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Fertilizer Industry Resists Rising Gas Prices

By Alexandra Terentyeva

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Having accepted the inevitable liberalization of gas prices, manufacturers of nitrogen fertilizers are seeking their own formula for how to calculate what they will have to pay for their primary raw material.

Starting in 2014, domestic gas prices will be liberalized to give producers equal profitability for domestic sales and exports to Europe. But industrial consumers of the fuel are already concerned.

In a joint letter to Prime Minister Vladimir Putin sent last week, the heads of 18 companies that make nitrogen-based fertilizers wrote that "plans to liberalize the Russian market for natural gas and the principle of equal profitability with the contractual price of gas for Europe ... will lead to the extinction of the domestic fertilizer industry."

The chemical companies are asking for a special gas pricing formula. The price should be

calculated using the minimal contract or spot price, or a combination of the two, for the West European markets of Germany and the Benelux countries, minus transportation costs and the export tax, they wrote.

The formula proposed by the Federal Tariffs Service, which would allow Gazprom equal profitability on the domestic and foreign markets, differs from that proposal only in that it relies on an average price derived from Gazprom's European contracts, which are based on a basket of oil products. The difference in price, however, is significant.

Gazprom's average European price is now about $280 for 1,000 cubic meters, while the forecast for the year is $308. European spot prices are much lower, averaging $207 in the first quarter and $214 in the second quarter on Britain's National Balancing Point exchange.

Denis Borisov, an analyst with Bank of Moscow, used the industry-proposed formula and found that it would now give a price of $120 to $130 per 1,000 cubic meters. Using the Federal Tariffs Service's formula the price would be $160 to $170, or about double what fertilizer companies are paying now.

A Gazprom spokesman declined to comment on the fertilizer manufacturers' initiative.

The agrochemical industry is one of the largest gas consumers. Gas is the main raw material used to make nitrogen fertilizers, ammonia and methanol, and it constitutes 65 percent of the manufacturing cost. As much as 80 percent of Russian fertilizer is exported, giving the country 7.4 percent of the world market.

The companies are concerned that after gas price liberalization their products will be uncompetitive. After all, the letter pointed out, a chemical complex in Oman will get gas for nine years at a price of no more than $27 per 1,000 cubic meters.

Until now, fertilizer manufacturers have stockpiled only raw materials directly related to production, buying up deposits of apatite-nepheline ore and potash. The only company with its own gas project was Acron, which had 21 percent of Sibneftegaz, but prices were prohibitive and they had to sell the stake.

"The gas business is too expensive," said a senior manager at one of the chemical companies. "Everyone should focus on their own core business, and make deals on everything else, otherwise you wind up building your own railroad to transport your own materials."

In the letter, the fertilizer makers also asked to be allowed to buy gas from independent producers on a priority basis, with guaranteed access to the pipelines, and they requested a 40 percent reduction on rail transportation tariffs for ammonia.

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