Emerging Europe: Gazprom Faces Hurdles In Crucial Year Ahead

By Andrea Chipman
Dow Jones Newswires
743 words
2 January 2001
The Wall Street Journal Europe
5
English

MOSCOW -- Russian natural gas monopoly OAO Gazprom faces a series of hurdles in 2001 that will determine whether the company continues to stagnate or takes advantage of European consumption demands to boost its fortunes.

Despite a lagging stock price and vocal complaints from minority shareholders, Gazprom has the chance to take advantage of a newly open European energy market.

But the company must develop new pipeline routes and desperately needs to attract the investment that will help it expand capacity, analysts say.

"Gazprom is going to have the possibility of increasing supplies to Europe by 10% (in 2001)," said Sergei Glaser, head of research at Alfa Bank in Moscow. "The major question is how Gazprom is drastically going to increase export capacity. It needs to attract money for investment and increase its attractiveness for investment."

Investors, in turn, have their own expectations for Gazprom in 2001: unification of the dual share structure that has caused its American depositary receipts to trade at a hefty premium to its local stock price, improvement on the corporate governance front and a replacement of current management.

Gazprom's unpopularity among investors is evident in its share price. The company's ADRs, equal to around 10 domestic shares, ended trading Friday at $6.25 (6.64 euros), down 35% from $9.55 at the start of 2000. By comparison, Russia's equities benchmark, the Russia Trading System Index, was down 4.5% on the year.

Given record-high oil prices, which lifted the Standard & Poor's International Oil Index 6% in 2000, the natural gas giant's performance is particularly dismal.

The company's local share price ended the year slightly higher at 30 cents a share, up from 27 cents at the beginning of January. However, market participants attributed the rise less to Gazprom's domestic appeal than to the distortions of the two-tier share structure.

Indeed, investors and analysts say Gazprom must eliminate the dual share structure -- which effectively prohibits foreign investors from buying the cheaper local shares -- as a first step to attracting new funding.

With a market capitalization of around $17 billion, the company is dwarfed by other large energy producers such as ExxonMobil, which has a market capitalization of more than $200 billion despite having smaller hydrocarbon reserves.

Another top priority for investors and shareholders alike is an improvement of transparency within the company, including clarification of the company's murky relations with its subsidiaries and with allies such as gas trading firm Itera.

An overhaul of the company's management is widely expected by the end of the first half of the year, when Chief Executive Rem Vyakhirev and other managers are due to step down. New faces should help Gazprom become less opaque, said Ivan Mazalov, oil and gas analyst at Troika Dialog bank in Moscow.

Also, the government, which owns 37% of Gazprom, has said it will look next year at proposals for a full-scale restructuring -- designed to increase the independence of the company's production subsidiaries and open up the country's gas market -- but Mr. Mazalov said officials would be wise not to rush the process.

"It will be critical to first clean up the company and then move on to restructure it," he said. "If the restructuring were to happen at this time, I don't think anyone would see it as beneficial."

An expected rise in domestic prices, currently around $15 per 1,000 cubic meters, will go further toward helping the company meet its costs. In the meantime, Gazprom's European gas exports remain lucrative at an average of more than $118 per 1,000 cubic meters, despite concerns that deregulation of the European gas market would have a leveling effect.

"The risk of deregulation was that it would have lowered gas prices, but we're in such a hot market that gas prices are going up anyway," said Jay Bhutani, emerging markets oil and gas analyst for Lehman Brothers in London.

In order to fulfill increased Western demand, however, Gazprom must develop new pipeline routes.

One much-discussed plan involves a new route crossing Belarus, Poland and Slovakia to deliver gas to Western Europe. An alternative plan for a second line along the Yamal-Europe pipeline route would be shorter and cheaper, and could double supplies to Germany and France, Alfa Bank's Mr. Glaser said.