Oil & Gas

NewsFlash

February 2016

International market headlines

- The World Bank (WB) expects the growth of Kazakhstan's economy to slow down to 1% in 2016, the WB says in its report "Kazakhstan: Adjusting to Low Oil Prices, Challenging Times Ahead." "GDP growth will be low at about 1 percent in 2015 and 2016, but may increase to 3.3 percent in 2017," the WB said in the report.

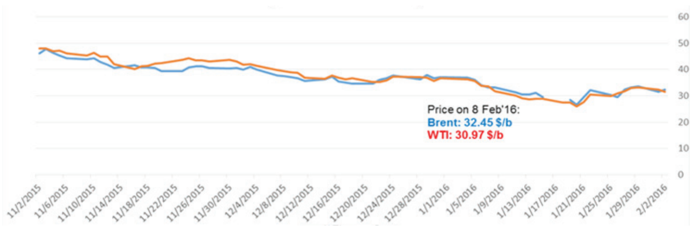
- OPEC, at the end of its regular session on 4 December 2016 in Vienna, has set the oil production quotas at 31.5 mb/d. At that, the new quotas has not accounted for the oil production by Indonesia, who joined OPEC recently (Indonesia produces about 800 thousand b/d). From December 2011, the OPEC oil-output quota made up 30 mb/d, however, the actual production output of the cartel over the past one and a half years surpassed this figure.

- Global oil industry reduced its capital-expenditure budgets in 2015 by $200 bln and may cut the investments by the same amount in 2016, all that causes more serious concerns than the current oil prices decline, says Claudio Descalzi, the Chief Executive of Italian oil company Eni SpA. "My main concern is what happens in the industry rather than the oil prices", he stated in the interview to Bloomberg agency. "We reduced capital investments by $200 bln and during the next year, I believe, the cuts will be at the same level. In the midterm, the cuts will cause the imbalance between demand and supply in the oil market".

- OPEC expects the oil production in the Russian Federation to reduce in 2016 from 10.77 mb/d expected in 2015, Bloomberg agency reports with reference to the global market forecast for December. In Q1, 2016, oil production in the Russian Federation is expected at 10.75 mb/d, in Q2 – at 10.67 mb/d, in Q3 – at 10.66 mb/d, and in Q4 – at 10.73 mb/d.

- On 31 December, the first tanker with oil of ConocoPhillips sailed from Corpus Christi, Texas, and arrived to Italian Trieste, from where oil was pipelined to the refinery owned by Vitol and Carlyle Group in Bavaria. Early in January the second tanker left the Houston terminal of Enterprise Product Partners for Marseilles, then oil was pipelined to Switzerland. The experts think than in the long term the Latin America and Europe may become the major markets for American oil.

Brent and WTI spot prices (2 Nov'2015 - 2 Feb' 2016)



WTI Brent Source: EIA

Brent Crude Oil Forecasts

Year	Consensus Bloomberg	Number of Forecasts	EIU
2013	-	-	108.6
2014	-	-	98.9
2015	-	-	52.4
2016	53.9	22	42.9
2017	61.25	15	60.0
2018	68.75	8	73.5
2019	68.5	7	72.8
2020	-	-	71.4

Source: Consensus Bloomberg, 3 months, EIU, http://gfs.eiu.com/Article aspx?articleType=cf&articleId=1243614708&secId=6

International market headlines (continued)

- The US oil service company Baker Hughes expects that the number of operating oil and gas drill units to reduce in the world by 30% in 2016 following the decommissioning of nearly a half of the number of drill units for the last two years. According to Baker Hughes, the number of operating drill units has reduced by 47%, from 3736 in February 2014 to 1969 units by now.

- Rapidly falling crude price – up to $30 per barrel - spurred concerns about possible bankruptcy of USD oil producing companies. According to Wolfe Research, if such price level were preserved for a long time, about third of US oil corporations would face the threat of financial collapse – bankruptcy and restructuring – by mid-2017.

- China imported a record amount of crude in 2015 against the oil's lowest annual average price in more than a decade. Crude imports last year increased by 8.8 percent to a record 334 mln metric tonnes, or about 6.7 mln barrels a day, according to preliminary data released by the General Administration of Customs of PRC.

- International Energy Agency (IEA) expects world demand growth of 1.2 mb/d - up to 95.6 mb/d in 2016, IEA says in its Oil Market Report. Oil production of OPEC in December decreased by 90 thousand b/d and was 32.28 mb/d, including Indonesia.

- China National Petroleum Corporation boosted overseas oil and gas production to record high. The total production was 72.02 mln metric tonnes which is by 10.5% higher than in the previous year, CNPC said in its statement. According to the results of the first six months of 2015, the overseas production increased by 18.6% as compared to same period of 2014.

- Royal Dutch Shell shareholders approved its $50 bln takeover of BG Group on 27 January 2016, clearing the last main hurdle to creating the biggest liquefied natural gas trader in the world. BG Group Plc shareholders also approved one of the biggest deals in the energy sector in the past decade on 28 January 2016 that will allow the two oil and gas companies to merge on 15 February. The companies expect to save about $3.5 bln in overlapping costs following their merger.

Kazakhstan market headlines

- The third section, Line C of the Kazakhstan-China gas pipeline that connects Turkmenistan, Uzbekistan, Kazakhstan and China, has been commissioned in Zhambyl district of Almaty region. The total length of Line C of the Kazakhstan-China gas pipeline is 1,303 km. The pipeline has successfully passed all preproduction test runs. Line C and Lines A, B of the gas pipeline Kazakhstan-China run across South Kazakhstan, Zhambyl and Almaty regions and provide gas for local consumers in these regions along the way. The Kazakhstan-China main pipeline is part of the 7,500-km cross-border gas pipeline, Turkmenistan-Uzbekistan-Kazakhstan-China.

- The validity of Euro-2 and Euro-3 standards for gasoline, diesel fuel, fuel for agricultural and off-highway equipment, has been extended until 1 January 2018. The Council of the Eurasian Economic Commission (EEC) made the decision on 2 December in Moscow.

- Shymkent Oil Refinery has launched a new production facility - sulfur production unit with a capacity of 4,000 tonnes per year. The first experimental batch of a new product - liquid sulfur has been received in the course of the facility commissioning. The project is implemented as part of the Program for Reconstruction and Modernisation of the Shymkent Oil Refinery.

- CEFC China Energy Company Ltd reached an agreement to acquire 51% stake in the Romanian division of Kazakhstan National Company "KazMunaiGas", KazMunayGas International N.V. The agreement was a part of the oil and gas, telecommunications and nuclear energy packages worth a total of $4 bln. signed in Beijing between Kazakhstan and China.

- During 2015, the National Company "Aktau International Commercial Seaport" transshipped 5.9 mln tonnes of cargo, which is 43% less than in 2014. In this regard, the transshipment of oil and oil products dropped by 40.6% up to 3.5 mln tonnes and that of metal products – by 16.7% up to 1 mln tonnes. In the past year the grain handling reduced by 27% up to 501 thousand tonnes, ferry transportation – by 4.2 times up to 466 thousand tonnes and shipment of other commodities – by 22% up to 338 thousand tonnes.

- Ministry of Energy forecasts that oil production in 2016 will amount to 77 mln tonnes with subsequent increase up to 92 mln tonnes in 2020, which is less than the previously forecasted volumes by 3.8 mln tonnes and 12 mln tonnes, respectively.

- In 2015, Kazakhstan has produced 2,876 mln tonnes of gasoline, including aviation gasoline, which is by 4.9% less than in 2014. Output of diesel fuel dropped by 9.6% up to 4,557 mln tonnes and that of residual fuel oil - by 4.5% up to 3,829 mln tonnes.

- During 2015, Kazakhstan produced 66,518 mln tonnes of crude oil and 12,935 mln tonnes of gas condensate, which is by 2% less and by 0.1% more, respectively, than in 2014. During the reporting period Kazakhstan produced 21,635 bln c. m. of natural gas (in gaseous state), i.e. by 1.7% more than in 2014. Production of petroleum gas during the reporting period amounted to 23,827 bln c. m. (i.e. increased by 8.8%).

- KazTransOil JSC pumped 61 mln tonnes of oil and petroleum products through its pipelines in 2015 or a decrease of 4.7% from a year earlier. Consolidated oil transportation last year totaled 45.446 bln tonnes/km or an increase of 2.8% year over year. In 2015, the volume of oil transported by KazTransOil alone amounted to 36.866 bln tonnes - km or up 2.9% year over year.

The 2015 UN Climate Change Conference, Paris 2015

Expectations were high for COP21.

The politics have changed – US and China have been more actively involved:

- Both announced cuts to their carbon emissions in a 2014 joint announcement;
- China to implement national carbon trading system in 2017.

Countries can set their own national targets to cut carbon rather than having them imposed.

Pressure from business and society calling for a strong agreement at COP21 (including 70% of KPMG's Global Platinum clients).

Costs of renewable energy technology falling rapidly.

COP21: an historic outcome

- "The Paris Agreement" comes into force in 2020.
- A clear and unequivocal signal to the private sector.
- Global political intention to shift to a low carbon, and ultimately zero carbon, future.

Pursue "best efforts" to limit increase of temperature to only 1.5˚C.

Countries agreed to peak greenhouse gas emissions as soon as possible.

Global carbon neutrality (zero net emissions) to be achieved between 2050 and 2100.

All countries will set national targets to reduce carbon emissions

- 188 have already done so.
- Targets are known as Intended Nationally Determined Contributions or INDCs.
- The INDCs must be strengthened over time because the current targets are insufficient to limit warming to well below 2°C.
- 5 year cycle of global stock takes and strengthening of national targets.

Countries will report transparently on carbon reduction. The agreement requires countries to report their progress transparently.

Richer countries will provide financial assistance for poorer countries. Developed nations will provide US$100 billion per annum by the year 2020.

Vulnerable countries receive finance for loss and damage from climate change.

Tax Amendments for 2016

Below we outline changes in the Kazakhstan tax legislation related to taxation of subsoil users operating in oil and gas sector. The majority of the amendments entered into force on 1 January 2016. Some amendments entered into effect retroactively. We indicated the effective date next to each retroactive change:

- The cost of a quota for emission of greenhouse gases that a taxpayer receives free of charge under the National Plan for the Allocation of Quotas for the Emission of Greenhouse Gases will be regarded as nil.

- The amendments clarify that 50 percent of the subscription bonus that a taxpayer pays after it wins a subsoil use tender or signs a protocol on direct negotiations with the state on the acquisition of the subsoil use rights constitutes the subsoil user's expenses on geological exploration and preliminary works and is subject to capitalisation.

- A taxpayer's expenses on the construction and liquidation of nonproducing wells are deductible together with the input VAT accrued in connection with these expenses. This norm entered into force retroactively from 1 January 2009.

- The amendments introduce a procedure for a refund of excess input VAT accumulated during the exploration and development of a deposit before the commencement of the minerals export transactions. A taxpayer may claim for the VAT refund after it commences export of the minerals within the statute of limitation period. The statute of limitation period begins upon the expiry of the tax period in which the export transactions commence. If the export transactions commenced before 1 January 2016, the statute of limitation period begins on 1 January 2016.

- For the purpose of ring-fencing of subsoil use contracts, a subsoil user should not include interest expenses to the cost of production and primary processing. This norm entered into force retroactively from 1 January 2009.

- The amendments introduce a formula for the estimation of the production costs of natural gas extracted with crude oil to apply for the separate tax accounting purposes.

- The amendments exempt from income tax in Kazakhstan dividends paid by a Kazakh subsoil user (except for dividends paid to entities residing in tax havens) if the following conditions are met simultaneously:
  - the owner of the dividends has held its stake in the Kazakh legal entity for a period exceeding three years as of the date of the declaration of dividends;
  - the subsoil user performs a subsequent processing (after the primary processing) of at least 35 percent of the mineral raw materials extracted during 12 months preceding the date of the declaration of dividends on the own production facilities.

  The abovementioned provisions on the tax exemption of dividends are effective from 1 January 2016 to 31 December 2017.

- Starting from 1 January 2017, the base rates of the charges for emissions resulted from flaring of associated and/or natural gas will be increased by 20 times. The amendments cancel the tenfold increase coefficient applicable to base rates in case of excess emissions and twentyfold increase coefficient applied by the local representative authorities (Maslikhats).

- A governmental resolution of 30 December 2015 extended the list of oil deposits regarded as low-margin, high-viscosity, flooded, marginal or worked-out. The resolution added to the list the following nine deposits with the mineral extraction tax rates from 0.25 to 2.5 percent:

Deposit	Subsoil user	Type of deposit	Tax rate
Eszhan	South Oil LLC	Marginal	2.5
Kalzhan	South Oil LLC	Marginal	1.5
North Akshabulak	South Oil LLC	Marginal	1.5
East Akshabulak	South Oil LLC	Flooded	1.0
Kenkiayak	CNPC-Aktobemunaigas JSC	High-viscosity	2.1
Kumkol	Petrokazakhstan Kumkol Resources JSC	Flooded	0.35
Sazankurak	Sazankurak LLC	High-viscosity	0.25
Kumkol and East Kumkol,	Turgai Petroleum JSC	Flooded	1.0
Arman	Joint Venture Arman LLC	Flooded	0.25

Decrease of the customs duty on export of crude oil

- On 22 January mass media officially published an order of the Minister of the National Economy of Kazakhstan reducing the customs duties on export of crude oil (code 2709 00 900 9 in the Classifier of International Trade Activities) from USD 60 to USD 40 per ton. The order states that this rate will be effective until 31 December 2016 inclusively. The order came into effect after the publication day and applies to transactions executed from 1 January 2016.

Balance of production, processing and distribution of gas of the Republic of Kazakhstan

for 2013-2014 and January-October 2015, billion cubic meters

	2013	2014	2015 January-October
Total production of crude gas in the Republic of Kazakhstan	42,3	43,2	37,1
Use of crude gas for own needs	19,5	19,7	17,3
for industrial and own needs	7,6	7,5	7,2
gas reinjection	11,9	12,2	10,1
Commercial gas for distribution	22,8	23,5	19,8
domestic gas consumption	10,9	12,5	9,0
export of gas, with SWAR-transactions	11,9	11,1	10,8

Source: Ministry of Energy of the Republic of Kazakhstan

Balance of LPG of the Republic of Kazakhstan

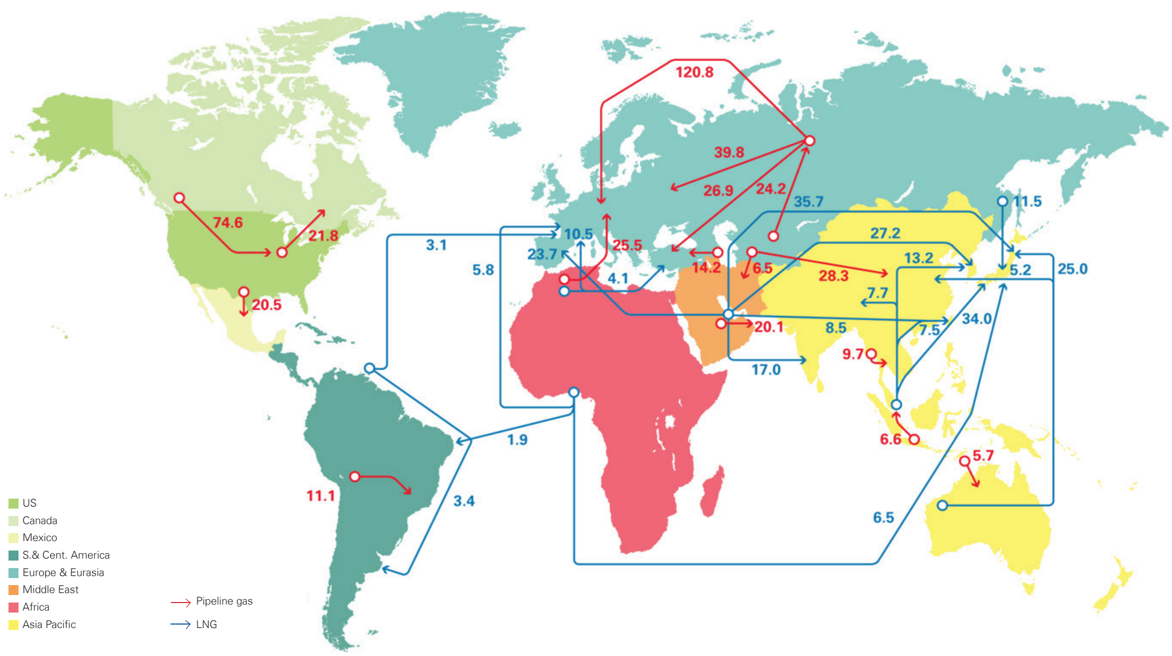
for 2013-2015, thousand tons

	2013	2014	2015 January-October
Production	2448,2	2464,1	2058,5
Export	1793,0	1840,6	1593,8
Domestic market	655,2	623,6	464,7

Source: Ministry of Energy of the Republic of Kazakhstan

Major gas trade movements 2014

Trade flows worldwide (billion cubic metres)



Source: BP Statistical Review of World Energy, June 2015, bp.com/statisticalreview

Production of gas in Kazakhstan for the three quarters of 2015

	Company	mln cubic metres
1	Karachaganak Petroleum Operating B.V.	13 439
2	Tengizchevroil	11 136
3	CNPC-Aktobemunaigas	3 743
4	Zhaikmunai	1 038
5	Kazmunaigas	826
6	Mangistaumunaigas	540
7	Kazakhoil Aktobe	482
8	Kazgermunai	356
9	Petrokazakhstan Kumkol Resources	324
10	Kazazot	201
	Total Kazakhstan	**59 475**

Total proved reserves of gas

	Country	2014, trln cubic metres
1	Iran	34.0
2	Russian Federation	32.6
3	Qatar	24.5
4	Turkmenistan	17.5
5	US	9.8
6	Saudi Arabia	8.2
7	United Arab Emirates	6.1
8	Venezuela	5.6
9	Nigeria	5.1
10	Algeria	4.5
	Kazakhstan	**1.5**
	Total World	**187.1**

Production, gas

	Country	2014, bln cubic metres
1	US	728.3
2	Russian Federation	578.7
3	Qatar	177.2
4	Iran	172.6
5	Canada	162.0
6	China	134.5
7	Norway	108.8
8	Saudi Arabia	108.2
9	Algeria	83.3
10	Indonesia	73.4
	Kazakhstan	**19.3**
	Total World	**3 460.6**

Consumption, gas*

	Country	2014, bln cubic metres
1	US	759.4
2	Russian Federation	409.2
3	China and Hong Kong SAR	185.5
4	Iran	170.2
5	Japan	112.5
6	Saudi Arabia	108.2
7	Canada	104.2
8	Mexico	85.8
9	Germany	70.9
10	United Arab Emirates	69.3
	Kazakhstan	**5.6**
	Total World	**3 393**

* Excludes natural gas converted to liquid fuels but includes derivatives of coal as well as natural gas consumed in Gas-to-Liquids transformation

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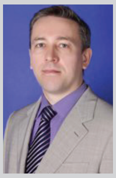

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