

A state-controlled Rosneft privatisation under BP watch

Blog post by Adviser Alexander Smotrov, 20 July 2016

The long-anticipated privatisation of the 19.5% government-owned stake in Russia's largest oil company, Rosneft has finally started to take shape with the government expected to reveal their offer to investors in the next two weeks. With BP owning 19.75% of Rosneft, making them the largest single private shareholder, this process will be watched as closely in St James's Square as in Red Square.

Ten years ago, in July 2006, Rosneft placed its IPO on the London Stock Exchange. Pumped-up with its newly acquired former Yukos assets, it offered a fifth of its shares worth \$10.4bn to international investors, including BP, in what became the largest Russian corporate public offering in history. Oil prices stood at a then record-high of \$75 per barrel, Russian IPOs were mushrooming and global investors were hungry for booming Russian assets.

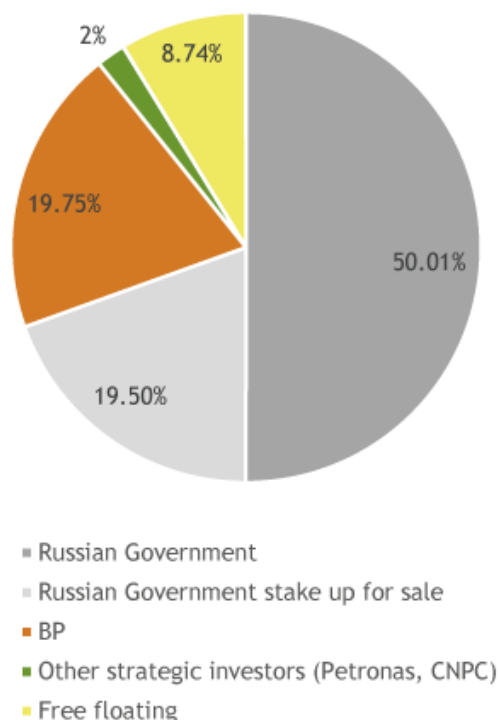


Fig: Rosneft shareholders
Source: Rosneft, public sources

A decade later, Rosneft - which recently overtook Gazprom by market capitalisation as Russia's largest corporate - is back on the privatisation butcher's block. Given ongoing Western sanctions and the slump in oil prices, the cash-strapped Russian government decided to accelerate the privatisation to raise funds to balance up the state budget. This would help the Kremlin to maintain economic and social stability in the 18 month electoral cycle which Russia is now entering.

The government, pressured by powerful Rosneft CEO Igor Sechin who was against any privatisation unless the oil price returns to \$100, has finally shed some light on the three major parameters of the sale - the timing, the price and the possible range of investors.

The preferred option now will not be an SPO but a sale of the whole stake, with a market value of up to \$11bn, to a small number of strategic investors - preferably one - on certain conditions, including a three year freeze on resale and support for government-

nominated board members. Moscow wants predictability on its own terms and less reliance on the West while its access to the international capital markets is restricted.

Realistically, this narrows down the number of potential acquirers to two choices: either a Chinese or Indian state-linked energy giant, or one of the loyal Russian oligarchs repatriating capital back into the country (or it could be a combination of all three). In any case, the Kremlin will retain a high degree of control over the asset while extracting the maximum possible value from the buyer.

The Western sanctions on Rosneft have so far had little impact on the BP-Rosneft relationship. The British company, which has been tempered by a decade-long tug of war with the Russian authorities and Russian shareholders of TNK-BP, apparently managed to insulate itself from both external and internal risks by becoming a 'strategic partner' for Rosneft three years ago. However, the bilateral energy relationship, often managed on the highest level between London and Moscow, might now get a bit more crowded and need to accommodate a third party playing by separate rules. The question is how comfortable BP will feel at the Rosneft board table with new faces who are perceived to be more closely aligned to the management (and Kremlin) than BP?