Welcome Address to Participants of FT Global Summit 2016
by I.I.Sechin, Chairman of the Management Board of Rosneft Oil Company

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Dear participants of the Summit,

First of all, I would like to express my appreciation to Mr. **Lionel Barber**, Financial Times' Chief Editor for the invitation to participate in this significant forum. It is a great honor for me to be in this hall with eminent businessmen, colleagues and friends.

Using this opportunity, I would like to briefly share with you my vision of our common concerns and the challenges we are facing on the current extremely volatile market.

I greatly respect your highly professional work. It is extremely important for the market, and its role and even responsibility are constantly on the rise.

Let me make a usual disclaimer, since even in such a brief welcome speech I will have to express **evaluative judgments**, because I will speak of the areas which concern all of us, and you, of course, are interested not only in the facts, but also in **my evaluations and conclusions**.

Over the past few years we essentially have witnessed a **change in the paradigm** in the oil market: for a long time it has been a common belief that OPEC is regulating the oil market; then, owning to groundbreaking technology innovation, a new regulator appeared which is the shale oil production in the USA. However, in our opinion, the new reality is that the market movement is increasingly determined by a combination of factors, including availability and quality of resources, impressive progress in developing and applying the most advanced technologies on **the physical market**, plus development of financial instruments and financial technologies, **actions of regulators.**

Moreover, a specific feature of today's environment is a stronger role of trading, which is rapidly raising its effectiveness under difficult conditions, making a **significant effect on the market**.

Trading arsenal aimed at efficiency is very much in demand under high volatility conditions; it includes potential for swop operations, long-term contracts and exchange trading, contango effect, optimal use and development of transport, storage and handling, in-depth understanding of logistics and conditions on operation on the consumer markets, production, financial and other tools. It is the trading companies that work with both physical volumes and derivatives in the financial markets, **creating a common platform** linking different elements of the market. Moreover, recently trading companies have started being active in production, processing and even in retail and this has become their specific feature. Here I would like to note operations of famous traders like Glencore in production, Trafigura in retail, Vitol in refining and retail.

Here we have the participants from different commodity markets. Briefly I would like to say that the oil and oil products market even after a drastic fall in the oil prices, still is most substantial in terms of value of its physical deliveries among these markets. The reason for this, in our opinion, is that, along with food market, the oil market is less flexible and it is aimed to meet the population vital needs and the needs of economy as a whole.
Oil along with gold also has a leading position with respect to the volumes of financial transactions on these markets. Commenting on the extent of the oil financial market's structure optimality and its perspectives is the subject of a separate review.
We heard a lot about the theory of "end of a super-cycle of high raw material prices" and a move into the era of "a super-cycle of low raw material prices", which, allegedly, can last for 10-15 years. I will immediately say that with regard to oil prices I do not support this concept. It is true that for a number of reasons we are facing a low price phase, but, as we will discuss briefly today, it cannot last long. It cannot last long at least by the major reason - current prices do not secure the complete cost cycle, i.e. they generate losses for the companies, that work at complex fields. And there are many fields like these.
Production will decline due to decommissioning of production assets unable to cope with the current price pressure.
The current phase of the market development is also featured by a stronger effect of the set of financial instruments.
I would like to emphasize that we have never supported extremely high oil prices either, and according to **Ben Bernanke**, a reputable expert, 'weak dollar policy' used by the US Federal Reserve made a noticeable impact on the oil price rise. A change in this policy made a comparable contribution to today's downturn in the oil prices.
Therefore, it has been acknowledged at the high expert level that oil contracts reference to US dollar was not the factor of oil market stabilization. It means that use of multi currency pricing at the oil markets and first of all in the regional transactions is becoming more and more important.I hope that it will be interesting to discuss these matters, including development of relevant financial instruments for mitigation of risk and hedging with participation of recognized specialists in the financial sector.

However we should not overestimate the role of changes in the dollar exchange rate in the oil price fluctuations. We can see often that a change in the dollar exchange rate or S&P 500 fluctuations by **one percent** are followed by an upturn in the oil prices by **five and more percent**.
Substantial excess of supply over demand is a decisive factor in the sharp downturn in the oil prices. Today the view is that excessive supply will be handled **within two years**; within this period, the surplus will be set off as a result of the

growing global economy and consumption, depletion of the existing fields, suspension of difficult and insufficiently efficient projects.

Therefore, it will take some time to have a well-balanced market that we believe is inevitable. During this period, the market will be characterized by a continued significant volatility, and in order to make appropriate decisions, an in-depth analysis of short-term and long-term factors, and a sound judgment about the significance thereof will be required.

I would like to draw your attention to the investments factor that plays the key role in the oil industry, which is much more important than with other Commodities. We see very substantial reduction of investment activities - for more than USD 250 bln already, and it will have long term implications.

Oil and oil products demand is going up stably enough - by 1.3-1.8 mln bpd per year. It is possible that with moderate oil prices this growth will keep pace with at least additional 1.2 mln bpd annually and additional 6 mln bpd annually will be required by 2020 compared to 2015. Moreover there is annual capacity decline of no less than **3 mln bpd** at the producing fields.

Who will be able to fill in the gap between the growing demand and available supply?

If we look at non-OPEC countries, we will see that a number of major projects under implementation to produce conventional oil were launched during the period of high prices are still continuing to increase the product output, or are beginning to stabilize their production. Among other things, it is also true for production of “expensive” oil (such as the deep-water shelf of Brazil and US or bitumen sands). This is **the investment process momentum** in the industry. At the same time, a broad-scale slump in investment activities is under way, and new projects of such nature or subsequent phases of the current projects will not be launched for a long time yet – until the prices settle at levels that create a sufficient “safety bag” that will, according to investors’ opinion, guarantee their economic efficiency. So, it is hard to expect any supply growth from this side within the period of until 2020.

Everyone is talking about such major source of new supplies as US hard-to-recover (shale) oil. Currently its production is declining despite employment of both preferential tax treatment and a broad range of financial instruments available in the USA for production support.

This fall will continue in view of the prices expected within the short-term perspective. Apparently, WTI price levels over 45$/bbl or even 50$/bbl, will be required to stabilize shale oil production.

At the same time, we can see financiers’ disappointment in sustainability and prospects of this sector, which dampens their willingness to undertake any new large scale investments therein. A number of companies in the sector have found themselves in a very difficult financial situation being burdened with high debt liabilities. Therefore, here also, as we see it, the **response to a change in the price situation will not be instant, and it will be softened**. It is even more important that according to the conclusion of official US sources like the US Energy Information Administration (EIA), US Department of Energy, even with much higher price levels the potential for the US shale oil production growth is limited – it cannot exceed **2-3 million bbl/day**.

On the whole, the economic indicators of shale production are improving, primarily on account of ongoing technological improvements.

I will say that full costs have not been calculated yet; in fact, there is no experience in the shale oil-field decommissioning meeting the environmental restoration requirements used in conventional oil production. However no one will be surprised, if special preferential conditions in this respect are also put in place for shale oil production.

At the same time, so far there is no major success in the attempts to repeat the phenomenon of the US shale revolution in other regions and it is difficult to expect the success also, since there is no combination of favourable conditions typical for the US elsewhere. Moreover, it is very unlikely at the current price levels on the market. Entering new regions and starting to develop such resources under other geological, technical and economic conditions will take time and they are really expensive.

This quick overview demonstrates that the demand for additional production will be back in place within three or four years.

Thus there is a bigger need for the market analysis, adequate information on the market position and its trends. This is the area where we can focus our efforts. For example, let’s look at the changes in both US oil production estimates (that’s clear, since making projections under trend changing market conditions is never easy), and the actuals, statistic data on this production. Market participants cannot wait for months for more reliable information to appear - they should respond to it immediately.

Estimates in respect of the major factor of excessive supply also change. Moreover, there is an impression that these estimates are sometimes "backdated” and adjusted to the market price changes.

Unfortunately, these estimates as well as other information "reasons” reflect the interests of the market participants and their representatives. The importance of this Summit in particular is that its organizers have created **a professional platform for the information exchange for a maximum number of participants** with a view to develop an unbiased fair presentation on the commodities markets.

I wish successful work to all participants.