the production levels of oil and gas are taken by the Russian government in accordance with the national interests and current social-economic situation.

Turning to Lukoil's strategy, what are your priorities at this moment?

We want to expand primarily in the downstream market. Now only 65% of the crude oil we extract is processed at our own refineries. So we lose some of this margin. Our strategy is to try and make up this gap and increase our downstream presence in Europe. We have successfully addressed this problem in South-Eastern Europe, now we want to do this also in the North-West of Europe. We are ready to invest in refining capacity in those regions. That could be acquisitions, yes, or joint-ventures.

How would you say Lukoil's strategy is different from Rosneft's or Gazprom's?

The programme of strategic development of Lukoil is prepared for a 10-year period, it is updated every second year and should be approved by the Company's Board of Directors. I should stress that the Board of Directors includes also independent representatives.

Can Lukoil become bigger again than Rosneft?

We would like to be better.

Or bigger than Exxon or Shell?

I would put it this way – our aim is to become as efficient as the oil majors. Lukoil is permanently analyzing the main operating indicators of the big players in the oil sector. In many aspects we are close to them, in some fields we are still lagging behind. We are not satisfied, in particular, with the disproportion between our oil production and our refining volumes, as I have indicated.

You are the most internationally active Russian oil company, actively pursuing exploration and production opportunities abroad. Can you say what opportunities to you see in countries like Iran, Iraq and Venezuela and in the Arctic region?

Lukoil is very interested in developing oil production projects both in Iraq and in Iran. In Venezuela we have developed cooperation in exploration and production. We consider that this is a region with very rich oil and gas fields, and Lukoil must therefore be present. Our intention is to produce oil in Venezuela and refine it there, making a link with Lukoil's presence on the US retail market. As to the Arctic region, we are very proud of our contribution to building oil transportation routes from there. Our Arctic oil terminal Varandey was put in exploitation last year. The oil production in the Arctic region requires joint efforts of oil companies because its large fields are difficult to access and require enormous resources to be exploited.

How much scope do you see for future production growth in Russia itself?

At its best moments, the USSR produced 625 millions tons of oil per year. This year it will be around 450-460 millions tons. The main Lukoil fields are located in Western Siberia. The current decline of the oil production in Western Siberia is a natural and predictable process. This year, Lukoil will start exploiting at full capacity the Yuzhnaya Khylichuya field in the Nenetsk Autonomous Region (in Western Siberia, ed.), which will substantially increase our oil production. Furthermore, preparations are under way to start production in the Caspian Sea and new projects are developed in Uzbekistan, which will enable us to increase the production levels of hydrocarbons.

You have also announced ambitious plans to expand your gas production. Is that a viable strategy in Russia?

We are expanding fast in gas. Already in Russia we are number one ... uh, sorry, number two. Nevertheless, we face numerous restrictions. We are obliged to sell all gas that we extract in Russia to Gazprom. Still, we have been successfully working with BP to supply gas to Turkey. We also produce outside of Russia.

Is it correct that you have managed to find gas in Saudi Arabia?

Yes, rather a large field. How much? Up to 300 billion m3. (This is almost four times the annual consumption of Germany, ed.)

I don't think Shell managed to find gas in Saudi Arabia, have they?

(He laughs) Bad luck!

If Lukoil did not exist and you had to look for a job with another company, where would you apply?

I have never thought about such a strange question because I have never had any reasons to think about it.

Who are the people that have been most influential in your career?

There are two men who have made enormous contributions to the development of the Russian oil industry. There is Alexander Usoltsev, former Chairman of the Board of Directors of Surgutneftegas. When I started my first job in Western Siberia, he was General Director of the oil company there. He died, but I will remember him forever. And there is Valery Greyfer, who is our Chairman of the Board of Directors, and who is a great mentor and teacher. These are great men, their names are written in golden letters in the history books of both the Soviet Union and Russia and worldwide. ■

Who is Vagit Alekperov?

Vagit Alekperov, born 1 September 1950 in oil town Baku, Azerbaijan, has worked all his life in the oil industry. He studied at the Azerbaijan Institute of Oil and Chemistry before taking a job at the oil rigs in the Caspian Sea. In 1979, he moved to West Siberia where he became General Director of Kogalymneftegaz in 1987. He became Deputy Minister of Oil and Gas in 1990, and then First Deputy Minister, one year before the demise of the Soviet Union. In 1991, he became President of a company named LangepasUrayKogalymneft, later renamed Lukoil. Lukoil informed us that he owns more than a 20% share in the company. Another approximately 10% is owned by Mr. Leonid Fedun, Vice-President of Lukoil. ConocoPhillips has a share of 20%. The company had sales of \$107 billion in 2008 (+31.5%) and net profits of \$9.1 billion (-3.9%).



Photo: Thierry Monasse