

COMMERCIAL UPDATE - SAKHALIN REGION, November-December 2003

Russian Far East

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This report contains the following items:

- **Oil and gas**
 - Sakhalin Regional Administration is demanding that Sakhalin-1 and 2 operators increase the Russian Content level.
 - This year Sakhalin oil industry companies extracted about 3 million metric tons of oil.
 - Petrosakh is a stable supplier of oil products for the Sakhalin market.
 - New Western Marine Port processed more than 5 thousand pipes delivered for Sakhalin shelf projects.
 - Ten Sakhalin districts became construction sites.
 - Tankers of PRISCO continue transportation in Far Eastern routes.
 - Two tankers named Yuri Senkevich and Viktor Konetski will provide services for Sakhalin-1 (Sovkomflot).
 - American ecologists demand that ExIm carries out more detailed ecological expertise of Sakhalin Energy.

- **Election Results from December 7, 2003**

- **Yuzhno-Sakhalinsk 2003 first nine months economic development statistics**

- **Local industry and companies.**
 - New life of Kholmsk cellulose plant.
 - Sakhalin gold mining breaks local records.
 - New agency to serve the needs of local traveling personnel – Russian Business Travel.

Oil and gas

** Sakhalin Regional Administration is demanding that Sakhalin-1 and 2 operators increase the Russian Content level.*

The Administration wants the level of Russian Content to reach 70%. Russian Content, according to them, should be measured not by the volume of services provided but by the contract amounts. Oil and Gas Complex Department Director Ms. Galina Pavlova reported at the press-conference that at this moment the amount of contracts signed by the Russian side reaches USD 5 billion, which is about 50% of the total contracts signed for the projects. The Department will be negotiating with Sakhalin-1 and Sakhalin-2 about the spheres of business where the Russian content can be potentially increased. SEIC already presented materials showing intension to increase the content to 70%. Galina Pavlova also stated that unfortunately, Russian companies are not ready to compete on certain projects due to lack of technical expertise and equipment, as well as weak financial capabilities. *(Source – Ostrova Information Agency, December 05)*

** This year Sakhalin oil industry extracted about 3 million metric tons of oil.*

During 11 months of 2003 102% of the annual extraction plan was fulfilled. The major amount was extracted by JSC Rosneft-Sakhalinmorneftegas (1.5 million metric tons of oil) and Sakhalin Energy (1.3 million metric tons of oil).

According to the same source, during 11 months of 2003 1.65 billion cubic meters of gas were extracted on Sakhalin.



LNG plant construction site. November 2003

As a result, the regional budget incomes from companies working on Sakhalin shelf projects increased significantly. According to Galina Pavlova, this increase happened not due to the carbohydrates output (which remained on the same level) but due to increasing investment volumes. Thus, says Ms. Pavlova, the existing official opinions that Sakhalin projects are not profitable for Russia is not legally valid. The projects presuppose initial investment into infrastructure.

In 2004 it is planned to start construction of pipelines and continue on construction of the LNG plant; new wells will be drilled. Together with the oil and gas pipeline it is planned to lay a trans-Sakhalin fiberoptic backbone and construct three industrial waste disposal sites. Sakhalin's share of gas is planned to be used at the Power Plant #1. Negotiations are carried out now on gas prices and the necessary Plant upgrades. Khabarovsk Krai is ready to purchase 3.5 billion cubic meters of gas – over 2 times more than before. (*Source – Sovetsky Sakhalin newspaper, December 06, 2003*)

** Petrosakh is a stable supplier of oil products for the Sakhalin market.*

During 9 months of 2003 Petrosakh manufactured and supplied for the local market about 20 thousand tons of oil products (the same amount as in 2002). Mr. Motovilov, Director, told the press that the company manufactured its maximum in 1995 - 75 thousand metric tons. For the Sakhalin market Petrosakh manufactures gasoline, kerosene, diesel fuel and mazut. Petrosakh's specific share in local market is 25%. The company operates for more than 12 years, the priority in development for Petrosakh is the Sakhalin-6 project which would help increase the output. Plant production capacity of the refinery is 200 thousand metric tons of oil products per year, which allows additional oil processing. In summer 2004 it is planned to drill an exploration well. Mr. Motovilov also spoke about the existing problem of personnel lapse factor because jobs in foreign projects are more attractive now.

Petrosakh can invest significant amounts into Sakhalin-6 if the perspective structures are found during the exploration phase, which already started. In 2003 tax income into the regional budget from Petrosakh was not so significant – as Galina Pavlova, Director of Oil and Gas Complex of

Sakhalin region explained, this happened due to the fact that Petrosakh is “in pre-sale readiness status”. (Source – Ostrova Information Agency, November 13, 2003)

** New Western Marine Port processed more than 5 thousand pipes delivered for Sakhalin shelf projects.*

The St. Spirit vessel was unloaded in the port – 900 pipes of different diameter were delivered for the Sakhalin-1 project. The line Port Vostochny – Sakhalin Western Marine is serviced by three river-marine vessels. The workload of Western Port is increasing significantly - in September, two vessels were serviced, in October – three and in November – seven. (Source – Ostrova Information Agency, November 24, 2003)



Picture courtesy of Lynden International

** Ten Sakhalin districts became construction sites.*



Construction in Nogliki. Picture by Exxon Neftegas.

The infrastructure for the oil and gas industry objects is under construction in 10 districts of the Sakhalin region. The local administration is trying to develop supply plans for the new infrastructure projects in order to utilize local agricultural companies potential to the maximum. The Regional Administration Committee for Industry and Trade is studying the existing schemes of cooperation between EPC's, other prime contractors and sub-contractors on services and goods supply. The Committee asked prime contractors to provide data on potential needs for their personnel (2004-2006) in order to study the possibility of existing manufacturing upgrade. So far, the data was submitted only by Eurest-IoCa (a catering company). The committee is also processing data gathered during the business trip of Georgi Karlov, Committee Chairman, to the northern construction sites. (Source – Gubernskije Vedomosti Newspaper, November 11, 2003).

** Tankers of PRISCO continue transportation in Far Eastern routes.*

For the third season the largest vessel of the Primorsk Shipping Company continues to ship Sakhalin crude oil from the Sakhalin-2 Vityaz terminal. The oil is shipped for the last time this

season from an Okha storage tanker at Aniva Bay. After the oil is shipped to the Japanese port Chiba, the tanker will go to Singapore to continue work.

Tanker Asia (40 thousand metric tons deadweight) headed for De-Kastri from South Korean port Iosu. The crew has to make four trips to deliver oil from the north-Khabarovsk port and then this baton will be passed to the ice-class vessels. (Source - <http://www.vostokmedia.vl.ru/>, November 17, 2003)

** Two tankers named Yuri Senkevich and Viktor Konetski will provide services for Sakhalin-1 (Sovkomflot).*

Two tankers of 100,000 metric tons deadweight each belonging to Sovkomflot will be constructed at South Korean shipyards (construction starts at the beginning of 2005). Term of construction - about 1 year. As Sovkomflot explained to the press, Russian shipyards do not construct tankers of such deadweight. (Source – RIA Novosti, November 25, 2003)

** American ecologists demand that ExIm carry out more detailed ecological expertise of Sakhalin Energy activity.*

The ecologists demand more detailed expertise before loans are granted to SEIC. The talks again are concerning the gray whale population and 500 thousand metric tons of waste water which can pollute the environment. It is reported that such companies as NRDC, Environmental Defense, Friends of the Earth, IFAW, Greenpeace, WWF and others signed the petition. (more details at <http://releases.usnewswire.com/GetRelease.asp?id=104-11252003>) (Source – www.sakh.com)

Election Results from December 7, 2003

The pre-election campaign had even more illegal methods used than the previous one. This fact influenced the opinion of many people who voted “against all candidates”. The new government has not been formed yet and many citizens already have no trust in it. Despite this negative tendency, more people came to the election districts than last time (40% on previous elections, 51.67% this time). 382,106 people participated.

For the Governor’s post, 35.14% of votes went to Ivan Malakhov, and Fyodor Sidorenko took 19.61%. For the second tour of elections the percentage of voters is not counted; the winner will be the candidate who takes maximum of votes of those who come to election centers.

The second round of elections will be held on December, 21st

pictured at right –

Ivan Malakhov, the front runner,
and
Fyodor Sidorenko, the current mayor
of Yuzhno-Sakhalinsk.



In terms of the State Duma parties and candidates, Sakhaliners voted the following way –

Ivan Zhdakayev – almost 28% (making him again the Sakhalin Deputy for the Russian State Duma) Vladimir Yefremov – 21.47%, Sergey Podolyan – 19%, 13.59% voted against all candidates.

- 30.22% voted for Edinaya Rossiya (United Russia)
- 18.97% for LDPR (Liberal Democratic Party of Russia)
- 12% for KPRF (Kommunist Party of Russia)
- 5.68% voted against all of the candidates

Yuzhno-Sakhalinsk 2003 first nine months economic development statistics

Population. The population of the city makes up 1/3 of the total regional population. As of October 1, 2003, it was estimated at 183, 200 people. The natural decrease of population is caused by prevalence mortality rate over the birth rate (in 2003 mortality was 20% higher).



Industry. As of September 1, 2003 Yuzhno-Sakhalinsk has registered more than 6 thousand companies and enterprises and more than 13 thousand private entrepreneurs. More than 78 thousand people are engaged in the local economy, 70% are large and medium-sized companies. The level of officially registered unemployment is 0.3% of the total population that is considered to be capable to work (the whole-region level is considered to be 1.3%). Official data on average salary in Yuzhno-Sakhalinsk is \$340 (35% increase to 2002)- compared to average regional \$227.

Industrial structure of Yuzhno-Sakhalinsk in 2002

28% - electric power industry;

60% - food-processing;

12% - printing, forestry, coal, light industry, construction materials manufacturing.

In 9 months of 2003, the increase of output in the food industry made up 122.7%. Fish-processing takes up 66% of this segment.

Construction. From January-September, 2003, Yuzhno-Sakhalinsk construction companies built 14.3 (153,924 square feet) thousand square meters of dwelling facilities (50% of the total for the region), twice as much than completed in 2002. Budget (State) funds are available only for construction of low-rise housing for people who lost their homes during natural calamities in Northern Sakhalin (total

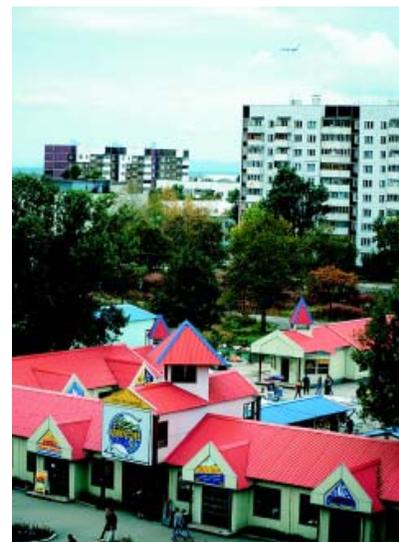


Photo by V.Titov

13,122 meters or 141,240 feet). The common tendency is for construction is of low-rise housing.

Transportation and communications. Aviation transport served 1,623 thousand passengers. The amount of mail and cargo shipped increased by 62%. Communications companies continue with equipment upgrade. As on October 1st, 2003 available total line capacity for all operators in Yuzhno-Sakhalinsk made up 67.7 thousand (13.2% increase).

Consumer market. Yuzhno-Sakhalinsk concentrates 97.4% of the total regional wholesale turnover, 59% of retail and 64.7% of catering market of Sakhalin region. 70% of consumer services are performed in Yuzhno-Sakhalinsk. In monetary terms, the average Yuzhno-Sakhaliner paid \$730 for consumer services during the first 9 months of 2003.

Small Business. The number of small businesses registered as of October 1st 2003 exceeds 2.5 thousand (about 40% of all companies). Their share in trade & services turnover is about 18% .

Foreign Economic Activities. 91% of economic ties are with Asia-Pacific countries. 75% of joint ventures are registered in Yuzhno-Sakhalinsk.

(Provided by the Economic Policy Office at the Committee For Economic, Yuzhno-Sakhalinsk Administration)

Local industry and companies

** New life of Kholmsk cellulose plan.*

The destroyed shops of the old Japanese cellulose plant are in use again. The former saw-mill is being reconstructed to start lumber manufacturing. The new mill of Troika-Sakhalin Company is planning to manufacture 900 cubic meters of lumber per work day (about 31783 cubic feet). The equipment was purchased in Japan; for the initial period the workshop will be operating in one shift (15 employees). In May 2004 the company is planning to install a dry-kiln and start manufacturing glued lumber which is in higher demand on the market than timber. *(Source – Sakhalin State Broadcasting Company, November 06, 2003).*

** Sakhalin gold mining breaks local records.*

On Sakhalin Island, gold is mined in the Smirnykh district by the Vostok-2 cooperative. The average annual output is not more than 230 kilograms (507 pounds). This year Vostok-2 mined more than 250 kilograms this season. But as the company reports, the reserves of the only field on Sakhalin are depleted. During the Second World War more than 5 metric tons of gold was mined here (11,000 pounds), but today the figure is 5 times less. Gold is currently mined in already developed fields. Vostok-2 does not possess the technology to develop the depleted field and the reserves are sufficient for 2-3 years only. The forecast exists that the Poronaisk region deposits have 70 kilograms more of gold. Another 500 kilograms can be mined near the

Pervomaiski Village of the Smirnykh district. (Source – Sakhalin Broadcasting Company, November 20, 2003)

* *New agency to serve the needs of local traveling personnel.*

Russian Business Travel / DAVS opened a fully-operational branch office in Yuzhno-Sakhalinsk. The company provides a full range of travel services both in Yuzhno and in Moscow, including:

air tickets (domestic and international)

train tickets

visa support

medical insurance

hotel reservations

car rental/VIP/limousine service/conferences/incentive/ leisure travel arrangements

The office accepts all major credit cards. Yuzhno-Sakhalinsk office can be contacted at +7 (4242) 744104; Fax +7 (4242) 74 4102; E-mail addresses: elina@davs.ru; marina@davs.ru

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