

АНАЛИТИЧЕСКИЙ ЖУРНАЛ • ИЗДАЕТСЯ С 1994 ГОДА

# НЕФТЬ КАПИТАЛ



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ИНДУСТРИЯ 



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# Oil and Capital

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In August, the realization of the first stage of the development program of the largest polyethylene producer in the Russian Federation, OJSC «Kazanorgsintez», is to be completed. The five years long modernization turns this enterprise into one of the most developed petrochemical facilities of Russia and Europe. The second stage of the development program that will be started soon covers the construction of a number of new facilities (including ethylene production), a twofold increase of production capacities and a fourfold increase of revenues.

There are some reasons to suggest that «Kazanorgsintez» will realize the second, and later the third stage of the development in partnership with OJSC «Gazprom». The latter can become the owner of the blocking stake of «Kazanorgsintez» in the nearest future with majority stake to be acquired in a four- or five-year period. «Neft & Kapital» reporter discussed the perspectives of the «Kazanorgsintez» development, the possible changes in the company's shareholding structure with Albert Shigaboutdinov, General Director of PSC «TAIF», the company that controls «Kazanorgsintez».

## Albert Shigaboutdinov: «Kazanorgsintez» is going through a period of changes



**«Neft & Kapital»:** *Albert Kashafovich, the «Kazanorgsintez» (KOS) development program, approved in 2004, should be realized in three stages. What kinds of projects are included in each of them?*

– You're right. The program consists of three stages. The first one was started in 2003 and to be completed this year. As part of this stage, a thorough modernization of the basic operat-

ing facilities was completed and few new ones were constructed. Thus, modernization of the HDPE plant allowed producing new for Russia and the CIS countries, advanced grades of production: bimodal and linear polyethylene. Modernization of ethylene production provided an increase in the production volumes of this material from 430 th tons annually to 640 th tons annually, and for phenol-acetone – from 35 th tons annually to 65 th tons annually. New plants were constructed to produce Bisphenol-A (70 th tons annually) and such types of polycarbonates produced on the basis of Bisphenol-A plants that had never been produced in Russia before. It should be mentioned that the most up-to-date technologies of the leading world licensees-designers were applied during the realization of the first stage of the program. The total volume of investments exceeded RUB 35 bln. As a result, the Company owns the production facilities, able to produce mar-

ketable goods for RUB 58 bln per year (in current prices). We're going to come to these volumes in two years. The realization of the goals set for the second stage of the development program would be started in parallel, as well as the establishment of a number of new facilities. The production capacity of the second line is up to RUB 65 bln of marketable goods per year (in current prices). The cost of the project is over \$3 bln.

After the completion of the second stage, «Kazanorgsintez» will produce the marketable goods for RUB 120 bln. Previously, the government of the Republic of Tatarstan recommended completing this stage of the project within six years, while later this term was reduced twice to three years. Frankly speaking, that for the time being we have a project how to realize this in four-year period.

**«Neft & Kapital»:** *That means, the schedules of the third stage of the development, currently planned for 2018-2020, would be postponed as well?*

– It seems that it would be. The realization of the third stage allows reaching the production level of RUB 200 bln of marketable goods per year. The specialists of the scientific and technical center of «Kazanorgsintez» are seeking for absolutely new efficient technologies. For the matter of that, the rough list of such technologies and facilities included in the third stage exists already. The preliminary calculations have been done, as well.

**«Neft & Kapital»: What projects are you talking about?**

For example, the production of syngas, and the polymers, copolymers on its basis, etc.

**«Neft & Kapital»: Are the volumes of the first stage provided with raw materials in full?**

– Exactly, in full. It is, for the most part, ethane supplied from Orenburg and Minnibaevsk re-

gions (i.e. supplied by LLL «Gazpromdobycha Orenburg» – former «Orenburggazprom» – and Minnibaevsk Gaz Processing Plant, part of «Tatneft» group), liquefied gases, ethylene from «Nizhnekamskneftekhim». As for «Nizhnekamskneftekhim», this enterprise is going to increase the supplies of ethylene to «Kazanorgsintez» by 47% – up to 260 th tons per year. These volumes, including 33 th tons for «Sevelen», represent the carrying capacity of ethylene pipeline Nizhnekamsk-Kazan. However, as soon as «Kazanorgsintez» comes to the level of production of 640 th tons of ethylene, «Nizhnekamskneftekhim» will redirect these volumes to the own production of polyethylene to be put into operation in the end of the current or the beginning of the next year.

Talking about the other production lines, all raw material supply

structures have already been developed. We elaborate them together with the suppliers, as, for example, the above-mentioned suppliers from the Orenburg region.

**«Neft & Kapital»: And do you manage to find any common solution?**

– Of course. The OJSC «Kazanorgsintez» modernization perfectly meets the interests of the Orenburg complex. «Orenburggazprom» always had enough capacity to supply to Kazan more volumes of ethane than Kazan could accept. As a result, the understandable discontent from the partner's side appeared. The situation remained the same down the recent times. As the first stage of the modernization to increase the ethylene production capacities is completed, the demand in ethane by «Kazanorgsintez» will grow from



*The total volume of investments for the first stage of the «Kazanorgsintez» development program exceeded RUB 35 bln.*

400 th tons to 650 th tons. That means, now «Kazanorgsintez» will process all produced in the Orenburg region volumes of ethane, providing the full loading of the ethane pipeline Orenburg-Kazan. This will be followed by the immediate improvement of the financial highlights of the Orenburg facilities. The deficient volumes will be supplied by Minnibaevsk Gaz Processing Plant that will produce up to 150 th tons of ethane after the completion of the modernization in 2008. (At present, we purchase 350 th tons per year of ethane from Orenburg, up to 100 th. per year – from Minnibaevsk).

At the same time, the specialists consider that after some reconstruction the ethane pipeline may supply over 1 mln tons of ethane per year. That is why one should increase the carrying capacity of ethane pipeline and the capacities to process ethane in Orenburg to make possible the realization of the second stage of «Kazanorgsintez» development. The partners from Orenburg welcome this idea; now, they are waiting for signing of an agreement with «Gazprom». Capital investments necessary for this project are not big in their amount.

**«Neft & Kapital»: You have already mentioned that you were going to initiate the development of ethylene ring, connecting today only companies of the Republics of Tatarstan and Bashkiriya. What is the need of this?**

– Yes, it is an issue of current concern. Today, the ethylene ring is formed by «Salavatnefteorgsintez», «Kaustik» from Sterlitamac, «Nizhnekamskneftekhim» and «Kazanorgsintez». When the plants being under the control of PSC «TAIF» were producing the goods for up to RUB 40 bln, this system wasn't so important for us. But now, as «Nizhnekamskneftekhim» made projections to reach annual revenue of RUB 150 bln per year, «Kazanorgsintez» – RUB 120 bln per year,

any shutdown of these companies' facilities would influence the complex's financial highlights. By 2012, these companies, together with OJSC «TAIF-NK» are to have reached the total revenue of RUB 400 bln. That means, one day of shutdown would cost us RUB 1.5 bln. The risk of gaining income less than estimated amounts as proposed by shareholders and the government (including taxes) is too high. That is why the reservation of ethylene becomes the necessary condition for the companies' successful development. This is important, as well, for the development of the petrochemicals sector of the whole Privolzhsky Federal District.

In 2006-2007, we carried out the modernization of the ethylene pipeline on the section Nizhnekamsk-Kazan, increasing its capacity up to 300 th tons per year. There are projections to increase these figures up to 600 th tons per year within a three-year period. Besides, there are discussions to develop the whole ethylene ring to 1 mln tons per year, followed by an increase up to 2 mln tons per year. This requires, first of all, the realization of the initial plan (developed as far back as in the USSR period) and the integration of Nizhnij Novgorod, Samara, and Bashkiriya production centers. These centers will feel for sure the necessity of joining the ring while starting to develop the oil & gas sector. It should be noted, that the interests of «Gazprom» are widely represented in the mentioned regions.

**«Neft & Kapital»: There are considerations that the second development stage would be realized by your company together with «Sibur» and «Gazprom»...**

– It is true, on the 29th of the last May, Head of «Gazprom» Alexey Miller and President of the Republic of Tatarstan Mintimer Shaimiev had agreed that Gazprom should become the shareholder of «Ka-

zanorgsintez». This taking account that in this transaction «Gazprom» would be represented by «Sibur» company.

**«Neft & Kapital»: What model will be used to include a new shareholder?**

– The first stage of convergence presupposes the refusal from processing (today 50% of ethane supplied from Orenburg is processed by «Kazanorgsintez» on tolling scheme) and, in parallel, «Gazprom» is to get a right to buy back 26% of shares of «Kazanorgsintez», presently owned by the state holding «Svyazinvestneftekhim», controlled by the government of the Republic of Tatarstan.

As the transaction is closed, «Kazanorgsintez» will come under the mutual control of shareholders who will bring to life the second stage. After the completion of the second stage and the facilities reach the production level of 120 bln of marketable goods per year, «Gazprom» will immediately increase its shareholding stake up to 50% + 1 share.

A working group was established to prepare the transaction where «Gazprom» is represented by First Deputy of Alexey Miller Valerij Golubev, the Republic of Tatarstan is represented by Prime Minister of the Republic of Tatarstan Rustam Minnikhanov. The Group includes, as well, such members as representatives of the «TAIF» and «Kazanorgsintez» management, the Head of «Sibur» Dmitrij Konov and his team. Besides, «Gazprom» controls the negotiation process through the Chairman of «Sibur» Board of Directors, acting as the Head of «Gazpromneft» as well, Alexander Djukov.

**«Neft & Kapital»: When the partnership agreement can be signed?**

– I don't know. May be, tomorrow, may be in a year. It is possible that the construction of the second line will be started using our own resources with «Gazprom»

joining later. The agreement between the parties will not be an easy one with many small details to be discussed. Both parties seek for serious guarantees that the partner fulfills all his obligations concerning the realization of the second stage. As for our side, we need guarantees for supply of raw materials. Our partner needs guarantees for processing and an increase of stake of shares.

**«Neft & Kapital»: Why has «Gazprom» a need for «Kazanorgsintez»? Gazprom announced again the intention to build its own oil, gas & petrochemical complexes in Salavat and Astrakhan'. Earlier, they had announced the projections to build the polymers production in Orenburg.**

As for «Gazprom» and «Sibur», the partnership with «Kazanorgsintez» has the same importance as for us the partnership with them. This kind of partnership provides stable, guaranteed, long-term processing of large volumes of hydrocarbon resources produced by the above-mentioned companies. This allows managing the logistics issues in the best way. I mean that «Kazanorgsintez» and the Orenburg facility are connected by the ethane pipeline. Besides, our partners are interested in the quality of our assets. As I've already said, during the first stage of the «Kazanorgsintez» modernization we had applied the most advanced technologies providing the competitiveness of our production on the world markets.

At the same time, it is common knowledge that the petrochemical companies of «Sibur» don't have enough developed technologies and their main advantage today is the advantage in the natural resources base. But the situation changes. New facilities require much time and investments. It will be more efficient, cheaper and shorter in time to develop the system Orenburg-Kazan than to construct new processing facilities in

the same Orenburg. The new ones can be put into operation not earlier than in ten years. What is the benefit of doing so? At the same time, «Kazanorgsintez» is the project that runs already today. What our partners need to do is only to take part in its financing, secure the supply of raw materials and provide good level of management. Besides, the staff issue is also of great importance for new facilities. Orenburg facilities simply do not have specialists in chemicals sector, while Tatarstan has kept and is constantly developing its multilevel system of training of such kind of specialists with a number of them already trained.

**«Neft & Kapital»: You've started the talks about consolidation when «Sibur» was simply a subsidiary company of «Gazprom». These talks will be probably completed when «Sibur» becomes a private company being in ownership of five top-managers. Will it save its status of «Gazprom» representative in «Kazanorgsintez»? And, generally speaking, do you feel comfortable with this situation, as it raises many questions. As, for example, why does «Kazanorgsintez» need «Sibur» without «Gazprom», i.e. without guaranteed supplies?**

– At the moment, we don't know for sure who will represent «Gazprom» in our transaction. Nevertheless, «Gazprom» and «Sibur» representatives have stated that the gas processing facilities of «Gazprom» remain technologically connected with the production facilities of «Gazprom». They depend on each other. Especially now when the issue of utilization and processing of associated petroleum gas becomes of top importance. The above-mentioned gas processing facilities are owned by «Sibur»; they themselves represent the guarantee for supplies by «Gazprom». Otherwise, what will «Gazprom» do with its resources? That is why one can logically assume

that even if «Sibur» and «Gazprom» «divorce», they will sign long-term contacts on mutual raw materials & feedstock supply and processing. This represents another guarantee for us when talking about the selling of «Kazanorgsintez» shares. We should be sure that by doing so we will increase the resource base of the company. That is the main point that is valuable for us in this partnership, apart from the understanding that together we become more powerful. It's better to consolidate the sector rather than to compete with each other. Our competition will be the competition with foreign producers on the world markets.

**«Neft & Kapital»: In May, «Sibur» showed its dissatisfaction with the actions of «Kazanorgsintez» shareholders several times. In particular, the «Sibur» representatives received the information about an increase of a number of authorized shares 35 times (from 720 mln shares to 25 bln shares) only in one month after the «Kazanorgsintez» shareholders meeting. These actions were considered to be the desire of «Kazanorgsintez» to carry on the additional emission of shares «without regard to the interests of «Sibur» as a potential shareholder»...**

– The increase in a number of authorized shares was initially offered by «Gazprom». By participating in the additional emission «Gazprom» could become one of «Kazanorgsintez» shareholders. By the way, this year, we offered two positions in the «Kazanorgsintez» Board of Directors to «Gazprom». They expressed the desire to accept this offer but immediately at that time the process of transformation of «Sibur» to a private company was started, so there were more important issues for them. Seeking for the approval from the company not being a shareholder of «Kazanorgsintez» is more than strange.

The earlier the partnership agreement is signed, the earlier we will start to solve together the issues concerning the development of «Kazanorgsintez».

**«Neft & Kapital»: «Sibur» showed the dissatisfaction for another fact, i.e. that in May «Kazanorgsintez» appealed to the holders of euro bonds for \$200 mln asking them to change the terms of loan agreement for one year period.**

– Yes, we have done so. The fact is that there is a covenant that debt/EBITDA ratio for «Kazanorgsintez» should not be higher than 4X but the breach of this covenant happened because of the following: an increase of capital investments required for the company's modernization, the delay in terms of realization of the agreements

reached by Shaimiev and Miller and, thus, changes in the plans of the development for 2008. There was essential need for changing the terms of the agreement. I do not see any problems here. TAIF provided the additional guarantee to «Kazanorgsintez», thus closing the problem.

**«Neft & Kapital»: But a conflict with «Sibur» can become too expensive. They demonstrated this last year by shutdown in supplies of ethane for three months period. By the way, how this influenced the company's financial highlights?**

– «Kazanorgsintez» kept the schedule of realization of the strategic development program. We simply stopped all facilities for maintenance. That means we received a unique opportunity

to spend not just one month as usual for this, but all the three. In 2007, «Kazanorgsintez» reached all financials that were laid in business-plan. Talking about unfulfilled commitments, they are the commitments that were taken in excess of plan to increase the revenues and profit. Nevertheless, the Company showed 135% increase of volumes vs the level of 2006. The company's share on the domestic polyethylene market increased up to 40%. It should be said that in 2007 «Kazanorgsintez» reached the best financial results throughout its history. So, «Kazanorgsintez» entered the anniversary 2008 year: the Company celebrates in August its 50th anniversary of establishment and the 45th anniversary of the first product output.