

Azerbaijan Oil and Gas Report Q4 2012

<https://marketpublishers.com/r/A018CBFCBBAEN.html>

Date: September 2012

Pages: 91

Price: US\$ 1,295.00 (Single User License)

ID: A018CBFCBBAEN

Abstracts

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BMI View: Progress on securing midstream infrastructure to carry Azeri volumes bodes well for our shortterm outlook, but the prospect of delays or disappointing volumes remains a key downside risk. Meanwhile, declining oil volumes may experience a temporary boost as new developments come online over the latter part of our 10-year forecast period to 2021, but peak Azeri oil production is approaching quickly. Nevertheless, the country's prospects are boosted by more optimistic developments in the gas sector, where both new discoveries and scheduled developments will help raise export volumes to Europe. The key developments in Azerbaijan's oil & gas sector are:

On the back of support from BP and the Energy Ministry of Azerbaijan, Nabucco West seems the most likely choice for the US\$20bn Shad Deniz II project. The Shad Deniz Consortium (SDC) must now decide between the Trans-Adriatic Pipeline (TAP) and Nabucco West as export routes for the next phase of the Shah Deniz Field. The decision, delayed from 2012, is now set for mid-2013.

The Shad Deniz II project is expected to allow exports of 10bcm of gas to Europe and 6bcm to Turkey by 2018. The Shah Deniz Consortium (SDC) was expected to reach a decision on which export pipeline it favoured for the transportation of Azeri gas to southern Europe by the end of Q112; however, this deadline was missed and a new one has been set for mid-2013. SDC includes BP (25.5%), Norway's Statoil (25.5%), Iran's NIOC (10%), SOCAR (10%), France's Total (10%), Russia's Lukoil (10%) and Turkey's TPAO (9%).

On June 26 2012, Turkey and Azerbaijan signed a US\$7bn agreement for the Trans-Anatolian natural gas pipeline project, (TANAP), which will carry Azeri natural gas across Turkey to Europe. The pipeline is set to begin construction in

2014 and draw supply from Shah Deniz II with first gas planned in 2018.

Azerbaijan's 2011 oil production declined by an estimated 12.1% year-on-year (y-o-y) from 2010 to 914,800 b/d. For 2012, we forecast production will rise slightly (0.46%) to 919,030 b/d, with production forecast to remain below 1mn b/d until 2014.

Declining production was due in part to maintenance-related output drops at the BP-operated Azeri-Chirag-Guneshli (ACG) oil fields, where Azerbaijan draws most of its supply. BMI had already reduced its estimate for 2011 production at the field to around 937,000b/d (-10% y-o-y), including gas liquids.

The further development of the Azeri-Chirag-Gunashi (ACG) complex and liquids from the second phase of the Shah Deniz gas field could deliver a surprise to the upside in terms of volumes but, equally, project delays could undermine progress.

Azerbaijan's dependence on energy prices leads to high volatility in the country's export revenues. However, continued demand from emerging markets and persistent efforts from Europe to secure access to gas from the Caspian ensure there will be no shortage of demand for Azeri resources. Although oil market has moved away from the cycle of tight supply we saw in 2011 and Q112, we have now arrived at marked by volatile demand and ample supply. With supply now comfortably meeting demand, we believe OPEC basket oil prices will hold steady from an estimated US\$107.52 per barrel (bbl) in 2011 to US\$107.05/bbl in 2012, creating upside risk for the Azeri macroeconomic outlook.

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