

THE SPEECH OF I.I. SECHIN
TOWARDS IDEALS OF EURASIAN INTEGRATION
AT THE X EURASIAN FORUM IN VERONA

October 19, 2017

Dear participants and guests of the Forum,

It has become a good tradition to meet in these October days here in Verona in Palazzo della Gran Guardia to compare notes and define new trends in the development of the economic integration in the Greater Eurasia.

I would like to specially note the role of Italy in this discussion which make a significant practical contribution to the Eurasian dialog and mutually beneficial cooperation. I would like to thank the State Secretary of the Council of Ministers of Italy Maria Elena Boschi for her attention to the Forum, esteemed Mayor of Verona Mr. Frederico Sboarina and organizers of the jubilee 10th Eurasian Economic Forum for creation of excellent conditions for our work. I would like to address my special words of gratitude to our great friend and main organizer Antonio Fallico.

It should be noted that the agenda of the Forum has significantly evolved over the recent years. Today people from various spheres who determine many solutions of political and economic issues in their countries gathered here. I would like to greet our friends with big political experience. They are Romano Prodi and Gerhard Schröder, our partners - directors of major companies - CEFC CEO Li Yong, Chief Executive Officer of Glencore Ivan Glasenberg, Jeremy Weir from Trafigura, Emma Marchegalia from Eni, Stefano Kao from Saipem, Chief of QIA His

Excellency Sheikh Abdullah bin Mohammed bin Saud Al Thani. I would like to separately greet deeply esteemed Special Advisor to the Minister of Economy, Trade and Industry of Japan Hirofumi Katase, Minister of Natural Resources of Iraqi Kurdistan Ashti Hawrami. Of course I would like to warmly greet my colleagues and friends from Russia. The State Secretary of the Union State Grigory Rapota, our ambassadors - Permanent Representative of the Russian Federation to EU Vladimir Chizhov, Russian ambassador in Italy Sergey Razov attend this meeting as well as Head of Gazprom Export Elena Burmistrova, businessman Oleg Deripaska, Head of Novatek Leonid Mikhelson, Managing Director of Nordstream Matthias Warnig, Chairman of Pirelli Board Marco Tronchetti Provera and many others.

The special talent of the Forum organizers is expressed in the choice of its time - the 19th National Congress of the Communist Party of China opened yesterday which will take important decisions about further development of this largest global economy and the Chinese society; today Russian President addressed to the international expert audience at the Valdai Forum. I hope that we will be able to take the messages of these great global leaders in our discussion, analysis and forecasts.

The year was very rich in serious events and for this reason my speech will be very thorough. I will tell you in secret that this is the fortieth version of the speech.

I would like to traditionally note the limitation of liability due to the presence of estimates and forward-looking judgments in the report.

CHANGING DEMAND OF THE GLOBAL ECONOMY

Development of Energy Sector and Joint Infrastructure Projects are the Most Important Factors of the Eurasian Integration For this reason I would like to start the discussion with analysis of the oil market. **I can assure you that the rumors about the “death” of oil are greatly exaggerated. Oil will remain the backbone of the world's fuel industry and for the future 20-30 years and more ahead.**

We are convinced of the sustainability of the growth in demand for hydrocarbons, due to the growth of the economy and the standard of living. The expected rate of world economic growth, especially in developing countries, in the coming decade will require further growth in the supply of liquid hydrocarbons by 0.7-0.8 million barrels per day annually, Growth will continue in the future, and I would like to note that growth of demand for energy resources will entail not only the corresponding production dynamics but it will also have a serious multiplicative impact on the development of associated economy sectors. The higher is the added value in the oil and gas industry with respect to production of sophisticated petrochemical goods the more high tech and science - driven will be the development of the related industries.

The share of liquid hydrocarbons in the global energy consumption structure over the long term will be slowly decreasing but still it will be rather high - around 30% of the global consumption of the primary energy with increase of the physical volumes. Some decrease of the oil share in the general balance will be almost completely offset by the growth of the share of gas and extension of the oil product chain, primarily, based on the petrochemicals; while reduction of the share

of coal will be compensated by the growth of the share of the cleaner energy sources including gas generation and possibly nuclear power generation.

Evidently, there are traditional challenges in the oil market. One of the main tasks of the today's forum is to try to find answers for them in the interests of the entire Eurasian community.

The challenges primarily include the prevalence of the financial speculations over the long term interest of the development of the industry. **The dominance of the financial players and short term speculative operations results in the excessive volatility of the price indicators. Unfortunately, this damages long term interests of the industry.**

Over the last 10 years the share of participation of financial players in the oil pricing has significantly increased. The size of the non-deliverable futures market exceeds the size of the actual market where physical volumes are traded more than 11 times and in dozens of times it exceeds the volume of physical deliveries. Such disproportion results in the excessive influence of volatile instantaneous expectations of the financial participants of the market and prevalence of the short-term financial speculations over the interests of the development of the industry. Majors and other public companies has a strong focus on tracking short-term price indicators and in the result they take into account speculative volatility in the investments plans. That is very dangerous. For example, in 2014-2016 the investments in the exploration drilling of major companies dropped 2.7 times - now we see accelerated recovery. But how can you justify such upswings in the industry with a long-term investment plans?

And for our part taking into account long-term interests of the

industry we see our goal in neutralizing whenever possible the volatility of the market, approaching the task of meeting the long-term the demand of the global economy in a profound and responsible way.

I would like to note the cases of irrational actions of the global and regional regulators. Very often regulators decide to implement regional, interregional or industry-specific sanctions, which corrupt market nature of the industry, primarily creating space for speculative and intermediary operations. The risks of removing certain volumes of oil from the market due to artificial limitations make a loss for everybody. Such steps are taken with damage to real energy security and customers' interests usually pleasing only conjunctural political agenda

Also accelerated development of electric cars when marginal source of electric power in many developing countries is a coal generation can result in the fact that actual environmental damage of transition to electric cars will be significantly greater than status quo. The issues of safe production and disposal of components of electric motors, quality, endurance, capacity and reliability of batteries.

I would allow myself a question for general discussion - is it better for regulators to focus more not on the limitation of the use of internal combustion engines and non-economic measures for their abandonment but on the accelerated reduction of the share of coal generation and expansion of the usage of environmentally safe gas fuel or nuclear power?

Where are the regulator measures for addressing these tasks?
Eventually, the customer pays for not well-thought decisions of a regulator. Today this price is rather high.

Non-market regulation can significantly degrade the economics of investment projects and will increase the cost of production of energy resources.

Then there is a problem of the stock "overhand" which means the absence of a transparent and single methodology of collection of statistical data, understanding of the inventory balance in the world.

A significant surplus of the oil and oil product inventory has been formed since 2014 due to surplus supply in this period in comparison with the demand. **Despite increase of consumption and reduction of surplus inventories by 60 MM bbl over 9 months after signing OPEC+ agreement it is only 25% of required reduction for reaching the average level of 2012-2016. The analysis shows that the declared goal of normalization of the level of inventories is not fully reached and it is too early to speak about the break.**

I would like to note that stock overhang is not an independent phenomena but it is a manifestation of other factors in the market. **The surplus of production over the demand formed in 2014 gradually was leveled through production limitations introduced by a number of countries and rather fast growth of global demand for liquid hydrocarbons. But this balance is very delicate and shaky - shale production in the US has a lot of drilled but not completed wells. With certain price levels they can greatly increase the production and destabilize the market. So I think we shouldn't wait for a rally in oil prices in the near future.**

The work for stabilization of the market is complicated by the absence of reliable and transparent information and analytics both

with respect to the stock and real situation with demand and supply balance. This creates ground for speculative market manipulations for short-term benefits. The key tasks here is to create a single system of measurement of stock and overcome the stock overhang problem.

Unfortunately we can see that some strategic market deals, such as Saudi Aramco's IPO, that can increase the transparency of market information on reserve volumes and prospective volumes of production, may risk not to become a fully-fledged international listing because of different factors, first of all due to certain legal risks. The scenarios of private share placement or local listing, which are being discussed today, unfortunately, will not achieve the goals, which the organizers had initially set out.

The challenge of desynchronization of the global economic cycle and investment cycle of the industry is also important.

The global economy has accelerated recently. However, due to processes that we noted the investments in the oil and gas industry significantly dropped. The industry is still in confusion, a number of projects are not implemented due to high uncertainty which can result in the inability to meet the growing demand for energy resources. A number of projects being implemented such as Australian LNG plants Gorgon and Wheatstone are commissioned but they do not have even minor changes to pay back amid the current and predicted price levels and potentially interrupt the stable trend of market development. Thus, the funds were distracted projects with higher investment efficiency which eventually will be paid for by end customers.

Finally, the serious challenge is the fact that a number of

producers focus on the short-term horizon for maximization of the current profit.

In this connection I would like to draw your attention to the fact that short term planning horizons and focusing on the current revenues compromising the long-term stabilization of the market cannot be a form of a responsible behavior of producers.

Also I would like to comment on the stability of the shale industry. According the recent report from Wood Mackenzie five major shale producers in the USA (Continental, Devon, EOG, Newfield, Pioneer) which are grouped into a synthetic Tight Oil Inc. face significant financial problems: these companies in 28 out of 29 quarters since 2010 have generated a negative net cash flow. But these companies in 2010-2016 spent more than 50 bln. USD on exploration and M&A deals!

Historically high infrastructure costs and significant drilling volumes determined the specific amount of investments in the development of the shale oil which is by one third higher than the conventional oil project parameters. The industry will generate positive cash flow not earlier than 2020 provided that oil price will reach 70 USD/bbl by this time.

Taking into account growing investment costs and OPEX a reasonable question arises what will end sooner - a period of low oil prices or the patience and hopes of investors?

Amid the current uncertainty of the outlooks of the development of the global oil market and risks of reduction (persistence) of the oil price swings the stability of the economic models of key market players becomes a top priority. The issue of stability of the economic models applies primarily to producers with the 4th cost quartile including deep

water shelf oil producers, Canadian heavy oil sands producers, producers of the shale oil outside the Permian basin and others.

It should be specially noted that our company is a leader of the industry in terms of hydrocarbon production costs. Our production costs amount to around 2.5 USD/bbl. At the same time the amount of our hydrocarbon reserves is almost two times greater than that of the following public oil company. Given our high reserves to production ratio and record low production costs we can focus on the long-term strategic tasks faced by the industry in general - our goals to the maximum degree are aligned with the tasks of improvement of the energy security of the anchor customers.

Our key priority of meeting the growing demand of the Eurasian economies which is very organic and creates a lot of opportunities both in the traditional liquid hydrocarbon consumption markets and in the new growing points of the global hydrocarbon business.

We believe in the future of our main oil market, but at the same time we evolve together. Thus, the most perspective way of demand for liquid hydrocarbons development is into petrochemical industry.

Just have a look around you, we are surrounded by the products made from oil and gas such plastic, construction and building materials, fertilizers. The demand for them consistently increases.

Namely, while the annual average growth of oil product consumption over the last 5 years amounted in average to 0.95 the consumption of petrochemical products annually grew at 3.9%. And it occurred despited the crisis in the global economy.

It is expected that by 2025-2030 the increase of oil demand from petrochemical industry should prevail over demand of the main consumer of oil products - transport sector.

The petrochemical products in average have the highest added value among all products made from oil and gas - their cost in times exceeds the price of the feedstock used to produce them.

The availability of efficient feedstock ensuring competitiveness in the global market, goods demand outlooks in the world and in Russia, vicinity of the sources of this feedstock to the largest and growing markets of the Asian-Pacific Region make the petrochemistry a prospective and important area for our business.

The other point of growth - natural gas, one of the most environmentally safe and accessible sources of energy.

We implement major gas projects in Russia such as Rospan, Kharampur, Kynsko-Chaselskaya group which bring us to the second place in terms of gas production in Russia after Gazprom. At the same time we implement the largest Zohr gas project in the Egypt shelf jointly with our international partners. Additionally, significant growth of the production of liquid gas fractions creates conditions for development of major petrochemical centers in the Volga region, Eastern Siberia and in the Far East.

CENTRAL ROLE OF EURASIA IN THE MODERN ENERGY SECTOR

Our Company implements projects all over the world focusing on the development in the Eurasia.

Eurasia is not just the largest and the most populated continent. This is the heart of the civilization, its driving force, economic and energy power. Suffice it to say that around 70% of the global population lives in the countries of the Great Eurasia from Lisbon to Peking and Tokyo. Over 70% of the global GDP is produced here [based on purchasing power balance], it accounts for around 76% of the global export of goods and services and 60% if direct foreign investments.

Eurasia is also a backbone of the global energy landscape. Eurasia accounts for 69% of the global demand of the primary energy and electricity and 63% of the global consumption of liquid hydrocarbons and natural gas. **The role of Eurasia in the global economy and energy will not shrink in the long term period. Despite the fact that some regions of our continent face shortage of energy resources the Great Eurasia is and for a long time will be balanced both in terms of oil and gas.**

The distinguishing feature of Eurasia is a possibility of creation of a uniform economic space of the energy industry with integrated regional infrastructure. The historical inertia, regulatory constraints, lack of developed infrastructure resulted in significant underutilization of the potential synergies of some regional markets. Unfortunately, we did not fully utilize the advantages of the historic Silk Way created by our ancestors.

Only now owing to the initiative of the President of the People's Republic of China Xi Jinping we can speak about project One Belt and One Road and other integration projects developed by this largest economy of the continent. Russia actively supports these projects.

Currently, there is ground for development of new vertically

integrated chains in Eurasia which includes first class and sustainable competitive resource base, large and rapidly growing consumption centers, developed financial and trading centers.

The important advantage of Eurasia is a harmony of interests of market participants, general understanding of sustainable and long-term cooperation, principles of mutually beneficial work, focus on improvement of energy security both in the separate regional markets and in the Eurasian market in general. Vertically integrated relations from wellhead to the customer allow for minimization of the agency and intermediary risks, distortions and volatilities, which unfortunately have their role in the aggravation of the crisis and decrease of the investment activity.

Rosneft actively participates in the process of pan-Eurasian energy integration, acting as its catalyst in many ways. We are proud of the largest European company BP, Qatar investment fund QIA, the largest private Chinese oil company CEFC and global company Glencore are our anchor shareholders, as well as our long-standing investors since the IPO procedure Petronas and CNPC. We are connected with all these shareholders in large joint projects. Our international shareholders structure and its participants' cooperation level allows Rosneft serve as a model of the ongoing integration processes.

We always try to find sources of synergy to benefit both the end customers and the producers. The main sources of synergies are not only the supply of energy resources but also the overcoming of the infrastructure constraints.

The implementation of joint infrastructure projects, harmonization of

institutional conditions, simplification of conditions for movement of people, capital, goods and services, technology transfer and development of reliable production and distribution chains focused on the end customer.

However, with a regret I should say that integration waves moving from the east of Eurasia frequently break at the competitive contradictions between the East and West. Europe following the USA ever more frequently is building walls instead of bridges and it tries to either block or destroy the existing bridges.

There is a great phrase from the Russian writer Leo Tolstoy: "Everything that unites peoples is kindness and beauty, everything that separate people is evil and ugliness". Actually we live in the period when certain division occurs in the world into those who are willing and ready to cooperate and those who think that any problems can and should be resolved through pressure, dictating and sanctions. It happens that there are two worlds - a world of declarations and sanctions and world of real deeds and cooperation.

EURASIAN COOPERATION PROJECTS AND EXPERIENCE OF JOINT WORK

Over the last years we have observed various projects of international integration in Eurasia. I would divide them into three main groups.

First are the projects of semi-closed type with deep economic integration which initially do not imply a large scale expansion. This is primarily the European Union which creates currently the common energy market and Eurasian Economic Union which forms the common markets of electric energy, gas, oil and oil products.

The second projects are open type projects which are essentially not so deep but which have wider coverage. These are the European Council, the Shanghai Cooperation Organization. These projects cover only certain parts of Eurasian but they evidently facilitate the development of the integration processes.

Finally, there is the third group of projects which do not attempt to unite but try break Eurasia into parts. I primarily mean the Trans-Pacific Partnership (TPP) and Trans-Atlantic Agreement. It should be noted however, that these projects fall apart before our eyes. The reasons are not only in the actions of the US Administration both old and new one, but evidently they lie in the fundamental flaws of the very idea to divide Eurasia, to catch its margins in the gravity field of the Western Hemisphere. And in this case suddenly it turned out that the gravity field of Eurasia is stronger than the any other external impacts.

However we lack the projects of the fourth group which are integration projects aimed to build bridges, infrastructure and economic corridors connecting the European coast of the Atlantic and the Arctic Ocean with the Asian coast of the Pacific and Indian Oceans.

Despite all market volatility and constraints including sanctional restrictions and continuing deterioration of the external environment Rosneft is really a locomotive of development of partnership pan-Eurasian and pan-Eurasian relations.

Rosneft is actively developing partnerships with leading oil and gas and investment companies of "Great Eurasia". **Over the past few years,**

we have significantly expanded the range of our joint projects, and today I can say that the value of projects in the energy collaboration sphere of Rosneft and its partners in Europe, Asia and the Middle East exceeds 110 billion dollars. These projects include the deals at the shareholder level, creation of partnerships for onshore and offshore exploration and production in Russia, international refining and petrochemical projects, Mediterranean gas resources development and other strategic projects. **Having added our trade flows, swap operations and prepayments to the scope of our cooperation with “Great Eurasia”, I can say that its value exceeds 500 billion dollars. And yet we are just at the very beginning of this path.**

ROSNEFT'S ROLE IN EURASIAN ENERGY SECURITY

We are closely watching and participating in a responsible way in the projects ensuring the promotion of the integrated Eurasian energy agenda. This meets our joint interests. I will tell you more that this agenda has been the basis of the Rosneft strategy over the recent years and there are many practical proofs of that. In Europe for example.

Traditionally, Russia is the leading supplier of hydrocarbons to Europe. Rosneft provides more than 40% of total Russian crude and oil products supply volume. **All attempts to alienate Russia from energy cooperation, whether in the logic of sanctions measures, or in the logic of achieving energy independence, will never work out.**

The export of crude from Russia to Europe continues to grow. In 2016 the deliveries increased by 7.8% to 168 mln.t, Russian gas export to Europe grew by 12% and exceeded 178 bcm.

However, our strategy is aimed not only at increasing of supplies, but also in implementing joint investment projects with European partners.

Our strategic position in Germany deserves a special attention. We are the third largest player in the German oil refining market with a production capacity of 12.5 million tons per year, which is more than 12% of all German refining capacities. One of the factors of the Company's success in the German market is the world's largest Druzhba pipeline system, consistently supplying Russian oil to Europe for more than 50 years, regardless of any political conflicts and political climate in general.

Our largest private shareholder BP directly entered in a number of Rosneft projects (Taas-Yuryakh, Ermak) and considers possibility of entering in a number of new projects. We also jointly participate in Zohr project and in the German refining business.

For example, we signed several comprehensive agreements with Eni which are related to the expansion of the cooperation almost in our areas of activities such as exploration, production, crude and oil product trading, refining, technologies. They move Eni closer to the large-scale production of oil in Russia. In late December - early January we will start the first E&A drilling with Eni, Saipem in the Black Sea.

Norwegian Statoil works with Rosneft studying hydrocarbon reserves of Domanic deposits in Samara Region, we jointly develop Severo-Komsomolskoe field, two offshore projects in the Western Arctic area and in the Sea of Okhotsk as well in the offshore license area in Norway.

With respect to the development of the “Russia – Asia” energy

bridge we develop multifaceted cooperation with Chinese companies. In 2016 Russia became the largest supplier of crude oil to China accounting for almost 14% of the Chinese import. In last year the share of China in the structure of the Russian oil export achieved 20.6% which made it our key trading partner in this sphere.

Cooperation with the Chinese company CEFC is actively developing. Alongside with the completed share capital acquiring, the parties are expected to cooperate in the field of exploration and production, refining and petrochemicals, crude and oil products trading.

Cooperation in the gas business also appears to be very promising. Beijing Gas acquired 20% in Verkhnechonskneftegaz.

Another strategic priority for Rosneft is cooperation with Indian companies. Suffice it to say that the value of assets within cooperation of Rosneft and Indian partners in Russia and India has already exceeded 35 billion USD. The Indian companies participate in the development of Vankor and Srednebotuobinskoe fields in Eastern Siberia and work with us in Sakhalin 1 project.

Recently Rosneft closed the deal for purchase of 49% in Essar Oil which is one of the most technologically advanced refineries (with an access to deep water port Vadinar and large retail chain) entering one of the most dynamically developing global markets which allows for improvement of efficiency of our trading division in the Asian Pacific Region. This deal became one of the largest foreign investments in the Indian economy.

Earlier this month, we discussed with Indian Prime Minister

Narendra Modi the prospects for further cooperation between Rosneft and Indian partners, as well as the creation of favorable conditions for expanding the Company's business in India.

Also, Rosneft is actively developing Vietnam offshore projects and plans to work in Indonesia.

Our export to Japan is focused on many production projects in our Far East starting with our joint project Sakhalin-1. Crude, naphtha and LNG export from Russia to Japan rapidly increases despite projected reduction of the energy demand in Japan and high saturation of the market. The Japanese companies participated in the joint production projects with Russian companies.

Over the last three years the Russian export to South Korea significantly increased - volume of delivered crude increased by 30% and volume of delivered oil products grew 2.6 times, I would like to especially highlight our cooperation in the construction of complex high-technology facilities for exploration and offshore production in the Far Eastern seas. I refer not only to the construction of the Zvezda shipbuilding complex, but also to agreements, that are planned to announce in the margins of this respected Forum, about the placement of anchor orders for the construction of ice-class ships for the development of prospective areas of the Russian North by Russian oil companies. We are developing this project together with South Korean partners.

Projects in the Middle East is another strategic direction for Rosneft's development. **We are discussing projects in Iran, where we want not only to participate in exploration and production projects, but to establish effective supply chains of Iranian and Central Asian oil to**

the world market. We are developing cooperation with Saudi Arabia. Finally, we are very serious about working in Kurdistan and Iraq in general. Our interest in these projects is purely practical - this region is characterized by the largest resource base with low production cost and potential that is not fully opened yet. It is very important that the oil from Kurdistan goes directly to our refineries in Germany. At the same time if we include this region in the sphere of Eurasian business integration, we will contribute to solving general economic and social tasks - energy stability and advance in living standard.

At present Rosneft is the only company that implements such large-scale integration projects. **I will not hesitate to say that we have an evident model role in the development efficient Eurasian energy dialog and its practical implementation.**

The scale and importance of these projects make it possible to hope for a significant transformation of the entire intra-Eurasian energy space, strengthening, cementing of its foundation, for looking over the horizon of the coming years and thinking about the practical implementation of even more global projects such as an integrated pipeline backbone of Eurasia, integrated continental gas market, integration of the capital markets.

Finally I would like to make the following conclusions:

1. Great Eurasia is a huge economic and energy space that has all prerequisites for economic rapprochement and integration.
- 2. The Eurasia gravity field is stronger than any external influences. The movement toward an integrated Eurasia is organic and natural.**

3. Mutual investments, asset and technology exchange in the Great Eurasia energy sector have a large scale despite such factors as sanction pressure.

4. Desynchronization of the investment cycle in the oil and gas industry with the global economic trends provides grounds for future oil deficit and increase of the pricing volatility.
5. The strategy of a responsible hydrocarbon producer should take into account both risks and uncertainties of the current condition of the global oil market and long-term outlooks of the global economic development.

I believe that our vision of the situation to a great extent coincides with the vision of the long-term agenda of many key players in the Eurasian space. I would like to cite a quotation. President Xi Jinping yesterday in his address at the opening of the 19th National Congress of the Communist Party of China said: "Currently the world is in the process of deep and complex changes. The outlooks of the development are still attractive but at the same time we face very serious challenges".

Despite all challenges of the international situation the potential of cooperation and constructive interaction in the Eurasian space will be implemented in ever greater extent. The jubilee 10th Forum in Verona can make a significant contribution to this process.

I wish good work to everybody. Thank you for your attention.