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The Future of Saudi Price Discrimination: The Effect of Russian Production Increases

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The Energy Dimension in the Russian Global Strategy:

Presentation of Study Findings

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Houston



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Asian Price Premium

Year	USD/ barrel	As % of Europe
1988	0.94	7.10
1989	-0.40	-2.39
1990	-0.34	-1.56
1991	0.57	3.42
1992	0.65	3.78
1993	1.43	10.03
1994	0.75	5.15
1995	1.04	6.65
1996	-0.07	-0.37
1997	2.69	16.79
1998	2.21	22.18
1999	-0.56	-3.15
2000	1.75	6.96
2001	2.29	10.98
2002	0.58	2.44
Average 1988-2002	0.90	5.87
Average 1991-2002	1.11	7.07



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Explaining the Asian Price Premium

The Asian price premium is the result of Saudi price discrimination

Conditions for successful price discrimination:

- must possess power to set price
- Must be able to identify separate markets in which the price elasticity of demand differ
- must prevent arbitrage by third parties. That is, prevent others from buying in the low price market and reselling in the higher priced market.



Controlling Asian Supply

- Saudi Arabia prevents resale of its exports with contracts barring resale without approval. Exporters must pay the formula price based on the destination of the crude.
- There are no other Middle East producers that could (or will) exploit higher Asian prices by significantly increasing their exports to Asia.
- The alternative to Saudi oil is West African crude that is disadvantaged in Asian market because:
 - transport costs
 - higher priced lighter, sweeter crude



Significance of Increases in Russian Exports-Long Run Scenario

TABLE 5: Projections of Net Imports by Region
(Millions b/d)

	2000	2010	2020	2030
OECD Europe	7.4	10.1	12.5	13.9
OECD North America	8.6	10.8	15.4	20.9
Asia	12.5	19.5	26.6	34.0
FSU	-3.5	-7.3	-7.6	-7.8
Middle East	-19.0	-23.1	-33.0	-44.6
Rest of World	-7.0	-11.0	-15.1	-17.2

Source: IEA, World Energy Outlook 2002



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Changes in Net Imports and Exports (million b/d)

	2000-2010	2010-2020
OECD Europe	2.7	2.4
OECD North America	2.2	4.6
Asia	7.0	7.1
Transition Economies	-3.8	-0.3
Middle East	-4.1	-9.9
Other	-4.0	-4.1

Source: IEA, World Energy Outlook 2002



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Middle East Production (Optimistic) Forecast

	2000	2005	2010	2010-2000
Iran	3.75	3.80	5.00	1.25
Iraq	2.90	2.30	4.50	1.60
Kuwait	2.40	2.40	3.00	0.60
UAE	2.40	2.50	2.50	0.10
Qatar	0.73	0.75	0.80	0.07
Total	12.18	11.75	15.80	3.62



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Alternative export Scenarios of Incremental Production (2000 - 2010)

	Net Import Increase	Import Sources				Total Increase in Supply	Saudi Exports 2000	Saudi Exports 2010	Saudi Share of 2010 Demand
		Other	FSU	Non Saudi Mideast	Saudi				
Scenario 1. All FSU New Exports go to Atlantic. Saudis reduce exports to Europe to accommodate FSU									
Europe + N. America	4.9	4.0	3.8	0.0	-2.9	4.9	2.9	0.0	0.0%
Asia	7.0	0.0	0.0	3.6	3.4	7.0	3.2	6.6	25.2%
Scenario 2. All FSU New Exports go to Asia, Saudis reduce exports to Asia to accommodate									
Europe + N. America	4.9	4	0	0	0.9	4.9	2.9	3.8	9.5%
Asia	7	0	3.8	3.6	-0.4	7	3.2	2.8	10.7%
Scenario 3. FSU New Exports are evenly split between Asia and the Atlantic.									
Europe + N. America	4.9	4.0	1.9	0.0	-1.0	4.9	2.9	1.9	4.7%
Asia	7.0	0.0	1.9	3.6	1.5	7.0	3.2	4.7	17.9%



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Conclusions

Ways to eliminate the Asian premium:

- end destination based pricing
 - challenge practice in various world organizations
 - take legal action to bar international oil companies from facilitating destination pricing
- reduce Saudi share of Asian market
 - import more petroleum products produced from non-Saudi crude
 - promote inter-fuel competition - including gas-to-liquids
 - de-link LNG and coal prices from crude
 - promote conservation and energy efficiency (gas-electric hybrid cars - especially in China and other developing economies)
 - develop clean coal and other technologies that reduce the demand for oil

If growth in Asian demand between 2000 and 2010 were reduced by 1 million b/d, the Saudi share of the Asian market would fall to 7.1% under scenario 2.



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