



ICIS [Special Supplement]



VERTICAL INTEGRATION
**SIBUR ACHIEVES
FEEDSTOCK &
ENERGY AND
PETROCHEMICAL
BALANCE**

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COMMENTARY

Welcome to this special SIBUR publication prepared by ICIS. Vertical integration has ensured SIBUR's rapid growth to become the leading gas processor and producer in Russia, CIS and central and eastern Europe – and the coming years mark an equally significant period in its brief history.

In its two main business divisions, feedstock & energy and petrochemicals, SIBUR continues to enjoy improving revenues and EBITDA margins, while it is also investing heavily in its portfolio and infrastructure despite the global economic downturn.

The imminent completion of several landmark projects – including Tobolsk-Polymer, RusVinyl and Ust-Luga, all featured in this supplement – offers huge potential, allowing the company both to access new markets and to strengthen its position.

Combine that with its endeavours to expand its footprint in developing markets, via agreements with major petrochemical players, and SIBUR's future is looking secure.

ANDY BRICE LONDON
 andy.brice@icis.com



Editor
 Andy Brice

Production
 Louise Murrell


Product director
 David Stanworth

Sales manager
 John Hill

Printed by
 Williams Press, UK

ICIS, The Quadrant, Sutton, Surrey,
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 +44 20 8652 3187
 www.icis.com

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 Reed Business Information

The RF Government urges chemical focus

Extracts from speech given by Russian energy minister Aleksandr Novak at a government meeting on the development of the chemical and petrochemical industries, Bashkortostan, 3 July 2013

“The Russian petrochemical industry is engaged in processing oil and gas production by-products, as well as oil refining. The petrochemical industry’s output includes polymers, synthetic rubbers, organic alcohols, oxides and glycols.

The industry currently has a surplus of hydrocarbon feedstock but makes up just 1.5% of GDP. Meanwhile the amount of investment is growing – roubles (Rb) 225bn (\$6.89bn, €5.29bn) last year, which is almost 50% more than the year before.

Considering Russia’s position as an exporter of feedstock for the petrochemical industry, it is important for us to understand what external challenges we face. There are three key challenges that I would like to highlight.

The first is the development of non-traditional hydrocarbon fields in North America, by which I mean shale gas and shale oil. As we all know, overall these have had a major impact on lowering the cost of the relevant feedstock in the US and on the competitiveness of the petrochemical industry.

The second challenge is the construction of new facilities in the Middle East, which today hosts the highest concentration of refinement activities. At the same time, the Middle East actually subsidises the production of ethane, a feedstock for the petrochemical industry, and the price of ethane in the Middle East today is about 15% of the cost of alternative sources.

The third challenge is expanding production of petrochemical raw materials and products in the Asia-Pacific region, including through the use of alternative technologies that will produce feedstock from coal.

As for domestic challenges, which we also regard as opportunities, today’s most significant issue concerns the lack of cracking and processing facilities in general, to cope with the large quantities of raw materials available. At the same time, we are seeing large volumes of petrochemical imports despite continued increase in demand for polymer production in the domestic market.



We need to boost the sale of finished products on the domestic market. And it is very important that the construction rate of new production facilities continues to outpace the growth in domestic consumption.

We expect the volume of petrochemical feedstock processed by petrochemical plants to double, while the number of cracking facilities will increase, with total capacity growing 4.5 times by 2030. At the same time, average per capita consumption of plastics and rubbers will grow 3.4 times and 2.6 times, re-



“It is very important that the construction rate of new production facilities continues to outpace the growth in domestic consumption”

ALEKSANDR NOVAK
Russian energy minister

spectively. Other countries currently consume around 1.5-3 times more plastic than we do.

Regarding petrochemical products, total production of polyethylene (PE), for example, will increase by 5.9m tonnes by 2020. Importantly, by 2017 we will have stopped importing PE, we will have a surplus on the domestic market, and it will be necessary to export and to develop domestic consumption.

The situation with polypropylene (PP) is similar, with imports of this polymer ceasing at some point between 2014 and 2017. The most effective method of stimulating domestic demand for petrochemical products is to decrease the imports of finished polymer products, which currently stand at close to 1m tonnes/year.

In addition to taking measures to stimulate the development of the domestic market, we suggest that the Ministry of Energy of the Russian Federation, together with other federal authorities, come up with a proposal to improve tax and customs rate policies in the hydrocarbon feedstock processing sector over the long term, in order to help attract investment and level out profits between different productions areas in the industry.” ■

SIBUR goes from strength to strength

Ambitious plans by Russia's largest petrochemicals company should cement its place as one of the leading players in the Russian, CIS and eastern European markets

Having enjoyed phenomenal growth in recent years, SIBUR has become one of the best performing petrochemical companies. This year marks arguably one of the most important chapters in its history, says CEO Dmitry Konov.

While many producers continue to face increasing cost pressures, with feedstock volatility and fluctuating demand eroding their bottom line and impacting profitability, the Russian major finds itself in an enviable position. As a vertically integrated gas processing and petrochemicals company, its resilience to the effects of the global financial crisis has not only allowed it to strengthen its portfolio but to achieve significant capex growth and undertake several large-scale investment projects. Total revenues for 2012 were up at rouble (Rb) 271.3bn (\$8.63bn, €6.66bn), and only a couple of months ago the company successfully issued its debut Eurobond and raised \$1bn.

SIBUR owns and operates Russia's largest gas processing business and consists of two operating segments: feedstock & energy and petrochemicals.

The energy business processes associated petroleum gas (APG) and specialises in the sale of natural gas, liquefied petroleum gases (LPG), raw NGL, naphtha and methyl tertiary butyl ether (MTBE) both domestically and internationally. The focus of its petrochemicals segment, meanwhile, is split between three lines: basic polymers (including polypropylene (PP), polyethylene and polyvinyl chloride (PVC)), synthetic rubbers, and plastics and organic synthesis (such as polyethylene terephthalate (PET), glycols, biaxially-oriented polypropylene (BOPP) films).

As of December 2012, SIBUR operated 27 production sites across Russia, and employed more than 30,000 staff – figures which Konov says will soon rise with several flagship projects nearing completion.

“We’ve been accelerating efforts to make changes in the company and have invested a lot of resources into creating capacity to run



Konov believes Russia has a lot of hidden potential

investment projects. It is often the best time to invest at the bottom of the cycle as projects of this scale take many years to complete," adds Konov. "Our strategy is about increasing market coverage, and we believe our major development areas are still in Russia where you can have very competitive production."

"Over the last few years SIBUR has more than doubled its gas processing capacities, expanding its pipeline infrastructure as well. This enables us to build large petrochemical facilities at a competitive cost," he says.

SIGNIFICANT INVESTMENT

SIBUR's landmark Tobolsk-Polymer project (see page 12) is scheduled to come on stream soon and will see the company double its basic polymers production capacity.

This project is among a series of new domestic capacities coming on stream that are expected to make the country capable of substituting imports of basic PP grades and becoming an exporter of PP.

The plant is costing around RB60bn, while over 70% of this (\$1.44bn) has been raised from international financial institutions. The syndicated loan was arranged by the Russian Bank for Development and Foreign Economic Affairs (Vnesheconombank), which is also one of the key creditors.

"It's safe to say that in terms of scale and the parties involved, the Tobolsk-Polymer loan financing scheme is unprecedented for modern Russian industry," says Konov.

Also due for completion next year is RusVinyl, a 50:50 joint venture between SIBUR and Belgium-headquartered SolVin, which will see the construction of a 330,000 tonne/year PVC plant and a 225,000 tonne/year caustic soda unit (see page 14). SIBUR is keen to capitalise on the thriving PVC market in Russia and CIS.

Among its other developments is the construction of a liquefied petroleum gases (LPG) and light oils transshipment facility at Ust-Luga seaport near St Petersburg (see page 15).



"We believe that with the type of feedstock allocation and pricing we enjoy in our business we will be competitive"

DMITRY KONOV
CEO

The major greenfield project will have a capacity of 1.5m tonnes/year of LPG and 2.5m tonnes/year of light oils.

By the end of 2013, a decision will be made on the approval of the ZapSibNeftekhim project, which is currently at the front-end engineering design (FEED) phase and will include a 1.5m tonne/year ethylene cracker and 2m tonnes/year of polymers.

DOMESTIC FOCUS

Russia's domestic market remains the priority for the business with key bulk commodities

expected to see strong growth in the coming years, says Konov.

"We are definitely optimistic in the mid-long term," he says. "There is enough competitively-priced stranded feedstock for petrochemicals in the region and very few alternative methods of monetizing it. This feedstock allows us to be extremely competitive from the cost side. Russia also has very low consumption of major petrochemical products because of a lack of investment in the past so there is a high potential for demand growth.

"In terms of petrochemicals, when we bring this product to the Russian market through some of our projects – RusVinyl and Tobolsk-Polymer – this will spur investment in processing and eventually grow our consumption. Unfortunately, growth markets in terms of consumption are sometimes very different to growth markets in terms of production," adds Konov.

Despite the emphasis on Russian markets, there are also several joint ventures planned where SIBUR will form international partnerships and provide its knowledge and technology. By establishing agreements with major global producers, SIBUR will soon be able to tap into high growth developing regions such as India and China, he says.

TOUGH TIMES

With the global financial downturn, greater competition from emerging regions, rising costs and increasing environmental pressures, the industry is clearly in a period of transition, says Konov.

While the US readies for a new era of advantaged feedstock through the discoveries of shale gas, China is seeing developments based on coal to olefins and gas to olefins technologies, which would have been prohibitively expensive in other regions of the world, he says.

The Middle East, meanwhile, looks likely to continue developing petrochemicals from heavier feedstocks and is focusing more on integrated sites such as Sadara and PetroRabigh.

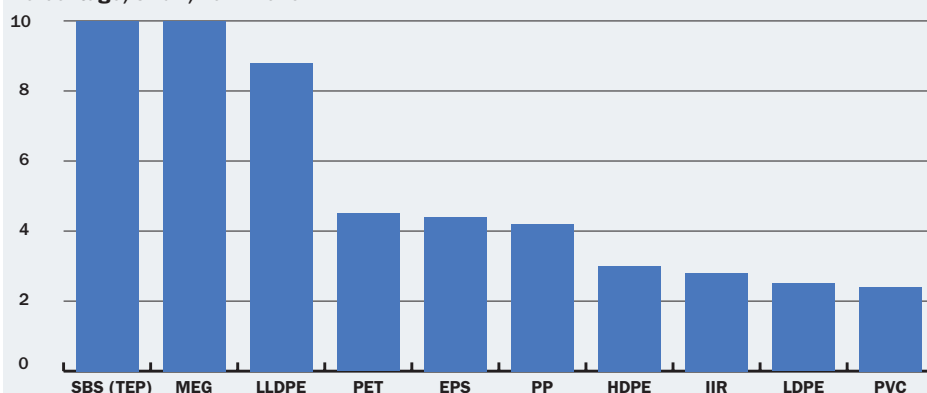
Europe remains one of the most disadvantaged regions on a cost basis and feedstock availability. Not only have financial constraints subdued spending but producers are typically heavy feed-based and integrated with refineries so suffer from two angles, says Konov.

Europe's move towards specialties rather than commodities should however leave it less vulnerable to feedstock costs.

"Compared with all of these regions, we believe that with the type of feedstock allocation and pricing we enjoy in our business we will be competitive," he says. "Fundamentally I believe that Russia has lots of potential. ■

RUSSIA CONSUMPTION GROWTH OUTLOOK

Percentage, CAGR, 2011-2020



SOURCE: SIBUR

SIBUR story makes historic strides

The company's rapid development has seen it become a major force in the feedstock & energy and petrochemical markets

It is not even two decades since SIBUR was founded, but the company is now the largest integrated petrochemicals company in Russia, Commonwealth of Independent States and central and eastern Europe in revenue terms and one of the leading producers. With access to advantaged feedstock through the development of world-scale production facilities and infrastructure in Western Siberia – home of the largest proven oil and gas reserves in Russia – SIBUR has developed a strong vertically integrated business model that compares favourably with its peers.

The company has grown rapidly since it was established in 1995, reporting increased revenues of roubles (Rb) 271.3bn (\$8.63bn, €6.66bn) for 2012 and recently raising \$1bn through its debut Eurobond listing.

The company was founded by an act passed by the government of the Russian Federation in March 1995, with 38% of its shares state-owned. The remaining 62% of the company was made public.

Towards the end of 1998, SIBUR started its transformation into a vertically integrated petrochemical holding with a full production chain from the processing of raw materials through to the manufacture of finished goods.

SIBUR subsequently built up assets by buying stakes in petrochemical companies all over Russia. Some 60 companies soon belonged to the company.

By 2001, Gazprom had acquired control of SIBUR with a 51% stake. Alexander Dyukov was appointed president in February 2003 and oversaw significant reform with the introduction of a long-term growth strategy.

By September, the stock was divided between Gazprom (25%) and Gazprombank (75%). Dyukov was succeeded by Dmitry Konov as SIBUR's new president towards the end of 2006.



Gazprom HQ: home to SIBUR's majority owner from 2001-2008, since when the two have been partners with no affiliation between them

Gazprom decided that the petrochemical business was a non-core asset in 2008, and SIBUR shares were sold to Gazfund in exchange for its energy assets. Both Gazprombank and Gazfund also withdrew from the Gazprom group. In December 2010 Gazprombank began a phased sale of SIBUR to a private shareholder, Leonid Mikhelson.

In 2011, its non-core tyre and mineral fertilisers segments were sold. SIBUR's focus was now its main polymer business.

The past few years, in particular, have seen the Russian giant embark on a series of land-

mark projects and joint ventures, which will provide access to new markets and help boost profitability. With the likes of its Tobolsk-Polymer, RusVinyl and Ust-Luga projects nearing completion, and joint venture agreements established with global petrochemical players such as India's Reliance and China's Sinopec, the future for SIBUR is certainly looking bright.

Since July 2013, SIBUR Holding is 82.5% owned by Mikhelson and Gennady Timchenko, as well as some current and former members of the management of OOO SIBUR and OAO SIBUR Holding, who own 17.5%. ■

Funding the future

Challenging market conditions have done little to dampen SIBUR's optimism as its robust business model and increased investment provides a solid base for growth

SIBUR's new CFO is bullish about the future. Despite difficult trading conditions, lacklustre demand and weak pricing for many of its petrochemical products over the past year, Pavel Maliy says the effects have been largely offset by increased production and several strategic acquisitions by the company.

The company reported a 9.1% increase in revenues in 2012 to rouble (Rb) 271.3bn (\$8.63bn, €6.66bn), fuelled by energy products and higher production and sales volumes for most products.

Sales volumes for petrochemical products increased by 4.9% in 2012, compared with 2011, to 2.27m tonnes.

Plastics and organic synthesis production increased by 39.1% during the year to 844,836 tonnes, while basic polymers production climbed by 3.4% year on year to 385,794 tonnes.

Synthetic rubbers production was most affected by the challenging market environment, stagnant demand and weak pricing trends – resulting in a slight decline of 0.7% year on year to 423,348 tonnes.



“Despite the challenging global environment, everything we’re doing is in line with, or better, than most of our petrochemical peers”

PAVEL MALIY
Chief financial officer

RESILIENT MODEL

Although the results suffered slightly following a strong 2011, Maliy says the performance demonstrates the resilience of SIBUR's model, with the company's increased investment offering good growth prospects for the future.

“We have certainly had areas where business has been more difficult than overall – but we are very satisfied with our results,” says Maliy.

“Despite the challenging global environment, everything we’re doing is in line with, or better, than most of our petrochemical peers. We continue to show a strong profitability trend at well above 30% and remain one of the top international petrochemical companies by EBITDA margin, which shows the strength of our model.

“Importantly, we are satisfied with our progress in delivering on our key objectives: continuing to grow our strategic investment plans and the security of our main feedstock streams, associated petroleum gas (APG) and natural gas liquids (NGLs).”

Earlier this year, SIBUR's debut Eurobond raised \$1bn. The issue was 5.5 times oversubscribed with orders received from 280 international accounts. »

MARKET SHARE

SYNTHETIC RUBBER BUSINESS FOCUSED ON HIGHER MARGIN PRODUCTS

SYNTHETIC RUBBER is one of the most complex chemistries in SIBUR, says Mikhail Gordin, managing director, head of synthetic rubbers division. The large scale specialty rubbers are the company's most expensive products on a per tonne basis. In 2012, the business represented around 15% of SIBUR's revenue.

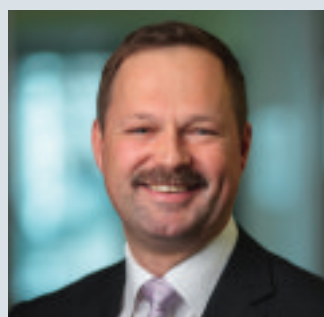
The synthetic rubber business has a significant market share in Russia, with 48% of basic rubbers and 65% in specialty rubbers in 2012, according to the Russian Rubbers Producers Association. The company is ranked in the top 10 in terms of global production, amounting to 423,348 tonnes last year. Sales are split roughly 41:59 between domestic and export markets.

“Part of our strategy is to have higher margin products to help protect us from any downturn,” he says.

“Higher margin products give us some price stability compared with more commoditised products. Clearly there is no point trying to expand volumetrically so we want to concentrate on improving margins.”

SIBUR enjoyed high margins during a period of decent consumption in 2010-2011 but demand has since slowed. In Q1 2013, specialty and commodity rubbers remained depressed because of both lower sales volumes and a decrease in the effective average selling price, says Gordin.

“Russia is now becoming more focused in terms of development and is producing more sophisticated, high-end products. We’re concentrating on efficiency and life-cycle assessment for our rubbers and have new styrene-butadiene-styrene (SBS) production that started in May for



Mikhail Gordin, managing director, head of synthetic rubbers division

higher value products and extra margin. It's a very cyclical market; today we're at a low point in the cycle, but we're hoping prices will soon go up.”

The facility in Voronezh is the only styrene-butadiene thermoplastic elastomers (TPE) producer in Russia. The innovative polymer will

be used in road construction to improve crack, heat, shear, water and frost resistance and help to reduce maintenance costs.

SIBUR announced its decision to build 50,000 tonnes/year of SBS production in 2009 and construction started in July 2011. It is also expanding a butyl rubber facility in Togliatti by 5,000 tonnes/year to 53,000 tonnes/year. Moving forward, Gordin says that it is considering the expansion of the capacities of its solution styrene butadiene rubber (S-SBR) and neodymium based performance butadiene rubber (Nd-PBR), hi-tech grades for high speed tyre applications with lower rolling resistance. Demand is growing for these more sophisticated grades, he says, which have been far less impacted than other segments. ■

» “This debut means that SIBUR has now established secure access to yet another pool of funding, which will help us with negotiations and creates a healthier situation going forward,” says Malvi. “What we have achieved through this issue is that SIBUR is now, for all intents and purposes, a public company. We have \$1bn of securities outstanding in the market and predominantly international institutional investors, and they expect us to behave as a public company.”

“SIBUR now has fully transparent records in terms of accounting, and we have an international-style prospectus. We have committed to continuous improvement in the frequency of our disclosures so from this year we are switching to quarterly reporting.”

SIGNIFICANT OUTLAY

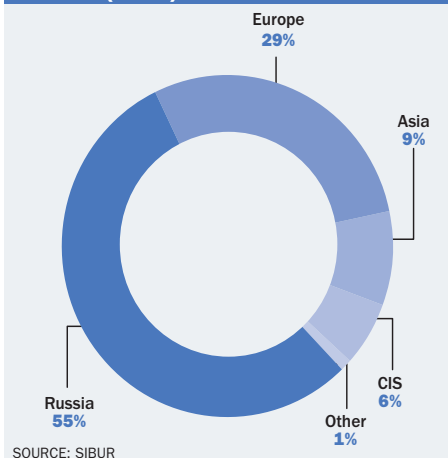
Almost Rb200bn have been invested over the past four years across the feedstocks & energy and petrochemicals divisions, with the capital expenditures (capex) plan already approved at board level for the next four years.

Malvi notes that the main changes this year will come from organic development, notably the flagship polymer project in Tobolsk. The full impact of its financial performance will be seen in next year's results, he adds.

“SIBUR has a good pipeline of organic growth projects, and these will have the main effect on our business growth,” he says.

Besides Tobolsk-Polymer, a new liquefied petroleum gases (LPG) and light oil products transshipment facility in the port of Ust-Luga is also scheduled for completion in 2013 and will support growth in LPG exports to the pre-

REVENUE BREAKDOWN BY REGION (2012)



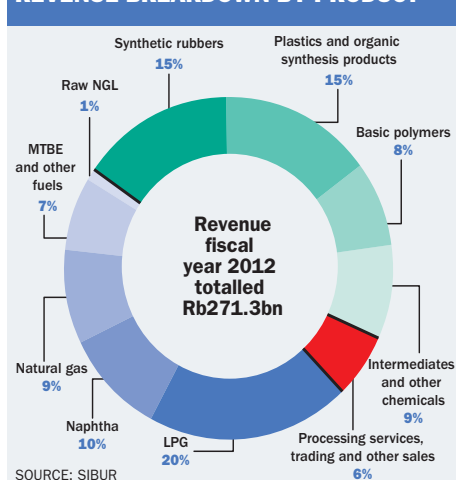
mium western European markets. It is expected to come on stream in the third quarter.

“This will also have significant potential for the shipment of naphtha and underpin further profitability of our feedstock export operation,” he says.

Later this year, SIBUR hopes to make a decision on whether to proceed with an integrated polyethylene (PE) and polypropylene (PP) production complex in Tobolsk. The ZapSib-Neftekhim project – known as ZapSib-2, is now at the front end engineering (FEED) phase, with works being carried out by engineering group Linde, TECHNIP and ThyssenKrupp Uhde.

The project would be the largest integrated facility for production of basic polymers in Russia and include a 1.5m tonne/year ethylene cracker, with 1.5m tonnes/year of downstream

REVENUE BREAKDOWN BY PRODUCT



PE and 500,000 tonnes/year of PP. It will include an 800,000 tonne/year swing linear low density polyethylene (LLDPE) and high-density polyethylene (HDPE) plant, plus 700,000 tonnes/year of HDPE. Fed by ethane and LPG from its own gas processing plants, it is expected to be more competitive with feedstock prices than the US is with its shale-based ethane prices.

There are several other equally important but lower-profile developments such as improvements in the production of polyethylene terephthalate (PET) and new expandable polystyrene (EPS) capacity, he says.

“You can expect very bold strategic development plans from SIBUR. We are trying to use all available financial instruments, some of which may not have been used in Russia before,” says Malvi. ■

EXPANSION

DOMESTIC MARKET KEY TO PLASTICS AND ORGANIC SYNTHESIS DIVISION

FOR SIBUR's plastics and organic synthesis division, the key objectives are to maintain a leading market position, boost production and expand its portfolio, says managing director Sergey Merzlyakov.

“We've seen no real changes to our priorities since the start of the global crisis in 2008 but have perhaps just intensified our efforts,” he says. “We've always treated cost-cutting initiatives, head count, optimisation issues and energy efficiency seriously.”

Over the past year, the business has been particularly active in expanding its range of biaxially-oriented polypropylene (BOPP) films, acrylates and plastics, as well as introducing a new expandable polystyrene (EPS) grade and marketing its geosynthetic products – innovations that can, for



Sergey Merzlyakov, managing director, head of plastics and organic synthesis division

example, help to improve the quality of roads and infrastructure.

“Besides BOPP, the main focus for our products is domestically. Our strategy is to produce polymers and organic synthesis products to meet domestic consumption through im-

port substitution,” he adds.

The business already holds a leading position in Russia and will continue to target local markets for its core products.

“BOPP is the only market where we're planning exports in 2014 because overproduction is expected. It is a much more profitable product and we have a strong competitive advantage that will help us grow our business.”

BOPP demand growth stands at around 3-5%/year globally, although this is as high as 10% in Russia, says Merzlyakov.

Among its planned projects, SIBUR is increasing the capacity of its PET facility in Blagoveshchensk, Bashkortostan region, to 210,000 tonnes/year. This year, the division is also expecting to complete two

restructuring projects in Tomsk of 38,000 tonnes/year and 30,500 tonnes/year in Novokubyshevsk (Samara Region) for the conversion of polypropylene (PP) to BOPP film.

SIBUR also recently launched a new 100,000 tonne/year facility for a new grade of EPS based on Sunpor (Austria) technology.

With demand also growing for surfactants in the CIS at than 6%/year, a letter of intent has been signed with Solvay to establish a surfactants joint venture called RusPav, located in Dzerzhinsk. SIBUR will contribute its raw materials, production and logistics capabilities to the joint venture. RusPav will be located near SIBUR's petrochemicals operations, 400km east of Moscow, and is tentatively expected to be operational in 2016. ■

Global ambitions

Although domestic markets remain central to SIBUR's strategy, it is keen to expand its global footprint too

SIBUR's synthetic rubbers division may have borne the brunt of difficult conditions these past few years but the business is working to minimise the impact of economic and market cycles. Whereas strengthening domestically is key to the company's overall strategy, managing director Mikhail Gordin is leading the synthetic rubbers division into key foreign markets through new joint ventures.

"India and China are places where we are leveraging our technology. We haven't had a lot of experience in international development – but this is a great way to get into these new markets," says Gordin. "We see no real volumetric growth in Russia; in terms of global rubber production, Russia has about a 10% share¹ – and more than half of that is exported. Our strategy is therefore to grow our margins there and increase volumes in fast-growing markets, such as India and China, by licensing our technology."

India's chemicals industry continues to boast rapid growth, with GDP projected to grow by 5.7% in 2013, according to the International Monetary Forum's latest World Economic Outlook report.

With the automotive sector particularly strong, SIBUR has formed a joint venture with India's Reliance Industries to tap into the country's thriving rubber industry.

SIBUR first announced plans to develop a 100,000 tonne/year butyl rubber site with Reliance in May 2010. The joint venture, called Reliance Sibur Elastomers Private Limited, will be located at Jamnagar in India's western Gujarat state and is already in the advanced stages of engineering. Construction is tentatively due for completion in 2015. This will be India's first butyl rubber manufacturing facility. Reliance will hold 74.9% in the venture, with SIBUR holding the remaining 25.1%.

"We've implemented the JV in India with Reliance to produce butyl rubber and SIBUR will play a technology partner role. It's a great opportunity for us to license our technology in a fast-growing marketplace where we ben-



Deals with leading international players are important for growth

efit from feedstock supplied by their refinery," says Gordin. "Reliance is a big company but relatively new to rubber, producing relatively simple grades. Butyl rubber is a highly sophisticated technology."

FORMING PARTNERSHIPS

There are countless hurdles to moving into a new territory but many of these can be overcome through close cooperation with a local partner. Reliance, with its worldscale capacity, infrastructure, and marketing experience, is helping to minimise the complexity of the project, he adds.

China is another notoriously difficult market to break into but forming a partnership with one of the world's major producers is helping to ease the process too.

Last year SIBUR discussed plans to form two possible joint ventures with China's Sinopec for the production of synthetic rubber. The first of these is now well underway and can possibly see the expansion of SIBUR's existing nitrile rubber (NBR) capacity in Krasnoyarsk, Russia, by 14,000 tonnes/year to 56,000 tonnes/year, if there is a decision.

"There are many benefits of using the existing plant and China is already a major customer," says Gordin. "We believe it will be better to have a major Chinese partner to make use of their marketing expertise and use their sales channels. It's a good partnership and could lead to other agreements."

The second joint venture is still in the early discussion stages but if given the go ahead could see another plant established to manufacture nitrile rubber (NBR) and isoprene rubber (IR) in Shanghai, China. If approved following feasibility studies, each plant would have an annual capacity of 50,000 tonnes. The joint venture will use SIBUR's patents and technologies.

"Sinopec is an international leader in synthetic rubber production but we're working with them on products they don't already have in their portfolio," says Gordin. "Our cooperation would be as a technology partner, with a share in the production facility in China and the ability to market product there. However, this is still under discussion." ■

FOOTNOTES:

¹ IISRP



SIBUR has more than doubled its gas processing capacities over the past few years

Feedstock position fuels growth

SIBUR's unique feedstock position has helped secure its place among the leading producers in Russia, CIS and eastern Europe

It is testament to the strength of SIBUR's business model that the Russian producer has seen such significant growth in its relatively brief history. Besides being a leading petrochemical producer, SIBUR has positioned itself as Russia's largest gas processor with unique facilities and infrastructure.

Its feedstock & energy segment has seven production sites, gathering and processing associated petroleum gas (APG): transporting, fractionation and other processing of natural

gas liquids (NGLs), and marketing and sales of energy products, such as natural gas, liquefied petroleum gases (LPG), naphtha, raw NGL, methyl tertiary butyl ether (MTBE) and other fuels and fuel additives.

The division is central to SIBUR's long-term vision, says managing director, head of hydrocarbon feedstock division, Konstantin Belkin, and has not only ensured its resilience in difficult economic conditions but is also important for the company's future growth. The group uses these materials as feedstocks for its

petrochemical business and also sells them as energy products both domestically and internationally. Sales are split almost equally between domestic sales and exports.

This advantaged feedstock position has cushioned SIBUR from the global economic downturn and allowed the business to remain highly competitive despite extreme pricing volatility, adds Belkin.

"Prices for the majority of the company's feedstock and processed goods are linked to oil or oil derivative values. As SIBUR is using

its own feedstock, the fall of oil prices decreases the revenue from external sales of feedstock products but at the same time makes producing our petrochemicals cheaper. A decrease in oil and oil derivatives prices may affect SIBUR's results of operations; an increase in feedstock prices may result in increased operating expenses," he says.

"Growth in prices for oil or oil derivatives generally has a net positive effect on our financial results because our position as a net seller of energy products allows us to mitigate the negative effect that growth in oil and oil derivative prices has on our cost base," adds Belkin.

Crude oil prices can affect the price of raw NGL, LPG and naphtha bought from third parties as feedstock but SIBUR also produces these to sell or process into petrochemical products. External sales of raw NGL, LPG and naphtha accounted for 31.1% and 30.5% of total revenue in 2012 and 2011, respectively.

STRONG STRATEGY

SIBUR is the owner and operator of the largest gas processing business in terms of APG processing volumes and boasts the most extensive integrated infrastructure for processing and transportation of APG and NGLs in the country.

By tapping into the rich resources of Western Siberia – the largest oil- and gas-producing region with 48bn bbl of proven oil reserves and 22tr cubic metres of gas reserves – it has developed seven of the nine Russian gas processing plants (GPPs), as well as five compressor stations and three gas fractionation units (GFUs).

Not only has the company been able to double its gas processing capacities in recent years but it has also been able to expand its pipeline infrastructure and invest in numerous projects to improve capacity utilisation and efficiency, says Belkin.

He notes that the division's core strategy is to secure access to feedstock through the expansion of existing APG and NGL processing and transportation infrastructure, as well as arranging long-term contracts with oil and gas companies. Another priority, he says, is to monetise stranded feedstock through the construction of large-scale petrochemicals facilities.

SIBUR's unique position along the value chain provides many distinct advantages over its competitors, he says. Despite the challenging market conditions, SIBUR continues to make good progress with its key objectives and securing its primary hydrocarbon feedstock streams. For both APG and NGL feedstocks, over 70% of supplies are now guaranteed through long-term contract arrangements with oil and gas companies. The average maturity for these arrangements now exceeds 11 years for APG and 12.5 years for NGLs.



"Growth in prices for oil or oil derivatives has a net positive effect on our financial results"

KONSTANTIN BELKIN

Managing director, head of hydrocarbon feedstock division

SECURE SUPPLIES

According to information service, CDU TEK, the total Russian output of APG reached 71.81bn cubic metres in 2012, up from 68.52bn in 2011 with an annual growth rate of 5% – above the 2.9% average annual growth rate during the period between 2005 and 2011.

The oil fields in Western Siberia are mature and unlikely to see any significant increase in APG volumes, while it is anticipated that the concentration of liquid fractions in APG may fall in the future. Nevertheless, SIBUR expects this trend to be partly offset by increased efforts to reduce flaring to comply with new government regulations. This stipulates that both the utilization rate of APG and volumes flared should be significantly lower.

According to official statistics, the total volume of flared APG in Russia totalled 17.08bn cubic metres in 2012 – 44% of which was seen in Western Siberia, in fact double this figure at 37.4bn cubic metres.

As the new rules are introduced, higher volumes of APG will become available creating the potential for sustained growth of APG volumes available for processing. IHS CERA estimates total flared volumes will be reduced to 10.4bn cubic metres by 2015 and to 3.2bn cubic metres by 2020. This poses significant opportunities for SIBUR, says Belkin.

CONTINUED INVESTMENT

A key growth driver in the feedstock & energy division is increasing efficiency – either

through improving utilisation rates or NGL extraction, he adds. The modernisation of the Gubkinskiy gas processing plant, for example, saw NGL extraction rates climb from 67% in 2007 to almost 99% in 2012. Currently, six of the seven GPPs extract over 90% of NGLs from associated gas, excluding ethane.

Belkin points out that SIBUR continues to invest heavily in capacity and infrastructure and by the end of 2012, several major projects had been completed.

These included the addition of a third compressor station at its Nizhnevartoskiy facility to increase capacity utilisation, and a recovery unit at its Yuzhno-Balykskiy gas processing plant – bringing its total APG capacity up to 3bn cubic metres/year.

In September 2012, work was also completed on upgrading the Vyngapurovskaya compressor station – a brown-field initiative that resulted in increased processing capacity of 750m cubic metres/year and raised the recovery rate to 99% from 56%.

In addition, SIBUR has invested in a new main NGL pipeline from the Purovsky gas condensate processing plant to Tobolsk-Neftekhim to transfer light hydrocarbons produced in Western Siberia.

The 1,100km pipeline consists of three parts, one stretching from the Purovskiy GCP owned by NOVATEK to the SIBUR's loading rack in Noyabrsk, the second segment continuing to Yuzhno-Balykskaya main pumping station, and the third connecting to Tobolsk production site.

Another key project for the feedstock & energy business includes the Ust-Luga LPG transshipment facility near St Petersburg, which will provide access to northwest European markets (see page 15).

POSITIVE OUTLOOK

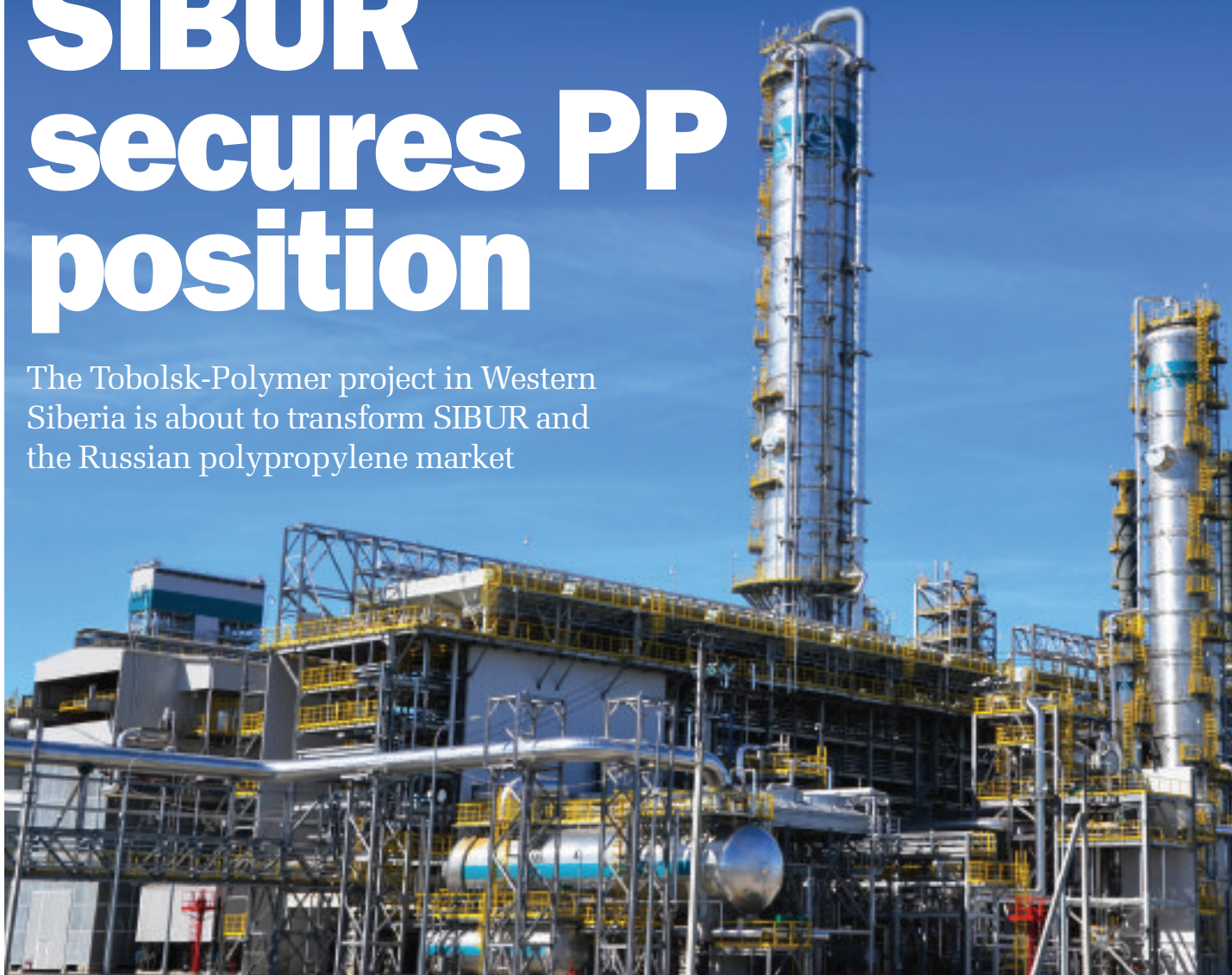
The world is yet to see the full impact of the shale gas revolution and the effects of cheaper ethane supply – a trend that has already contributed to a general decline in the price of natural gas in the US and may drive down prices globally in the future. Although this could reduce prices for gas-based feedstock and intensify competition among producers because of oversupply, Belkin is confident SIBUR will remain robust in the face of market pressure.

The company's performance in recent years has not only helped the group to increase revenues and profitability, but has also allowed it to raise capital expenditure and retain its place at the top of the league tables for EBITDA margins.

There may be challenges ahead for the business but SIBUR's unique and highly advantaged position as an integrated gas processing and petrochemicals company will ensure continued growth and success, he insists. ■

SIBUR secures PP position

The Tobolsk-Polymer project in Western Siberia is about to transform SIBUR and the Russian polypropylene market



There has never been a petrochemical project of this size and scale before in Russia

A small northern Russian city with a population of only 100,000, 300km from the nearest airport, has been a flurry of activity for the past three years – thanks to the 6,000 workers building a vast petrochemicals facility there.

SIBUR's flagship Tobolsk-Polymer project is set to revolutionize the company's polypropylene (PP) production, doubling its output and positioning the Russian major as one of the world's leading players, says Mikhail Karisalov, deputy chairman of the management board – executive director. Its completion means the country can substitute imports of basic PP grades and become an exporter.

Western Europe is set to move from a state of oversupply for PP in 2012 (384,000 tonnes/year) to a deficit of 1.7m tonnes/year by the end of the decade, according to IHS Chemical.

To complement the existing gas fractiona-

tion and butadiene (BD), isobutylene and methyl tertiary butyl ether (MTBE) facilities this site is now home to another two plants – a propane dehydrogenation (PDH) plant based on UOP technology and capable of producing 510,000 tonnes/year of propylene, and another that converts the output into 500,000 tonnes/year of homopolymer PP. This uses technology from UK-based INEOS.

The greenfield project required new infrastructure including utilities, electricity, cabling, water and steam pipelines in addition to the existing facilities of Tobolsk-Neftekhim. Construction and pre-commissioning is now complete.

"The plant is fully integrated into the feedstock chain and will help Russia to become a totally new petrochemical player globally," says Karisalov. "This project has been a major challenge – with the construction industry

specifically – because a lot of competences have been lost since the end of the Soviet Era. Everything had to be learnt anew.

"Everything will change dramatically when our project fully comes onstream. There will be totally new markets and new capacity available to us. This market is very dynamic and really promising – we do believe it has bright prospects because it's growing very fast on the back of the utility, automotive and consumer industries," he says.

Tobolsk is home to the largest natural gas liquid (NGL) fractionator in the former Soviet Union, the 3.8m tonne/year unit connected via a pipeline grid to gas processing plants in Western Siberia, adds Sergey Komyshevan, managing director of the basic polymers division.

"Historically, it's a well developed petrochemical site and that was the basis of our decision to install our project there. The market

situation is significantly more favourable for polypropylene than for ethylene derivatives such as polyethylene (PE)," he says.

"We see very good demand in Russia and CIS and notice trends in Europe where over-supply is gradually changing to a deficit – we believe this will continue for years to come. We also see a deficit in China for PP, so someone has to fill in the gap. Building a facility in Tobolsk made sense because the cost of transporting resin is significantly less on a per tonne basis than that of light hydrocarbons, which requires special railcars and safety provisions," adds Komyshan.

Transportation costs are expected to be comparable to those from Middle East, US and Asian producers, with a replenishment lead time of around 4-5 weeks. About 70 grades are expected to be available after the plant's start-up.

"Our cost position will be that of an integrated player – based on competitive cost of hydrocarbons in western Siberia. Tobolsk-Polymer should be able to find itself in the first quartile in terms of competitiveness," he points out.

INTERNATIONAL DIPLOMACY

Companies from seven countries were involved in the mammoth task, including licensors from the US and the UK, designers from Italy and Germany, as well as manufacturers from Russia, South Korea and Japan.

Managing the different languages, mentalities, cultures and working practices, as well as dealing with various time zones and moving equipment over huge distances certainly posed a few challenges, notes Karisalov.

"In Russia, there has never been a similar petrochemical project that included two huge production integrated facilities. We've seen some major greenfield facilities but we've never had any of a global scale with this level of capacity," he says.

"Such large scale construction only started to emerge in Russia a few years ago. There were no competencies, policies or standards so we had to act almost as a cocktail shaker and mix all the required elements in strict proportions. It was a delicate mix of dozens of ingredients. We've been ready and willing to learn and get the necessary experience for this project."

SIBUR appointed several leading licensors and contractors to assist with the ambitious plans. UOP – a specialist in processes and technologies for the dehydrogenation of light alkanes – was joined by INEOS with its Innovene polymerisation technology. Tecnimont was also approached based on its skills and track record with similar large-scale projects globally.

"Our licensors UOP and Tecnimont shared knowledge with us in terms of similar projects and their experience really helped a lot to properly structure and plan all the operations and works," he says. "More than 100 of our staff from Tobolsk were trained at production



"Everything will change dramatically when our project fully comes on stream. There will be totally new markets and new capacity available to us"

MIKHAIL KARISALOV

Deputy chairman of the management board – executive director

sites for two weeks in the US, Thailand and Saudi Arabia. The conclusions we have drawn from this experience is that there will be no hurry, no compromises, and no actions aimed at saving time for the sake of quality."

This was Linde Engineering's biggest engineering procurement and construction (EPC) project as a general contractor, and the sheer scale of the task posed a few difficulties.

With several thousand staff onsite, as well as more than 100 people in Dresden, Germany, and its Indian office, careful management was essential, says Jörg Linsenmaier, managing director, Linde Engineering Dresden. An integrated team was established with SIBUR to control the overall construction site, and proved extremely effective.

"This is a very big site which has to be managed very precisely and very well. There is a lot of planning involved. I think that we have found a very good way of working with SIBUR and overcoming problems because we are openly discussing those; I think we have managed to resolve problems together quite well," he says.

With low temperatures from -35-40°C, the windows for ships to sail to the small port through the Northern Rivers were extremely tight, sometimes lasting just a few weeks.

Ferruccio Tatanardini, project manager at Tecnimont, was involved in the engineering,

procurement and construction of the high capacity PDH unit.

"This kind of project takes two or three years to complete. We had more or less 3,000 people working day and night. The big challenge was to bring the materials to Tobolsk due to the fact that most of the equipment was oversized. The only chance to move the equipment was through the river in the north of Russia and this is not frozen for only 20 days of the year. You have to take into consideration that starting from November, up to March, the temperature in Tobolsk is -25°C, so the difficulties working in these conditions are evident," he says.

Despite the difficulties getting the cargo vessels through the waterway and unloading them, 11 shipments and 23 pieces of large-sized heavy equipment were successfully delivered for the plant's construction. In 2010 alone, more than 650 containers, 100 rail cars and 470 trailers arrived safely onsite.

To accommodate some of the oversized deliveries, dredging work was needed at the river port to cope with the demands. One column for the propane dehydrogenation (PDH) facility weighed 1,096 tonnes and measured 10 metres in diameter and 100 metres in length. It was shipped from South Korea through the Panama Canal to Arkhangelsk, before being loaded onto a barge to the Irtysh river.

OUTREACH PROGRAM

Support from the local administration far exceeded SIBUR's expectations, helped by early discussions with the regional governor to outline the specific plans for the project.

Meetings were arranged at both a local level with the regional governor and with direct support from the Russian government.

The project is transforming the area. It is the first that involves the advance processing of crude hydrocarbon in a region typically associated with extracting crude hydrocarbon. It will also have a significant effect economically as a major taxpayer and will create jobs.

"Regarding the ordinary local people, there are always some unhappy with projects like these, but I personally worked on this project for three years and the overwhelming majority were really positive. The key to success was openness, transparency and our heavy investment in communication," says Karisalov.

"We've run several initiatives to help create a very positive picture – even planting one million young trees in several districts in Tobolsk to create a huge forest. Then there were public hearings, meetings and sessions with local parliament members and public representatives. There were independent environmental experts involved and the publication of the environmental audit reports in the local press. We've also sent public representatives to similar projects globally for them to get familiar with what we're implementing in Tobolsk." ■

PVC ups profile

The RusVinyl joint venture project will help SIBUR to grow its presence in the thriving polyvinyl chloride market

Kstovo, a small town on the bank of the Volga river, 450km east of Moscow, is set to become a key source of polyvinyl chloride (PVC) once SIBUR/SolVin's new plant is completed, as expected, next year.

Costing more than rouble (Rb) 50bn (\$1.54bn, €1.17bn), the RusVinyl complex lies in the Nizhny Novgorod region of Russia and is a 50:50 joint venture with SolVin, itself a 75:25 JV between Belgium-headquartered Solvay and Germany's BASF. Once complete, the country's largest integrated PVC plant will have nameplate capacities of 300,000 tonnes/year of suspension PVC, 30,000 tonnes/year of emulsion PVC and 225,000 tonnes/year of caustic soda. The polymer will be used for various applications, including rigid profiles, pipes, bottles, fittings, cable insulation, flexible films and sheets.

Ethylene, a key monomer used to produce PVC, will be supplied from SIBUR's steam cracker that is being expanded in parallel and lies 0.5km from the RusVinyl site.

Discussions started with Solvay in 2005, the negotiations culminating in the joint venture being agreed in June 2007. Basic engineering was complete in 2008, with the first stone laid in the ground in 2010.

The European Bank for Reconstruction and Development (EBRD) is also lending support to the initiative by contributing one fifth of a €750m financing package. Besides EBRD committing to an 11-year loan worth €150m in roubles, this sum is being matched by Russia's Sberbank. The export credit agencies of France and Belgium – COFACE and ONDD – will pro-

vide insurance cover on the remaining €450m in loans from a group of commercial banks comprising ING, BNP Paribas/Fortis, and HSBC.

"This is a great example of genuine project finance which is very rare in Russia. We're now in the middle of construction and plan to be complete by end 2013, with commissioning in 2014," says Sergey Komyshevan, managing director, head of basic polymers division.

"The novelty of this project for Russia and CIS is that joining forces with SolVin we have brought together outsourcing partners for two significant parts of the project. One is the logistics platform, which has been built on a turn-key basis by Karl Schmidt, for the technical gases we have Air Liquide building and operating the oxygen and nitrogen producing unit," he says.

"In light of these decisions we have now started looking much more carefully and with more interest at these kinds of opportunities. We have introduced them into SIBUR's existing sites and will consider them for future projects. I have to admit we've learnt a lot while structuring and executing this project and plan to use these ideas in other parts of our organisation," notes Komyshevan.

Last year, PVC consumption in Russia and CIS exceeded 1.4m tonnes, with a growth rate of around 6%. Imports amounted to almost 500,000 tonnes. Emulsion PVC is barely produced in Russia and imports account for about 90% of the 170,000 tonnes consumption.¹

"Market research² suggests the PVC market in Russia and CIS will continue growing at a rate of 5-6%/year from 2012-2020, mainly driven by the construction industry," he says. "We believe we will sell all the PVC within



"We've learnt a lot while structuring and executing this project and plan to use these ideas in other parts of our organisation"

SERGEY KOMYSHEVAN

Managing director, head of basic polymers division

Russia for domestic use and there will be no need to tap into export markets."

Komyshevan sees plenty of potential for the new venture. PVC consumption per capita in Russia is still rather low at around 8kg/head whereas in Europe this is closer to 12kg,³ so there is certainly room for increased uptake, he says.

Conversely, the situation with caustic soda is a little different. The market was reasonably balanced in 2012 with demand growth relatively modest at about 2%/year.⁴ Sluggish demand in Europe resulted in several shutdowns and a decline in capacity utilisation of electrolysis units in the region – which in itself poses opportunities for the new venture. Some of the output may be exported but most of the caustic soda will remain in Russia, he says.

Even after the capacity comes on stream, it will not cover the deficit in the PVC market and some tonnage will still be imported. Komyshevan points out that the designs therefore include an option to increase capacity in the future.

"If the market permits, and we achieve our marketing targets, then together with our partner we'll look at the situation. The logistics platform and facilities will support the expansion," he says. ■



RusVinyl is a great example of genuine project finance

FOOTNOTES:

^{1,3} CMAI; ² CMAI, Alliance-Analytics; ⁴ Alliance-Analytics

Launch pad for LPG

A major new seaport being developed in Russia will allow SIBUR to target northern and western European markets with its surplus LPG

Russia's liquefied petroleum gas (LPG) production is growing rapidly, with forecasts suggesting it will total 16.4m tonnes/year by 2015, up from 9.7m tonnes/year in 2010.

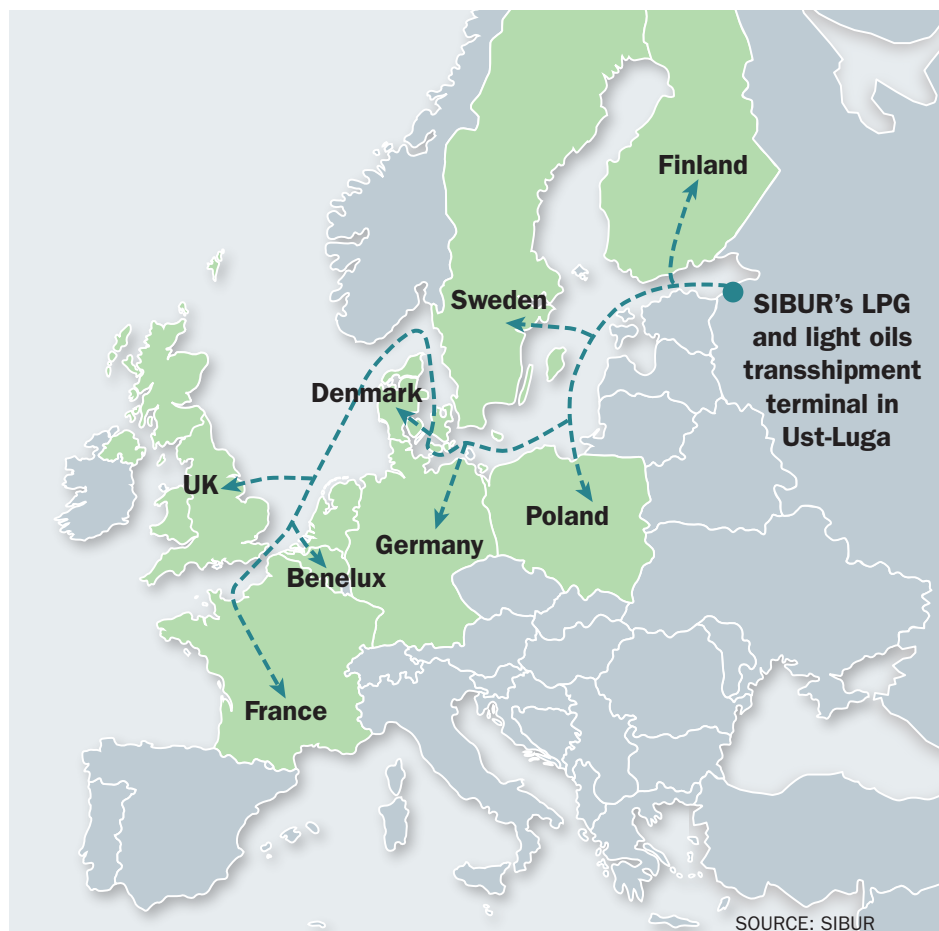
Although most of the output will be supplied to the domestic market as a feedstock and fuel to the thriving utility sector, there is still likely to be an excess in supply in the coming years because of insufficient growth in the petrochemical market. Consultancy Nexant forecasts global LPG production growth at an average of 2.4%/year from 2011-2020, climbing to 312m tonnes/year by the end of the decade. Russian LPG consumption is expected to grow at around 2.8%/year through to 2020 with production expected to grow at an average rate of 2.7%/year over the same period. With such intensive production growth expected, SIBUR decided to pledge significant investment into developing extensive export infrastructure.

SIBUR is Russia's leading producer of LPG with 34% of the domestic market. In 2012, the company processed 18.7bn cubic metres of associated petroleum gas (APG).

Its decision to invest in a 138 hectare (341 acre) transshipment complex, located at the Ust-Luga commercial seaport in the Lenin-grad Region in the northwest of Russia, means SIBUR will now be able to tap into new routes and markets, and ship LPG cargoes throughout northwest Europe.

The company signed a memorandum with Ust-Luga Company for the construction of the terminal in 2007 and local authorities approved the plans. In June that year, SIBUR established SIBUR-Portenergo, the operator of the LPG export terminal.

Ust-Luga is a multipurpose seaport on the border of Russia and the EU, in the Gulf of Finland, with direct access to northwest Europe. It boasts the largest LPG tank storage capacities in Russia and the Commonwealth of Independent States (CIS) and is also the only terminal in the region with refrigerated LPG tanks. It



UST-LUGA DATA

- Area - 138 hectares (341 acres)
- Transshipment capacity – 4m tonnes/year
- High pressure LPG – 380,000 tonnes/year
- Refrigerated LPG – 1.07m tonnes/year
- High pressure LPG tank storage capacity – 10,000 cubic metres (5,610 tonnes)
- Refrigerated LPG tank storage capacity – 40,000 cubic metres (23,640 tonnes)
- Transshipment capacity – 4m tonnes/year
- Light oils tank storage capacity – 100,000 cubic metres (68,800 tonnes)
- Rail-road pier for LPG unloading for up to 84 rail tank cars (RTC)
- Rail-road pier for light oils unloading of up to 72 RTC

also has the advantage of year-round operation, with shipments not restricted by ice.

The project required significant dredging work in the mooring area, removing soil to increase the water depth from 1.6-4.5 metres to 13.5 metres. The terminal will be able to accommodate ships, gas carriers and tankers up to 185 metres in length, with an overall deadweight of up to 48,000 tonnes.

The terminal will feature an isothermal LPG storage, says SIBUR. The cooling of the

liquefied gases will allow bulk transportation since cargo capacity of a refrigerated LPG carrier is comparable to the capacity of as many as 10 conventional pressure-type gas carriers.

It is also well supported in terms of infrastructure, with railway access, full transshipment facilities, an onsite laboratory and customs.

The first LPG carriers arrived in late June. The complex is designed to handle up to 1.5m tonnes/year of LPG and 2.5m tonnes/year of light oils. ■



Head office
16/1 Krzhizhanovskogo St.
Moscow, GSP-7, 117997, Russia
Tel/fax: +7 495 777 5500

SIBUR International GmbH
Moscow Office
 18/4 Krzhizhanovskogo St.
 Moscow, 117997, Russia
 Anti-fraud and business abuse
 mailbox
 Email: compliance@sibur-int.com
 Secretary
 Tel: +7 495 974 7458
 Email: office@sibur-int.com

Shanghai Office
 Jinmao Tower, Room 2508B
 Century Ave.88,
 Pudong New Area,
 Shanghai, 200121, China
 Tel: +86 21 5098 8933

Vienna Office
 Nussdorfer Platz 8,
 1190 Vienna, Austria
 Tel.: +43 1 370 8000
 Fax: +43 1 370 8000 20
 E-mail: office@sibur-int.com
www.sibur-int.com

SIBUR's Representative Office,
China
 Suite #2504, Tower D, Central
 International Trade Center,
 6A Jianguomenwai Avenue, Chaoyang
 District, Beijing, 100022, China
 Tel: +86 10 8567 9790/8567 9793
 Fax: +86 10 8567 9792
 E-mail: sibur_china@yahoo.com.cn
www.siburchina.cn

WOC SIBUR Petrochemical India
 Private Limited
 Level 9, Platina
 Suite 911 & 912

C- 59, G Block
 Bandra Kurla Complex
 Bandra (e)
 Mumbai 400051, India
 Tel: +91 22 6700 0648
 +91 22 6700 0649

Media Centre
 Anna Lebed>Lastukhina
 International Media Relations
 Tel: +7 495 937 1726
 Mob: +7 926 754 0851
 E-mail: lebedai@sibur.ru

Investor Relations
 Anna Kareva
 Director, Investor Relations
 Tel: +7 495 777 55 00 (ext 3420)
 E-mail: karevaa@sibur.ru
sibur_ir@sibur.ru

Export Department
 Polymers
 Email: export.p@sibur.ru
 Products of Organic Synthesis
 Email: export.o@sibur.ru
 Synthetic Rubbers
 Email: export.sr@sibur.ru