RUSSIAN ENERGY COMPANIES IN CENTRAL ASIA

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Recently, the largest Russian oil and gas companies have turned their attention to Central Asia and have been developing their cooperation with the post-Soviet republics in various forms and with different results. Their successes will allow Moscow to recapture the positions that until recently looked as lost forever to Western rivals. The Russian firms stepped up their activity in 2001 when the geopolitical situation had changed dramatically: the counter-terrorist operation in Afghanistan brought American military bases to the region, while the United States started seeking closer political and economic ties with the new independent states.

Kazakhstan

Kazakhstan, the republic rich in mineral resources, resolved to attract as many investors as possible to its raw-material sectors, is one of the key Russia's post-Soviet partners and the most attractive Central Asian republic. LUKoil is active there; with dominating positions in the Caspian Region it also dominates oil prospecting in the Russian Caspian sector.

Until recently its presence in Kazakhstan was limited by its 2.7 percent of shares in the JV Lukarko, part of the Caspian Pipeline Consortium (CPC) that exploits the Tengiz-Novorossiisk oil pipeline. The company also owned 15 percent of shares of large gas-condensate fields Karachaganak in the west of Kazakhstan and 50 percent of the Turgai Petroleum JV that produce oil in Kumkol (the country's central part). However, LUKoil was not an operator of these projects, and the company has posed itself the task of concentrating on the projects in which it can obtain the operator status.

It was the Russian-Kazakhstani intergovernmental agreements on the delimitation of the national sectors of the Caspian signed in 2003 that urged LUKoil to act. Under the same agreement the countries decided to work jointly on the contestable and very promising structures Kurmangazy, Tsentral'noe, and Khvalynskoe. Having registered their parity involvement, each of the sides appointed a company responsible for the further development of the structures. There were no surprises: Astana appointed a state oil and gas holding Kazmunaygaz as an operator of the projects, while Moscow gave similar powers to several firms (LUKoil—Tsentral'noe and Khvalynskoe; Rosneft—Kurmangazy; and Gazprom—Tsentral'noe). Hypothetical reserves of the three structures have been assessed at about 1.5 billion tonnes of oil and over 800 billion cu m of gas. Their commissioning is expected in 2005-2006.

This delimitation allowed Kazakhstan to look for foreign investors for its hydrocarbon resources. The country plans to bring up annual oil production to about 150 million tonnes by 2015. In these plans Astana stakes on active development of its marine oil fields, especially the Kashagan field in the northern past of the sea, where AgipKCO discovered oil reserves amounting to about 9 to 13 billion barrels. According to the most conservative assessments, the field contains about 1 billion tonnes of oil. This is one of the largest fields in the world discovered in the last 30 years.

At the first stage, in 2004-2005 the republic intends to invite bids for about 23 promising plots, its marine sector containing 100 such plots. Kazakhstan plans to follow in the footsteps of Azerbaijan that starting in the mid-1990s has already concluded 15 production sharing agreements with foreign investors for several of its promising structures in its Caspian sector. Astana expects that its sea sector contains blocks similar to the Azeri-Chirag-Gunashli block of Azerbaijan where the AIOC international consortium headed by British Petroleum discovered the sources of about 5.4 billion barrels of oil.

Several large Western companies, some of them already working in Kazakhstan, have betrayed their interest in the coming bids, yet LUKoil outstripped them all. Within a very short period of time, in less than 12 months, it conducted a series of talks and signed an agreement with Astana. It is the first in the series of the marine PSA that are still being elaborated for Western investors. Early in 2003, even before the talks were concluded, LUKoil and Kazmunaygaz had signed a memorandum on cooperation in prospecting and extraction of hydrocarbons in the Kazakhstani and Russian sectors of the Caspian (the document covered the promising structures as well). In addition, Kazmunaygaz got the right to participate in prospecting in one of the blocks of the Russian sector of the sea. There is the opinion that Kazmunaygaz can be invited to work on the Iu. Korchagin field situated next to the Tiub-Karagan block covered by the agreement.

Active negotiations were crowned with a production sharing agreement for the promising Tiub-Karagan structure signed by LUKoil and Kazmunaygaz on 9 January, 2004 during President Putin's visit to Kazakhstan. This field is found on the northern Caspian shelf, to the northeast of the port of Bautino where AgipKCO has its supply base. To realize the project the sides will set up a JV on the parity basis that will carry out prospecting and extraction. The total reserves are estimated at 674.9m tonnes of oil equivalent, 466m tonnes of it being oil. The contract is signed for 40 years; capital expenditure will amount to $2.1 billion; operating costs, $1.7 million. The first exploratory well is expected to be drilled in 2005; the entire exploratory program presupposes seismic 2D prospecting and drilling of two wells. LUKoil will pay for this stage. The companies signed another agreement on studying the neighboring Atash (formerly, Kazakhstan) structure. The Russian firm agreed to shoulder the risks related to geological prospecting, the cost of which would amount, according to the firm's experts, to $150-170 million.

In April 2004, LUKoil launched 2D seismic prospecting in the contract area. According to the available information, by September the company had already studied about 1,712 sq km at the depths from 7 to 35 m. The service Kazakhstankaspiyshelf company with a rich experience of geophysical investigation of the Kazakhstani sector of the Caspian was appointed the contractor. The cost of this stage is assessed at $4.2 million. LUKoil has stated that seismic prospecting is expected to clarify the block's geological structure and prepare it for exploratory drilling.

Politically, this contract can be described as the first serious success scored by the Russian oil companies in Kazakhstan, the country rich in mineral resources. Before that LUKoil had to be satisfied with partnership in the projects dominated by Western firms. The Russian oil giant has captured a niche in this Caspian sector; since that time on it can expect new tempting offers from its Kazakhstani partners.

One more thing: LUKoil had managed to sign the agreement several days before the new taxation regime in the oil sector, which caused serious displeasure among the investors, was introduced in Kazakhstan.

The New Rules

According to the Ministry of Energy of Kazakhstan, in 2004 the republic will produce 55m tonnes of oil; in 2005, 60m; by 2015 it would be producing 150m tonnes every year (if the branch manages to attract no less than $54 billion of foreign investments). The steadily increased amounts of produced and exported oil and the steady flow of petromoney to the country's budget tempted Astana, late in 2003, to tighten the taxation regime.

In November 2003, the parliament's lower chamber (Majilis) adopted at the second reading a draft law that introduced a rent tax on exported oil that depended on the cost of oil, transportation costs and other expenditures (see Table). K. Atekenov, Deputy Minister of Economics of Kazakhstan, had the following to say in this connection: "We shall take into account the average weighted price … the oil brands close to the Kazakhstani brands fetch on the world markets. It is the task of the government to readjust them." The calculations of plant costs compensation and profit oil sharing have been tightened.

The new taxes are limited to the new projects the contracts for which will be signed when the draft becomes law. Before that the investors paid 16 percent VAT, royalties and certain excise taxes.

This came as an unpleasant surprise for investors; the foreign companies wishing to take part in 2004 tenders for new offshore projects expressed their concern. According to an employee of one of the companies already involved in an offshore project, the situation has obviously worsened; the investors have been left with a possibility of demanding taxation privileges for the most complex projects.

Table

New Oil Export Taxes

Average Price of the Basket of Brands ($/barr.)	Tax Rate (% of price)
0-18	0
19	1
20	4
25	16
40 and more	33

He sees no possibility of returning to the old regime; the investors, however, can obtain certain privileges for special projects and difficult geological conditions (in the Northern Caspian in the first place).

Investors are convinced that together with the threat of lower world oil prices the inflated taxes may undermine an interest of foreign firms in the Kazakhstani projects. The desire to raise the taxes is natural, yet the government should always bear in mind that the world prices can slide down; this will force many companies to abandon large-scale capital-intensive projects, related, in particular, to the sea's northern part.

Significantly, the new stricter taxation rules appeared in anticipation of the first bids for offshore projects planned for 2004. Discontent among the investors has already postponed them—they are expected to take place in 2005. Rosneft that had planned to launch the joint Kurmangazy project in 2004 was among the discontented. Late in March 2004 the company's President S. Bogdanchikov said that the new Taxation Code reduced the project's profitability to 8 percent, the level his company was not prepared to accept. He said, in particular: "The text of the production sharing agreement has been studied in minutest detail, yet if the new Taxation Code of Kazakhstan is applied to it, participation in the project will bring practically no profit."

Rosneft suggested that the intergovernmental agreement should be supplemented with a provision under which the PSA should be applied within the taxation regime that existed when the protocol had been signed. In April, Minister of Fuel and Energy of the RF Viktor Khristenko supported this position during his visit to Astana with no positive results. Premier of Kazakhstan D. Akhmetov said that Kazakhstan would not grant tax privileges to Rosneft, yet planned to sign the relevant PSA in 2004. His press secretary explained that the statement should not be taken to mean that Kazakhstan's position is a rigid one, yet he hinted that his country should not bear losses when it came to sharing profits. The premier also pointed out that his country counted on 70 to 85 percent of profitable products obtained in Kurmangazy.

Rosneft has found itself in a quandary: Kurmangazy, a border site between the Kazakhstani and Russian Caspian sectors, is an interstate project, therefore the company cannot drop it without lengthy preliminary negotiations with the RF government. "We do hope to reach a compromise and raise the project's profitability; because of its high status we cannot drop it all of a sudden." This comment came from a source in Rosneft who did not exclude a possibility of a compromise that might lead to signing the contract in 2004. In this way, Rosneft that depends on state policies was trapped in intergovernmental agreements of the two countries. If it manages to disentangle itself from the project, this may not only postpone the latter's realization but will also complicate the relations between Moscow and Astana that settled mutual claims in the Northern Caspian by signing in 1998 a delimitation agreement. Under this document the shelf stretches on both sides of the border will be developed jointly. The Kurmangazy and the neighboring Tsentral'noe and Khvalynskoe sites should be developed by the specially appointed companies of Russia and Kazakhstan: the state holding Kazmunaygaz and Rosneft. Another Russian company, Zarubezhneft, has already betrayed its interest in the project as well as Total of France. The hypothetical reserves are from 700m to 1 billion tonnes of oil; the project needs up to $10 billions of investments.

The three-year long preliminary period that will cost $50-70m presupposes seismic 2D prospecting in the contracted area and drilling of two exploratory wells. Astana planned to make one of the two in Kurmangazy within 2004, yet it seems unlikely that the sides will promptly settle all disputed questions. The tighter taxation regime (introduced when the republic's oil industry had left the initial period behind) looks logical. Kazakhstan is actually following in Russia's footsteps and, until certain moment, will be prepared to sacrifice certain geopolitical interests. The already raging conflicts with the shareholders of two other large projects (Tengiz and Kashagan) testify that the republic is not yet ready to agree to serious compromises; it may even tighten its demands on investors.

On the other hand, Russia and Kazakhstan are close geopolitically within the CIS, therefore the Kurmangazy problem will be probably resolved by the political leaders of the two countries.

Prospects for the Gas Sector

Despite the objective difficulties, the Russian companies still hope to carve a niche for themselves on the highly promising energy market of Kazakhstan. In February the Energy Ministry of Kazakhstan announced that Rosneft, in alliance with Gazprom, could be invited to take part in building a new gas processing plant at Karachaganak, a huge gas-condensate field.

According to Premier D. Akhmetov, Rosneft will be invited to the third, so-called gas phase, of the development of Karachaganak that contains 1.2 billion tonnes of oil and gas condensate and 1.35 trillion cu m of gas. Since the mid-1990s, a consortium of foreign companies Karachaganak Petroleum Operating (KPO) headed by BJ of Britain and ENI of Italy has been working in the field.

According to KPO expectations, the completed new capacities within the second stage (2003) that cost $4.3 billion will increase gas production from 5 to 14 billion cu m. John Morrow, the KPO president, has said that 6.6 billion cu m will be sent to the Orenburg Gas Processing Plant in Russia; 1 billion will go to Kazakhstan's domestic market, and another 6.6 billion cu m will be cycled. The KPO president added that further increase in production (to 18-25 billion cu m a year) is contained by lack of markets; therefore the consortium could concentrate on condensate production and limit gas production. The government of Kazakhstan, however, lobbied another gas processing plant not envisaged by the KPO contract obligations—hence a need for other partners.

Premier Akhmetov has said that the republic is resolved to develop its own gas processing and petrochemistry rather than continue exporting expensive raw materials; by the same token, Kazakhstan will free itself from its dependence on the Orenburg Plant. By the summer of 2004 Kellogg Brown & Root of the U.S. completed feasibility studies ordered by the Ministry of Energy of Kazakhstan for a new gas processing plant in Karachaganak with the optimal annual capacity of 400,000 tonnes of liquefied gas; the plant and an export pipeline will cost $1-1.2 billion; the project's realization will take about 3 years.

It is planned to build the plant in two stages with the annual capacity of each being up to 5 billion cu m; each stage will have its own gas storages and loading facilities to pour liquefied gas into car and mobile gas tanks. It is expected that the first stage will be completed in 33 months.

Today, it is commonly believed that site No. 7, about 23 km to the northeast of Aksai, in the Burlin District, is best suited for the plant construction. On the whole, according to the feasibility study, there are three suitable sites. The first is the Algabas railway station in the Terektinskiy District, Western Kazakhstan Region. There are several settlements nearby (Karabay, Shoptikol, Besagash, Karaoba), but all of them will remain within the 5 km wide sanitary-protective zone. The second site is found at about 27 km to the northeast of Aksai, 1.5 km away from the fields. The authors of the feasibility study are convinced that site No. 7 is best suited to all sanitary requirements: there are no settlements within the 9 km wide area; there are no sources of fresh water within the area either. This makes the site absolutely acceptable and safe.

It seems, though, that the local gas processing facilities will hardly allow Kazakhstan to completely ignore the Russian market; recently Gazprom, unwilling to let considerable amounts of gas escape its control, has been displaying a lot of interest in the Karachaganak project.

Today, Kazakhstan has to use Gazprom pipeline systems to reach the European markets; meanwhile, the Russian company closely controls the volumes of gas exports from Turkmenistan and Uzbekistan, where it buys gas for obviously low prices. Kazakhstan has already expressed its desire to sell its gas to Western Europe or to Russia at the accepted prices; this has already predetermined the partner for the new gas processing plant.

Gazprom invited Kazakhstan to set up a JV based on the Orenburg Plant's capacities; it expressed its readiness to transfer to the new JV several units with the total annual capacity of 8 to 10 billion cu m, two functioning pipelines connecting the gas fields and the Orenburg Plant, and other technological equipment. It is expected that Gazprom will offer Kazakhstan parity in the JV. At the same time, to process the Karachaganak gas and gas condensate in Orenburg the local plant should have to increase its capacity just a little, while a new plant at the field will cost more and will take a lot of time to be completed. According to Gazprom's experts, construction will cost about $1.3 billion, while the Orenburg project was assessed at $300m.

The Ministry of Energy of Kazakhstan says that the republic prefers to have its own gas processing plant; they have to admit, however, that construction will cost a lot; the payback period may take up to seven years. Marketing the products will also cause problems that can hardly be resolved without Russia.

It seems that Astana will opt for a political decision: a JV together with Gazprom on the basis of the Orenburg Gas Processing Plant. This will solve the problem of marketing and relieve the republic of its complete dependence on its foreign KPO partners the relations with which have been going from bad to worse, which may seriously affect the republic's plans for the future. For example, last July a conflict around supplies of gas condensate from Karachaganak to Orenburg flared up. The financial police of Kazakhstan opened criminal proceedings against BJ Karachaganak Distribution, a BJ daughter. It was accused of smuggling in 2001-2003 from the Karachaganak fields to Russia unstable gas condensate to the total sum of nearly $2.7 billion. The Russian Company Orensal that bought and processed condensate at the Orenburg plant was also accused.

If the conflict develops, Astana may fine the BJ Karachaganak Distribution or arrest certain amounts of products, say, part of the condensate delivered to Orenburg or sent to the CPC. In this case, pressure of the republican authorities on the foreign investors may be explained both by the talks under way about BJ's intention to buy 16.67 percent of shares in the Caspian Kashagan project and by the discussions about the best site for the new gas processing plant. The doubtful conditions under which condensate was delivered to Russia and accusations of smuggling can serve as another trump card Astana may lay on the table when discussing a new plant.

At the same time, Gazprom is prepared to buy shares of the republic's gas transportation system (if and when they reach the market). According to Deputy Chairman of the Gazprom Board of Directors A. Riazanov, not only Moscow (and, therefore, Gazprom) will profit from this, but also Astana. Said he: "We look at Kazakhstan as an important transit state, in the first place, therefore we are following closely how its gas transportation system is developing. Its capacities do not meet our requirements… Russia has serious contracts with Uzbekistan and Turkmenistan that will require large transportation transit capacities to move Uzbek and Turkmenian gas to Russia via Kazakhstan." He has said that starting in 2007 these volumes will never be below 70-80 billion cu m a year. (In the first six months of 2004 Gazprom moved across Kazakhstan 20 billion cu m of Turkmenian gas and over 2 billion cu m of Uzbek gas.)

Joint-stock company KazTransGaz in which 100 percent of shares belong to the state controls the main gas pipeline system of Kazakhstan (10,000 km of pipelines). Today, it is engaged in an investment program that concentrates on re-establishing the transit capacities of the main gas pipeline Central Asia-Center (CAC); its modernization is expected to take 10 years and will cost about $1.3 billion. The company plans to invest over $500m until 2005; it expects to invest its own funds and tariff incomes, invite international financial groups, and borrow from banks of Kazakhstan.

The strategic interests of the Russian monopolist and Kazakhstan are identical: they both need greater carrying capacity of the CAC, which is today 45-50 billion cu m a year because in 2003 Gazprom signed a long-term contract with Astana in anticipation that by 2007 it would buy up to 70 billion cu m of gas from Turkmenistan (as against 5 billion bought today). In 2004, Gazprom announced that it was prepared to invest over $1 billion in developing gas fields in Uzbekistan.

So far, officials in Astana say that the republic's gas transportation system does not need privatization. According to N. Rakhimov, General Director of KazTransGaz, "there are no problems in the gas transportation system that would require Gazprom's involvement." Observers are inclined to interpret these statements as preparations for negotiations with Gazprom in which Astana may try to exchange its participation in privatization for certain concessions in other projects.

Uzbekistan

The republic is rich in oil and gas: 190 energy fuel fields have been discovered; 94 of them contain gas and gas condensate and 96 are oil and gas, oil and gas-condensate and oil fields. Forty seven percent of them are functioning; 35 percent are ready for functioning; on the rest prospecting is still going on.

Uzbekistan is the third among the East European and CIS countries where the prospected natural gas reserves are concerned; it has the fourth largest deposits of liquid hydrocarbons. Its assessed gas reserves are 2 to 5 trillion cu m; oil, 5.3 billion; gas condensate, 480m tonnes. Today, the republic produces about 58 billion cu m of gas a year (it exports no more than 10 billion cu m; the rest is consumed at home). The republic is far removed from the world markets, which considerably limits its export potentials. In addition, Uzbekistan needs foreign money to properly develop its gas fields—this opens the doors to foreign, Russian in the first place, companies. As distinct from Astana, however, Tashkent never posed itself the task of attracting Western money in large quantities.

The expert community believes that separated from the neighboring countries (Turkmenistan and Kazakhstan) investments in the Uzbekistani gas sphere might prove ineffective because of the country's geographic location. In fact, in the mid-1990s this frightened several potential investments away; until recently the oil-and-gas niche remained vacant.

Obviously, any potential investor with an interest in the Uzbek gas should seek a unified strategy for the three countries—something that Gazprom has been doing for the last two years. An agreement of 2003 for the period of up to 2012 the company signed with the government of Uzbekistan presupposes joint development of gas fields and deliveries of gas (5 billion cu m a year up to 2005 and 10 billion cu m a year starting in 2010). The CAC main pipeline that connects Russia and Turkmenistan heightens Gazprom's strategic interest in Uzbekistan.

In December 2002, Uzbekneftegaz and Gazprom signed an Agreement on Strategic Cooperation for the Period of up to 2012 under which Uzbekneftegaz and closed joint-stock company Zarubezhneftegaz (set up in September 1998 with 60.1 percent of shares belonging to Gazprom; 24.9 percent, to Zarubezhneft, and 15 percent, to Stroitransgaz) signed a PSA on the investment project "Additional Development of the Shakhpakhty Field in the Ustiurt Oil and Gas Bearing Region" on 14 April, 2004 in Tashkent. This field was discovered back in 1962; its reserves are assessed at 39.9 billion cu m of gas; today, recoverable reserves amount to about 8 billion cu m. In February 2002, production was discontinued because of depleted equipment.

Under the above agreement, Zarubezhneftegaz should invest over $15m in modernization of infrastructure; the sides will divide the profit equally among themselves. It is planned to resume production in the latter half of 2004, to complete construction within 2004 and to develop it further for 13 years more (it is expected to produce 500m cu m of gas every year starting in 2005). By the end of 2004 the investor is expected to complete the booster compressor station. This will make it possible to produce, starting in July 2004, 200m cu m of natural gas and send it to the Karakalpakia compressor stations of the CAC for export. In 2005, annual production and export of gas will reach the figure of 400m cu m.

The Russian company has just signed its first agreement in Central Asia on gas production; in the middle term this will allow Gazprom to move away from resale of gas to its production. This will mean a new stage of its business in the region, restoration of the Soviet chain of geological, extracting and transportation assets, and Gazprom's stronger exporting potential and closer economic relations with its Central Asian partners. It is expected that within 2004 Uzbekneftegaz and Gazprom will sign another production sharing agreement on developing the gas condensate fields in the Ustiurt Region; its total cost is about $1 billion.

It is interesting to note that Itera was the first Russian company to reach Uzbekistan; together with LUKoil it spent many months negotiating a PSA for Kandym-Khauzak-Shady block in the south of the country. The volume of known geological reserves in the contract territory is 283 billion cu m. The reserves of the largest of them, the Kandym fields, are over 150 billion cu m. However, in 2003, Itera folded up its business in Uzbekistan and closed its office in Tashkent: it lost to Gazprom in stiff rivalry. Gazprom practically monopolized not only Uzbek but all Central Asian gas exports.

LUKoil finished the talks about Kandym-Khauzak-Shady alone. On 16 June, 2004, during President Putin's visit to Tashkent, the Russian oil giant signed a product sharing agreement with Uzbekneftegaz for gas production in the Bukhara-Khiva region, in the republic's southwest. The agreement was signed by Chairman of Uzbekneftegaz A. Azizov and LUKoil President V. Alekperov. The partners will set up a JV with 90 percent of Russian and 10 percent of Uzbek shares. LUKoil had increased its share from 70 to 90 percent six days before the contract was signed. The agreement was signed for 35 years; total investments will reach about $1 billion. Industrial production will start in 2007. In this way LUKoil has become the second Russian company that realizes a project in the oil-and-gas sector of Uzbekistan under a PSA.

The maximal level of annual production in this project will reach 9 billion cu m, while the total accumulated volume of production may reach 207 billion cu m. A state-of-the-art gas chemical complex with an annual capacity of 6 billion cu m is planned; its first phase being commissioned in 2010; 240 development wells will be drilled; over 1,500 km of pipelines will be laid. Two more compressor stations are planned to be built together with gathering stations, shift settlements, high-voltage power line, a railway about 40 km long, highways and approach roads. Gas will be transported through main gas pipelines operated by Gazprom. This will ensure the Russian monopolist an indirect role.

The feasibility study of the project was supplied by the UzLITIneftegaz Institute, a daughter company of Uzbekneftegaz; the PSA was elaborated by Baker & McKenzie of the U.S. Both documents were approved by the Special State Commission of the republic set up to formulate the conditions of the use of mineral resources and examine PSA drafts.

The largest Russian oil and gas companies gained domination in the fuel and energy sector of Uzbekistan—something that none of the foreign investors had achieved so far—because of their active position. In Kazakhstan, however, the Russian firms will compete with the world's largest companies—ChevronTexaco, ENI, BG, and others. In Uzbekistan, the coordinated efforts of the Russian companies and control over the transportation lines (production-transportation controlled by Gazprom and LUKoil) will allow Russia to build up more effective geopolitical relations with Tashkent. So far, Uzbekistan is the only Central Asian country in which Russian companies have not yet encountered objective problems.

Turkmenistan

Russian companies started their expansion into the marine sector of the republic at a time when the majority of Western giants and medium-sized firms believed investments to be too risky for their taste. The political factor is not the only problem: prospecting and development of the republic's marine sector is hampered by depleted oil infrastructure and its obviously inadequate development. It was Azerbaijan that inherited from the Soviet Union the entire park of drilling rigs, pipe-laying barges and assembly sites. Its relations with Turkmenistan are far from simple. For the same reason the republic cannot develop the debatable Kiapaz (Serdar for Turkmenistan) site on which Ashghabad signed several agreements (with ExxonMobil of the U.S. in particular) in the 1990s. Having reached no progress in its talks on Garashyzlyk 2, the company left Turkmenistan altogether.

Today, the republic is developing several projects, some of them under PSA, that involve Dragon Oil of the UAE and Petronas of Malaysia. According to Turkmenian experts, in the near future their investments will reach the figure of about $3 billion.

In an effort of attracting more foreign money to its marine sector, the government elaborated a Licensing Program for the Turkmenian Caspian Sector up to 2010 that envisages tenders for 32 highly promising blocks (discovered through seismic exploration). The investment climate, however, does not allow the republic to expect large investments. In addition, the republic concentrates on gas production and its main reserves are found on the continent.

In Uzbekistan and Turkmenistan Russian oil and gas companies can successfully replace Western investors that either left the country or never came to it. Gazprom, which in 2003 signed with Ashghabad a long-term agreement on purchase of fairly large amounts of natural gas, was the first of Russian investors.

In 2003, Ashghabad reached, in principle, an understanding on a marine project, with considerable potential economic and political dividends. Zarit, a consortium of Russian companies Itera (37 percent), Rosneft (37 percent) and Zarubezhneft (26 percent) started developing a PSA for prospecting and developing blocks 27-30. According to the results of seismic prospecting, this Caspian sector is the sea's richest in hydrocarbon resources. According to independent experts, it contains 11 billion tonnes of oil and 5.5 trillion cu m of gas. With the help of this project Russian oil companies would strengthen their positions in the republic's oil and gas sector and take part, for the first time, in developing its shelf. The reserves of the contract area have not been identified, yet, according to specialists, in peak years the four blocks will produce about 15m tonnes of oil a year.

It was planned to sign the agreement on 12 December, 2003 after which Zarit would have been able to start drilling the first exploratory well in 2004. But because of certain disagreements the contract was to be signed in February 2004. The operating margin of each of the participants and its distribution was one of such problems. There is another problem hard to overcome: the contract area is adjacent to the Iranian sector of the Caspian; what is more, part of it is found in the Iranian sector. The Russian side is convinced that Iranian oil firms should be invited to take part in the project. So far, official Tehran is in no haste of accepting the invitation; it prefers first to delimitate the national sectors and reach an agreement on the sea's legal status.

Iran's irreconcilability on this issue is too well known: the country that has no offshore hydrocarbon reserves in the Caspian insists on an equal division of the sea among the five Caspian states in order to gain control over several promising oil and gas blocks now owned by Azerbaijan and Turkmenistan. Until the final documents are signed Iran refuses to recognize any oil-and-gas agreements on the Caspian as legal. To avoid disagreements, Russia invited Iran to join the project as a shareholder—Tehran answered that until the sea obtains its legal status and the national sectors are delimited it would keep away from the Caspian projects and would never look at them as legitimate.

Viktor Kaliuzhniy, special representative of the RF president for the Caspian issues, actively defended the interests of the Russian companies. Back in 2003 he said that Iran's involvement in Zarit would be greeted. He said that its involvement would accelerate the project because Iran was convinced that the blocks were found in the debatable zone.

Mehti Safari, Iran's special representative for the Caspian issues, said on 17 March, 2003 in Baku that his country would never enter into any bilateral or trilateral agreements with its Caspian neighbors and that it was ready to sign a five-sided agreement on the sea's legal status.

This practically stopped the project in the same way as the ExxonMobil and BP projects had been earlier discontinued in the southern part of the Azerbaijanian sector (the exploratory blocks Savalan and Alov). An official of one of the Russian companies involved in the Zarit consortium said that until Tehran agreed to participate in the project all other agreements would remain meaningless and that no exact date of signing the contract can be named.

Obviously, if Russian diplomacy manages to overcome these obstacles, Zarit will become the first project on the disputed territory that will bring together Iranian, Turkmenian and Russian oil companies. There is a lot of skepticism, however, in the expert community about a consensus on the division of the Caspian based on the principles already registered in the agreements between Russia and Kazakhstan, Russia and Azerbaijan, etc.

The situation will aggravate if the project is started without first settling the relations with Tehran. A political decision is one of possibilities—this has already happened with Kurmangazy project in Kazakhstan. Today, however, Moscow and Tehran have other problems to discuss: cooperation in the sphere of nuclear technologies and another crisis in the relations between Iran and the United States.

Observers are convinced that despite the old trade contacts Russia and Iran have not become close diplomatic partners: they share common approaches on certain issues, yet disagree on other issues (development of energy resources and export routes). Even though the two sides are united to curb the mounting Western influence (the U.S. influence, in the first place) in the Caspian, the two countries remain rivals when it comes to exporting considerable amounts of Turkmenian gas, which will interfere in coordinating their political efforts for several years to come.

So far, Russian presence in Turkmenistan is limited to the purchase by Gazprom of large amounts of gas. The Russian firm drove away all other serious users of Turkmenian gas (at least for the near future) as well as more ambitious projects (pipeline to Afghanistan and Pakistan or a trans-Iranian gas pipeline that branches off to Turkey and Europe) for a longer period.

Conclusions

After several years of inaction Russian oil and gas companies managed to return part of their positions in Central Asia. They look at the most promising Central Asian market as a means of diversifying their business risks, expanding their influence to new regions and withstanding rivalry with Western firms.

This is promoted by the growing ambitions of the Central Asian countries that make new requirements of their Western partners, as well as by the traditional geopolitical closeness between them and Russia. Political factors and the level of cooperation between the state structures will undoubtedly help resolve certain problems. The already functioning transportation routes and the huge market will help Russia (through its companies) gradually strengthen its positions in the region and resolve some of its geopolitical problems there.