

**Key takeaways:**

Gasoil Trade Flows: Growth of Russia's gasoil surplus, competition from the U.S., and quality constraints will cause more Russian gasoil to flow to Asia and less to the Western Hemisphere (pg. 1).

Fuel Oil Exports to Climb: Russian fuel oil exports will pick up again in the second quarter, one of several bearish developments in global fundamentals that should cause discounts to widen (pg. 3).

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MORE RUSSIAN GASOIL TO FLOW EAST

Crude oil is not the only area in which Russian exports to Asia are growing. Russia exported 112,000 b/d of gasoil to Asia in 2009, up 60,000 b/d from 2008. Relying on a variety of data sources and on ESAI's analysis of global trade flows, this issue of CISWatch examines patterns in Russian gasoil exports and likely future developments.

Weak refining margins led to lower European gasoil output in 2009, causing European net imports to grow 170,000 b/d in 2009 to 750,000 b/d. According to import data, Russia captured more than half the increase, with imports growing from 330,000 b/d to 424,000 b/d (see chart). Russian export data indicate Europe absorbs even more Russian gasoil, which may be in part explained by definitional differences. Russian data show significantly higher exports to Italy and the United Kingdom. On the other hand, Russian export data show large flows to the Netherlands and Latvia, much of which is clearly ultimately destined for other markets. The "other" category on the chart, which comprised 150,000 b/d in 2009, is comprised of additional gasoil either exported to Europe or re-directed to other markets.

The biggest development in terms of new market penetration was the doubling of exports to Asia. In 2009, Russia shipped 27,000 b/d of gasoil to Singapore and another 17,000 b/d to Hong Kong, up from just 3,000 b/d and 1,000 b/d respectively the year before. Russia exported another 44,000 b/d to China and 11,000 b/d to Vietnam.

It is somewhat surprising that there apparently is no new market penetration in South America. In terms of quality, South America is a natural fit for Russian gasoil and ESAI in the past predicted that the region would absorb gasoil from FSU countries. It could be that the region ab-

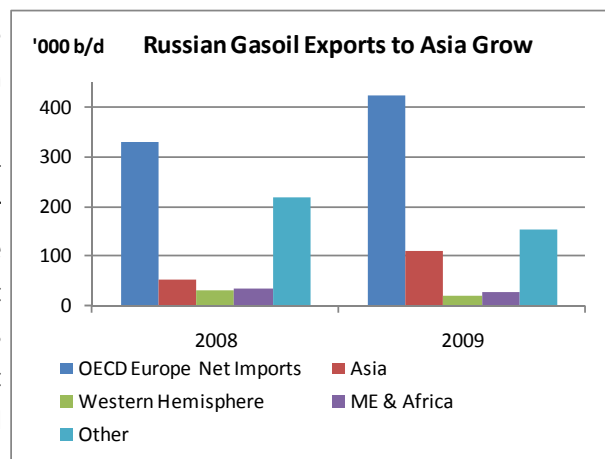
sorbs more Russian gasoil from the Netherlands or elsewhere and that these flows are not captured by Russian

export data. At the same time, the U.S., itself a significant gasoil exporter, has a geographic advantage over Russia in this market.

What Next?

The increase in outflows to Asia contrasts with a growing flow of gasoil from Asia to Europe. Europe is importing a growing amount of quality diesel from Korea, while Asia is an appropriate market for inferior quality Russian gasoil. Russian gasoil will continue to find its way to Asia, though China is not a growth market due to its expanding refining capacity.

In the Atlantic Basin, the U.S. is a competitive threat to Russia due to the quality of its exports and their growing volume (see March issue of Atlantic Basin Stockwatch Marketview). Russia can defend its position in Europe by increasing Euro5 10ppm diesel exports. The new Nizhnekamsk refinery, to start operating in October 2010, will eventually produce 55,000 b/d of Euro5 diesel. That development will enable Russia to increase Euro5 diesel exports from the Baltic Sea, currently about 100,000 b/d.



Selected FSU Crude Exports to non-CIS States (000 b/d)												
	Exports to non-CIS States			Urals from Main European Pipeline &			Light Sweet from Black Sea & Mediterranean Ports			Asia		
	Russia	Kazakhstan	Azerbaijan	Black Sea	Baltic Sea	Druzhba	CPC Blend Novorossiisk	BTC Blend Ceyhan (1)	Other Light Sweet (2)	China (3)	Sakhalin	ESPO Blend to Kozmino Bay
				31.8 API, 1.35% S			43.3 API, 0.59% S	34.8 API, 0.16% S			Light sweet	32.6 API, <1.0% S
Jan-09	4,277	1,216	645	1,226	1,470	1,205	761	593	138	225	269	-
Feb-09	4,255	1,593	869	1,246	1,531	1,204	759	681	242	234	274	-
Mar-09	4,180	1,238	852	1,118	1,521	1,222	768	729	191	288	273	-
Apr-09	4,354	1,331	878	1,173	1,574	1,230	745	713	239	329	277	-
May-09	4,415	1,321	930	1,269	1,467	1,297	684	787	219	316	261	-
Jun-09	4,254	1,356	919	1,082	1,581	1,221	744	821	182	325	280	-
Jul-09	3,894	1,373	916	1,026	1,464	1,146	747	776	198	345	267	-
Aug-09	4,144	1,346	867	1,109	1,579	1,141	716	774	134	353	246	-
Sep-09	4,309	1,305	897	1,092	1,522	1,237	746	780	211	365	325	-
Oct-09	4,227	1,205	874	1,042	1,604	1,241	744	772	212	302	292	-
Nov-09	4,033	1,205	835	1,072	1,486	1,243	742	725	207	357	279	-
Dec-09	4,327	1,647	721	1,133	1,556	1,246	758	664	203	366	285	24
Jan-10	4,405	1,350	609	951	1,567	1,287	796	556	167	338	305	210
Feb-10	4,282	1,350	967	924	1,281	1,271	714	794	212	408	293	265
Mar est	4,450	1,350	870	1,050	1,450	1,150	745	680	225	410	280	295
Apr est	4,450	1,350	870	1,100	1,500	1,150	745	680	225	410	280	310
May est	4,450	1,350	870	1,100	1,500	1,150	745	680	225	410	270	315
Jun est	4,400	1,350	870	1,050	1,450	1,150	745	680	225	410	270	315

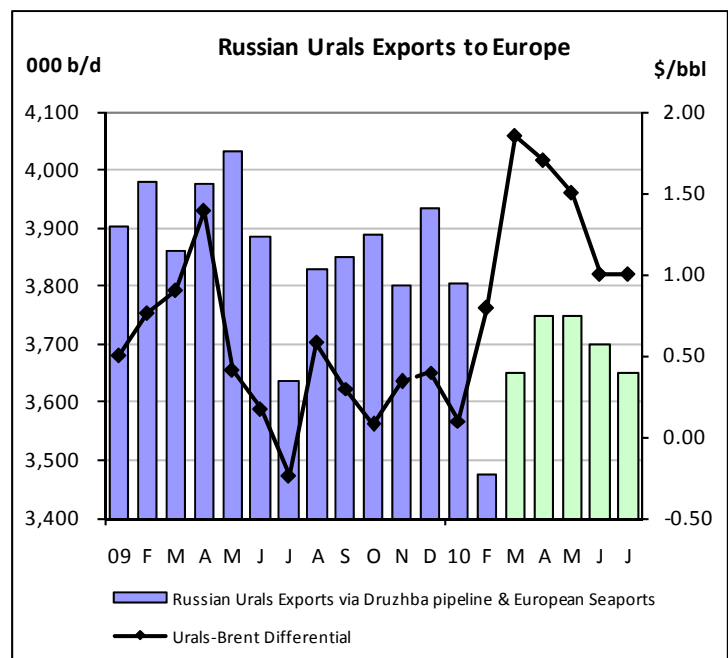
1. BTC Blend includes supply to Ceyhan from Azerbaijan and Kazakhstan.
 2. Other light sweet is composed of Siberian Light from Russian port of Tuapse and Azeri crude exported from Georgian Black Sea (excluding deliveries to Ukraine). Figures do not include additional small volumes of crude from Kazakhstan and Turkmenistan exported from Georgia's Black Sea.
 3. Exports to China include overland deliveries from Russia and Kazakhstan.

Asia

Exports of ESPO Blend from Kozmino Bay likely averaged 295,000 b/d in March and are expected to plateau at about 315,000 b/d from May (see table). Meanwhile, overland deliveries of Kazakh crude through the Atasu-Alashankou pipeline exceeded 200,000 b/d in February. China recently ceased importing Russian crude by that route and is increasing its take of crude from Kazakhstan. Combined overland and sea exports will reach one million b/d in April, up from 600,000 b/d six months ago.

Urals

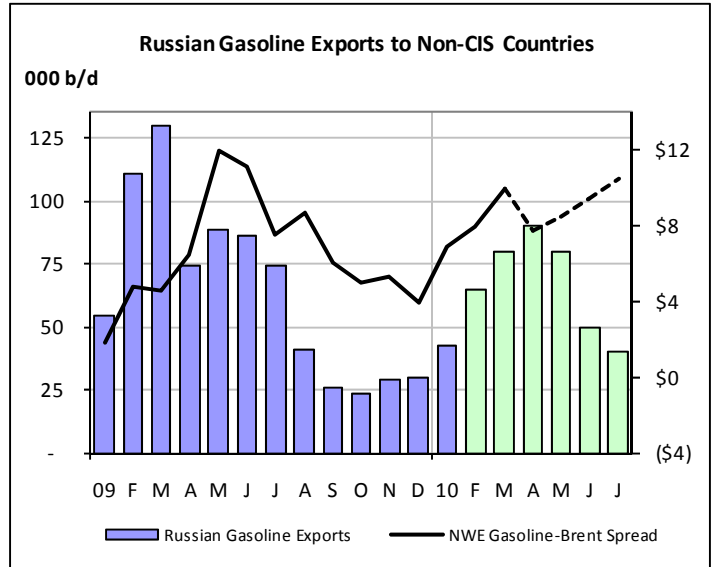
Exports of Urals to non-CIS countries in Europe fell to just 3.5 million b/d in February, with weak outflows from all directions (see table). Strong domestic throughput in February contributed to the decrease, as did Kazakhstan's shift of crude outflows to China and away from Russia (see above). ESAI expects Urals exports to recover from February's unusual low, especially as throughput eases. Average volumes will level off at just over 3.7 million b/d in the second quarter, down 200,000 b/d from a year ago. Reduced outflows in February were a



bullish development, but refinery maintenance in Asia reduced that region's draw of Urals and medium sour from the Middle East. The resulting softer medium sour fundamentals caused the discount of Urals to Brent to widen. The draw from Asia will pick up after the shoulder season and cause the discount to narrow again.

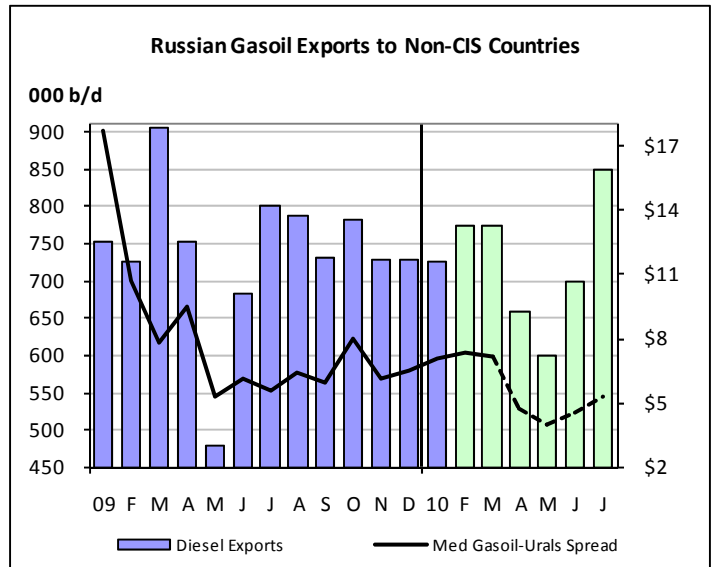
Gasoline

Russian gasoline exports should pick up from April due to seasonal demand trends. At the same time, Russia’s annual gasoline balance remains quite static. Demand averaged 730,000 b/d in 2009, unchanged from 2008. Production was also steady at 830,000 b/d, leaving a 100,000 b/d gasoline surplus. With slightly more than half of gasoline exports destined for non-CIS markets, exports averaged 64,000 b/d in 2009. Demand weakens seasonally in the second quarter, which should lead to above-average exports. ESAI projects gasoline outflows to non-CIS countries will average 75,000 b/d in the second quarter.



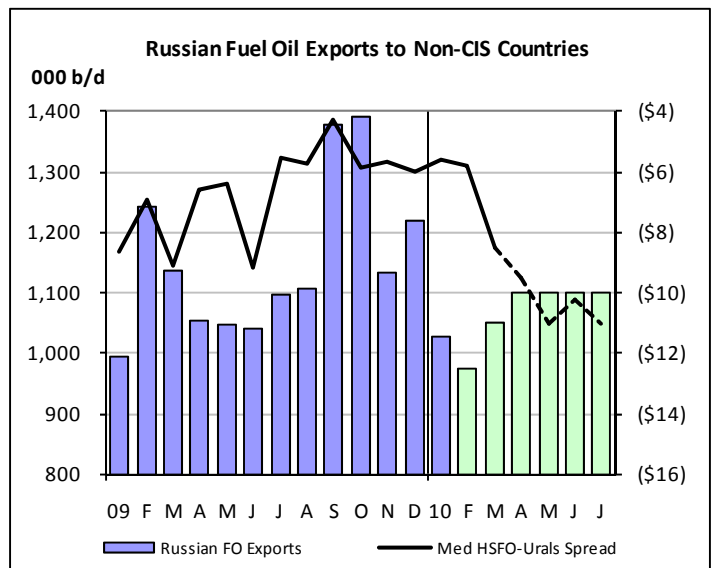
Gasoil

Gasoil exports will remain strong in 2010 due to weak demand. Annual demand declined 80,000 b/d (12 percent) in 2009 and weak industrial output growth suggests the recovery will be slow. Exports to non-CIS countries averaged 725,000 b/d in the three months through January, slightly lower than the total 2009 average of 740,000 b/d. Strong diesel demand in the agricultural sector typically undermines exports in the early second quarter, such as in May 2009 (see chart). ESAI does not expect average exports to be much less than 740,000 b/d in 2010, but increased seasonal demand will again undermine exports in the April-May period. Though reduced exports are bullish, that will be little relief for still bearish distillate inventory levels in Europe.



Fuel Oil

Strong demand reduced Russia’s fuel oil surplus in the first quarter. As a result, exports to non-CIS countries fell to a one-year low of 1.03 million b/d. Though that volume is 120,000 b/d less than the 2009 average of 1.15 million b/d, exports were still up year-on-year. After continued weak exports in the first quarter, seasonally weaker demand will cause exports to again climb to at least 1.1 million b/d in the second quarter. Growth of Russian exports in the second quarter is one of several bearish developments in global fundamentals that should cause discounts to widen.



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Crude & Condensate Production in CIS Countries, '000 b/d

	Azerbaijan	Kazakhstan	Belarus	Ukraine
Jul-08	1127	1366	35	88
Aug-08	662	1318	35	87
Sep-08	810	1356	35	84
Oct-08	690	1450	35	86
Nov-08	756	1493	35	84
Dec-08	840	1526	35	88
Jan-09	860	1499	35	86
Feb-09	975	1518	35	77
Mar-09	958	1490	35	86
Apr-09	1101	1544	34	82
May-09	1071	1478	34	84
Jun-09	1080	1568	34	81
Jul-09	1021	1611	35	86
Aug-09	1043	1533	35	86
Sep-09	1055	1540	35	82
Oct-09	1052	1616	35	82
Nov-09	1004	1658	35	76
Dec-09	953	1638	34	76
Jan-10	1012	1585	34	78
Feb-10	972	1658	34	79
Mar est	1010	1590	35	79
Apr est	1030	1640	36	79
May est	1040	1590	37	79
Jun est	1060	1690	38	79

Belarus & Ukraine product exports to non-CIS countries, '000 b/d

	Mogas	Gasoil	Resid
Jul-08	46	89	135
Aug-08	38	65	93
Sep-08	46	79	134
Oct-08	65	114	152
Nov-08	57	99	145
Dec-08	60	105	126
Jan-09	54	122	123
Feb-09	46	100	110
Mar-09	38	80	122
Apr-09	48	81	156
May-09	55	61	188
Jun-09	34	67	194
Jul-09	34	65	167
Aug-09	34	75	137
Sep-09	20	51	188
Oct-09	12	71	168
Nov-09	25	62	217
Dec-09	34	68	238
Jan-10	42	66	152
Feb est	20	40	100
Mar est	20	40	105
Apr est	20	35	110
May est	20	45	115
Jun est	20	45	115

Selected CIS Countries Supply and Demand in January 2010 (000 b/d)

	Production				Thrup	Implied Demand			3 Products total
	Crude	Mogas	G&D	Resid		Mogas	G&D	Resid	
Azerbaijan	1012	29	53	2	134	26	16	2	44
Belarus	34	60	121	85	293	15	57	24	96
Kazakhstan	1585	78	84	72	278	73	63	26	162
Ukraine	54	72	65	58	238	85	64	13	162
Total	2685	238	323	217	942	198	200	65	463

Exports by Selected CIS Countries in January 2010 (000 b/d)

	Crude			Mogas		Diesel		Resid	
	CIS	non-CIS	total	CIS	non-CIS	CIS	non-CIS	CIS	non-CIS
Azerbaijan	55	609	664	1	2	5	32	0	0
Belarus	0	0	0	6	42	16	61	2	109
Kazakhstan	40	1630	1670	0	1	5	15	2	40
Ukraine	0	0	0	8	0	3	5	8	43
Total	95	2239	2334	15	44	28	113	12	192

Note: Includes some ESAI estimates.

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