

OIL AND GAS SECTOR

1.00

WHITE BOOK BALANCE SCORE CARD

Recommendations:	Introduced in the WB:	Significant progress	Certain progress	No progress
Introducing the marking of marine fuel sold to vessels in the domestic water transport.	2021			√
Reintroducing excise refund for marine fuel used in the domestic water transport.	2021			√
Applying a general VAT rate of 20% on CNG consumption, as well as an adequate level of excise taxation, in order to eliminate the effects of CNG's preferential status in relation to other motor fuels.	2021			√
Reducing the level of excise taxation for LPG in order to increase the consumption of this petroleum product.	2021			√
Concluding bilateral agreements on carriers' eligibility for VAT refund on fuel purchased in Serbia with Bulgaria, Turkey, Greece, North Macedonia and Montenegro, as well as with other countries from which trucks use Serbia as a transit country.	2021			√

CURRENT SITUATION

In 2021, the upward trend in the price of crude oil continues, as a result of the reduction of the negative effects of the COVID-19 epidemic and the acceleration of economic activities at the global level. The price of Brent crude oil recorded an upward trend in 2021, stimulated by the wider usage of vaccines, and therefore increased demand for petroleum products due to the lifting of emergency measures and movement restrictions, and reached its maximum of 85.53 USD/bbl in October 2021. A slight price drop followed, after which the price continued to rise, especially rapidly since the beginning of the conflict in Ukraine, reaching 127.98 USD/bbl at the beginning of March and 122,01 USD/bbl at the beginning of June 2022. The average price in 2021 was 70.68 USD/bbl, which is 28.72 USD/bbl or 68% higher than the average price in 2020. The average price of Brent crude oil for the first 6 months of 2022 is 107.9 USD/bbl, which is 53% more than the average for 2021 and 2.5 times higher than the price in 2020.

The global increase in oil prices also affected the domestic market. The energy crisis in the world as well as the global disruption in the market of petroleum products resulted in the adoption of the Regulation on limiting the price of petroleum products (Regulation) by the Government of the Republic of Serbia on February 10th of 2022, in order to prevent major disruptions in that market and preserve the living standard freezing petroleum and diesel prices. From March 11, the implementation of the Rulebook on the Calculation of the Average Wholesale Price of Oil

Derivatives Euro diesel and Euro premium BMB 95 came into force and the Regulation was amended, that stipulated that the price of petroleum products is adjusted on a weekly basis. It is important to note that because of price limitations, sales of petroleum products in border areas have increased, taking into account that prices in most countries in the surrounding area are higher than in the Republic of Serbia, which was the opposite trend in the previous period. In addition, due to limiting of the price of euro diesel for farmsteads at RSD 179 per liter at gas stations in accordance with the adopted Regulation, which is significantly below the prescribed retail prices, a high growth in the consumption of this petroleum product by farmers in 2022 was noticeable in comparison to the previous period, consequently questioning whether derivatives for agriculture were purposely used. Since no control has been established as to whether diesel fuel is actually used for agricultural purposes, and in the first two months there was no purchases restriction, there are indications on the market of inappropriate use of the preferential price for agricultural holdings, which also calls into question the adequacy of the implementing mechanisms for the preferential price for agricultural holdings.

In addition to limiting the prices of petroleum products, the Government of the Republic of Serbia also passed a Decision on the temporary reduction of excise duties on petroleum products in order to further reduce of the price of petroleum products in the country. The Decision first reduced excise taxes by 20%, and the reduction percentage in certain periods was -15 and -10%. The last measure

that was adopted was the ban on the export of Eurodiesel, which increased the available quantities on the domestic market by about 30,000 t per month.

During 2022, on several occasions, prices were determined by the Regulation that did not cover import costs, so that in May, imports were lower by about 53% than in May last year, in June by as much as 70% and in July by 64% compared to the same month in 2021. The imported goods availability was also affected by the measures taken by the governments of the countries in the region from which most of the imports arrive in Serbia under normal circumstances, as well as planned and unplanned overhauls of refineries, logistical restrictions, the low water level of the Danube, but also the rationalization of the quantities of importers who imports with a negative margin were replaced by a small but guaranteed margin in procurement from the domestic market. We would also point out that the state authorities in Serbia, at the initiative of business entities and in order to overcome some of the logistical restrictions, allowed foreign flags ships to Serbian river ports, in order to facilitate the import and transport of petroleum products into the country. All the mentioned factors affected in the supply structure of the market.

Everyone in the distribution chain, from importers, wholesalers, retailers and legal entities consumers, that relied on the import of Euro diesel found themselves in a difficult situation and with more or less success were forced to adapt to the new circumstances. The measure adopted by the Government in order to mitigate the impact of the global energy crisis will last most of the 2022, and given that they have lost their temporary character, they should be adapted as soon as possible to the new business conditions, in order to preserve the structure of the oil and oil derivatives market, so that security of supply is increased.

In addition to this, due to the sudden increase in the price of natural gas, the Regulation on the temporary measure of limiting the price of gas and compensation of the difference in the price of natural gas procured from imports or produced in Serbia in the event of a disruption in the natural gas market was adopted as well.

According to data published by the Energy Agency of the Republic of Serbia, the total consumption of crude oil and intermediates from domestic production, imports and stocks in 2021 stood at 3.945 million tons, which is a

9% increase on 2020. In 2021, about 0.817 million tons of crude oil was produced (20.7% of total consumption), while imports accounted for 3.128 million tons (79.3%).

The total consumption of motor fuels in 2021 was about 2.6 million tons, which is 10.8% more than a year before. In the structure of motor fuel consumption, gasoline accounted for 17.1%, diesels 77.6%, and LPG - 5.3%. Total gasoline consumption has increased by 11.6%, compared to 2020, consumption of Euro diesel increased by 11.9%, while Gas oil 0.1 was withdrawn from the market. The consumption of extra light Euro L Gas oil increased by 21.7%, while the consumption of liquid petroleum gases, including auto gas, decreased by 4.4%.

The annual production of natural gas, delivered to the country's transport distribution system in 2021, totaled 226 million m³, which is 14.7% less than the production in the previous year. In 2021, a total of 3.105 million m³ was available from import, domestic production and underground storage, and 2.853 million m³ of natural gas was consumed, 14.9% more than in 2020. Most of the natural gas was imported from the Russian Federation in the amount of 2.294 million m³, while domestic production of 226 million m³ could meet only 7.9% of the demand.

IMPROVEMENTS

With the adoption of new laws in April 2021 by the National Assembly of the Republic of Serbia (four laws in the field of mining and energy, out of which two were new laws - the Law on the Use of Renewable Energy Sources (RES) and the Law on Energy Efficiency and Rational Use of Energy, and another two laws were amended - the Law on Energy and the Law on Mining and Geological Exploration) a new and improved legal framework was established.

The new legal framework will enable alignment with the EU's key goals in the field of energy and environmental protection, as well as directing Serbia in the direction of decarbonization of the energy sector.

The Law on the Use of Renewable Energy Sources will increase the share of RES in the total energy production, contribute to the preservation of the environment and reduce the costs of citizens.

The Law on Energy Efficiency and Rational Use of Energy regulates energy savings and contributes to the sustaina-

ble use of natural resources.

The Law on Energy ensures the security of energy delivery and supply, while the Law on Mining and Geological Exploration will create conditions for more efficient and sustainable management of Serbia's mineral and other geological resources, as well as conditions for increased investments in geological research and mining.

From the aspect of energy security, conditions have been created for raising of its level through the obligation to form operational reserves and defining the types of petroleum products that certain energy entities should hold.

REMAINING ISSUES

The price regulation of trade in oil derivatives in 2022 has led to a significant decrease in the profitability of importers and wholesalers of oil derivatives, dependent on imports, as well as retailers, especially in companies with a small number of gas stations. Consequently, price control in the long term reduces investment attractiveness in the oil and gas sector in the Republic of Serbia, and may lead to the gas stations number decrease.

Intensive controls are continuously carried out to stop illegal trading in petroleum products in the country. It is necessary to keep them in order to prevent a reduction in the volume of the grey economy. Accordingly, additional supervision is needed regarding marine fuel supply to vessels in the domestic traffic.

The high level of excise duties on liquefied petroleum gas (LPG), which is among the highest in the region, discourages

the use of this environmentally friendly petroleum product, resulting in a continuous drop in annual consumption.

Conversely, the lack of excise duties and a lower tax rate of 10% for trading in compressed petroleum gas (CNG) makes it more competitive compared to other motor fuels.

In the international passenger and road freight transport, fuel is not purchased in Serbia, while on the other hand there is an increasing number of domestic carriers that buy fuel outside of Serbia due to a more favorable tax policy in the countries of the region.

Systematic control of imported petroleum products for re-export has not been established yet.

New regulations on the production and trade of explosives and other dangerous substances have not been adopted yet.

Due to the significantly lower price of euro diesel for farmsteads and the consequent increase in sales, and bearing in mind that there is no quantitative limit for purchases by farmers, as was the case in the system of subsidizing the purchase of fuel for agricultural production in previous years, the possibility opens up for non-purpose procurement and use of euro diesel.

Restrictions on the retail prices of oil derivatives, primarily during the 2nd quarter of 2022 when prices were at below reference international markets levels, as well as price fixing for agricultural holdings at levels far below market levels, led to a decline in the competitiveness of a part of oil companies in certain business segments, which resulted in significant changes in the market shares of oil companies.

FIC RECOMMENDATIONS

- Repeal the Regulation on the limitation of the price of oil derivatives.
- Introducing the marking of marine fuel sold to vessels in the domestic water transport.
- Reintroducing excise refund for marine fuel used in the domestic water transport.
- Reducing the level of excise taxation for LPG in order to increase the consumption of this petroleum product.

- Applying a general VAT rate of 20% on CNG consumption, as well as an adequate level of excise taxation, in order to eliminate the effects of CNG's preferential status in relation to other motor fuels.
- Concluding bilateral agreements on carriers' eligibility for VAT refund on fuel purchased in Serbia with Bulgaria, Turkey, Greece, North Macedonia and Montenegro, as well as with other countries from which trucks use Serbia as a transit country.
- Improve the system of support by state authorities to farmsteads in the procurement of petroleum products through the re-establishment of the system of subsidies for the procurement of petroleum products per hectare, with database improvement. The support system should be determined on market principles through discussion with the participation of interested competent state authorities, representatives of agricultural holdings as well as oil companies, all with the aim of finding an adequate solution for all stakeholders.