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INTER-AMERICAN DIALOGUE'S
LATIN AMERICA ADVISOR ▶ ENERGY

FEATURED Q&A

Will the Argentine Government Hinder Shale Investment?

Q In recent weeks, the Argentine government has faced off with the country's largest energy company, Repsol's YPF, blaming the increase in fuel imports on a lack of investment from YPF and other producers. Despite a previously good relationship, the government has threatened to nationalize YPF and banned it from exporting until a tax was paid, while the company has blocked politicians from its board meeting. Meanwhile, on Feb. 24, Argentine provinces demanded that energy firms raise their oil and natural gas output by 15 percent in the next two years or risk losing their concessions. Does the Argentine government's contentious relationship with YPF and other oil companies threaten investment in the recent shale gas discoveries, which analysts have called a "game changer" for the country? How will the relationship between the government and oil producers continue to play out? What is to blame for "under-investment" in the oil and gas sector?

A David Richardson, Latin America upstream research analyst at Wood Mackenzie: "The Argentine government's contentious relationship with YPF is unlikely to affect the current evaluation of the of the Vaca Muerta shale in the Neuquén Basin. Some recent entrants to the basin such as ExxonMobil and EOG Resources are already committed to investing in the shale assets within their portfolios. Other shale players such as Apache and Total have held positions in Argentina for a number of years and have the experience of dealing with the political uncertainty. Given the world class potential of the Vaca Muerta shale, these companies will continue with their current evaluation programs and are unlikely to want to give up their positions. Some of the recent changes to the government's energy policy, however, are likely to make poten-

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Mexico May Face Stagnant Oil Production for 14 Years

Mexican oil production will likely stagnate at 2.8 million barrels per day for 14 years unless state-run oil company Pemex increases its investment, the country's energy ministry, headed by Jordy Herrera, said Wednesday. See story on page 2.

File Photo: Mexican Government.

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ENERGY SECTOR BRIEFS

Bolivia's Evo Morales May Expropriate More Oil Companies

Bolivian President Evo Morales may seize additional oil companies if they do not meet investment expectations, Bloomberg News reported Wednesday, citing Bolivian daily *La Razón*. Last month, Morales took over **Pan American Energy**'s stake in the $1.6 billion Caipipendi natural-gas project. "[Oil] companies that are boycotting or sabotaging investment will be repossessed, we now have the capacity to recover shares," said Morales.

Brazil's CPFL Energia to Buy Bons Ventos Wind Farms

São Paulo-based **CPFL Energia** will pay 1.06 billion reais ($620 million) for **Bons Ventos Geradora de Energia**, a Brazilian wind power company, and assume 462 million reais of debt, Reuters reported Sunday. CPFL is one of the largest non-government electricity utilities and its purchase of Bons Ventos includes four wind farms with a capacity of 157.5 MW in the northeastern state of Ceará. The projects will become part of CPFL's renewable energy unit, Ersa.

International Arbitration Tribunal to Hear Chevron-Ecuador Case

A panel set up through the Permanent Court of Arbitration (PCA) at The Hague said Tuesday that it would hear **Chevron**'s case against Ecuador which alleges that the Andean nation violated treaties and international law, Dow Jones reported. PCA decided that it has jurisdiction in the case and will now rule on whether an agreement between Ecuador and **Texaco**, which Chevron acquired in 2001, shields Chevron from liability. According to legal experts, a final ruling could take more than a year.

Oil Sector News

Mexico May Face Stagnant Oil Production for 14 Years

Mexican oil production will likely stagnate at 2.8 million barrels per day for 14 years unless state-run oil company **Pemex** increases its investment, the country's energy ministry said Wednesday. Currently the world's seventh-largest oil producer, Mexico is faced with the possibility of becoming a net importer of oil within a decade as demand for energy increases. Mexico has a current oil output of 2.55 million barrels per day as the country has stabilized plunging production at aging oil fields, including the Cantarell field. However, Pemex has had difficulty in replacing declining output with new discoveries. Cantarell's production is expected to fall from this year's 444,000 barrels per day to 150,000 barrels per day by 2026, the Energy Ministry's report said, according to Reuters. Amid declining output from Cantarell, Ku-Maloob-Zaap has become the country's top oil field-producing 847,000 barrels per day this year, 32.5 percent of the country's total oil output. Ku-Maloob-Zaap's production is forecast to peak by 2017 at 933,000 barrels per day and then begin to decline, said the report. Just maintaining Mexico's level of production at about 2.8 million barrels per day for the next 15 years will require 292.33 billion pesos ($22.86 billion) in investments. However, it added that if Mexico were to increase investment by 21 percent, the country would be able to produce 3.35 million barrels per day by 2026. On Monday, Pemex also reported a loss of 23.83 billion pesos ($1.7 billion) in the fourth quarter, an increase from its 23.56 billion peso loss in the same period in 2010, Reuters reported. According to the company, higher taxes and a depreciation of the peso contributed to the widened loss.

Maintaining Mexico's level of production for the next 15 years will require $22.86 billion in investments.

Argentina's Fernández Does Not Indicate YPF Takeover in Speech

Argentine President Cristina Fernández de Kirchner did not mention taking over the country's biggest energy company during an annual speech to Congress on Thursday, Bloomberg News reported. The administration has heavily criticized **Repsol**'s **YPF** for failing to invest in the country's energy sector, shifting the country from a net exporter to a net importer. "If we hadn't had the increase in imports, we would have posted a trade surplus of $15 billion," said Fernández. However, despite speculation that the government has been considering a full or partial takeover of YPF, the president made no mention of that possibility. YPF shares fell 14 percent on Wednesday amid those fears, but rose 12 percent in New York trading and 17 percent in Buenos Aires following her speech on Thursday.

Fernández

File Photo: Argentine Government.

Armed Group Abducts 11 Colombian Oil Workers

Eleven Colombian oil workers were kidnapped from their bus by an unidentified armed group near the Venezuelan border this week, Reuters reported. Colombian Defense Minister Juan Carlos Pinzón said Wednesday that the contractors disappeared Tuesday in Arauca province as they traveled to work on the Bicentennial pipeline. The government believes that that the ELN, the country's second largest rebel group, is responsible because of the location where they were taken, an army commander told Caracol Radio. The FARC had announced on Sunday it would halt taking hostages for ransom and free 10 military and police officials it has held captive for more than a decade.

Power Sector News

Brazil May Aid Beleaguered Electricity Generator Celpa

Brazil's government may intervene to aid electricity distributor **Celpa**, which filed earlier this week for bankruptcy protection, Reuters reported Wednesday, citing unnamed government officials. The government's intervention to help the debt-laden company could be more effective than a bailout put together by Brazil's state-run power company **Eletrobras**, one of the sources told the wire service. Another possible way to solve the problems at Celpa, which distributed electricity to the northern state of Pará, may be revoking the company's license, one of the sources added. Celpa, which is short of cash, is beset by a possible looming default on 2 billion reais ($1.17 billion) worth of debt.

Endesa Chile Uninterested in Regasification Terminal Stake

Power generator **Endesa Chile** said Wednesday that is does not want to buy a stake in the country's GNL Quintero regasification terminal, which Britain's **BG Group** wants to sell, Reuters reported. A day earlier, Endesa Chile's chief executive officer, Joaquín Galindo, said his company was "evaluating" the possible purchase of all or some of the 20 percent stake in the terminal. The CEO's comments "were meant to signal that the company always analyzes, as part of its normal business, all the opportunities that arise in the Chilean energy sector, but that doesn't mean the company is analyzing purchasing a new stake [in GNL Quintero]," Endesa Chile said in a statement. Currently, the company has a 20 percent stake in the regasification terminal, the same percentage that Chile's state oil company **Enap** and natural gas distributor **Metrogas** also hold. Recently, BG Group announced that it was seeking to reduce its 40 percent stake in GNL Quintero by half. In coming years, the British company wants to sell about $5 billion of assets including ones in the gas distribution, power generation and transmission areas. Endesa Chile is a unit of regional energy company **Enersis** and operates in Argentina, Brazil, Chile, Colombia and Peru.

Galindo

File Photo: Endesa Chile.

Itaú BBA Receiving Loan of as Much as $100 Mn for Green Projects

Brazil's **Itaú BBA** is receiving a loan of as much as $100 million from the Inter-American Development Bank in order to finance projects aimed at helping the environment, the bank said Feb. 24. The proceeds will be used for projects in Brazil, Chile, Colombia, Paraguay, Peru and Uruguay. Projects that can be funded from

The Dialogue Continues

Is Mexico Prepared for Deepwater Drilling in the Gulf?

Q Pemex is not prepared for risks such as a spill or other serious accident that could happen as it plans to drill two wells in ultra-deep waters of the Gulf of Mexico, said Juan Carlos Zepeda, the head of Mexico's National Hydrocarbons Commission, in a Feb. 15 interview with *The Wall Street Journal*. According to Zepeda, his agency's resources amount to about 2 percent the size of its U.S. counterpart's budget. Pemex officials, however, say that the company is capable of carrying out its plans safely. How prepared is Mexico to deal with a serious accident in the Gulf of Mexico? Is the company sacrificing safety in its bid to improve competitiveness and meet production goals?

A Carlos Morán, junior partner at Goodrich, Riquelme y Asociados: "Before Pemex's ultra-deep-water program is put in place, it would be important to review the restrictions existing in our legislation for foreign shipping companies and foreign-flagged vessels with a view to allow foreign environmental response companies to swiftly assist in the event of an oil spill casualty in Mexican waters. Even though Pemex and the Mexican Navy are supposed to have a large stockpile of oil spill fighting and clean-up equipment and a large trained staff, it would be important that experienced international environmental response companies may be permitted to bring their experts and equipment without bureaucratic delays. Environmental response companies usually have to deal with numerous authorities during their operations. Those authorities include environmental, maritime, health, fisheries, aviation, immigration, water and Customs authorities. Occasionally, the requirements of one authority to let such companies operate contradict the requirements of another. This happens even when such authorities are acting within a technical committee assisting the Navy and Pemex in the planning, monitoring and assessment of the emergency. Therefore, in my opinion, the Navy—as the authority in charge of coordinating contingency response efforts—should be given sufficient authority to make quick rulings that are binding on Pemex and all the authorities involved. The Navy should be given such authority in order to ensure an efficient coordination as well as to ensure that environmental response companies have their plans authorized and implemented without any unnecessary bureaucratic obstacles. In addition, those companies should be guaranteed that they will not run the risk of being held liable at civil, criminal or administrative courts if they implement a plan that has been previously approved by the Mexican authorities."

Editor's note: The above is a continuation of a Q&A published in the Feb. 20 - 24 issue of the Energy Advisor.

the loan include ones related to renewable energy and energy efficiency in addition to projects that can generate carbon credits, the bank said. "There is a shortage of financing for green projects in Latin America and this is part of our efforts to bridge this gap," said Daniela Carrera-Marquis, chief of the bank's Financial Markets Division at the Structured and Corporate Finance Department. In recent years, the department has approved $325 million in loans to Latin American and Caribbean financial institutions in order to finance environmentally friendly projects.

Biofuels News

Brazilian Government Boosting Investment to Up Ethanol Supply

Brazil will give ethanol producers as much as ($2.6 billion) of government financing to store fuel in a bid to stabilize prices, Bloomberg News reported Wednesday. Prices of anhydrous ethanol rose 30 percent in 2010 in between harvests, leading the government to set a regulation requiring companies to store ethanol with the goal of avoiding such a price spike. Over the next four years, the government will invest 52 billion reais ($30 billion) to revive ethanol production and attract private sector investments, Platt's reported Monday, citing the Ministry of Agriculture. The government will provide subsidized credit of 29 billion reais to lower the average age of crops as well as 23 billion reais to expand the planted area. Officials estimate that an additional 3.8 million hectares will be needed by 2015 to meet rising demand. [Editor's note: See Q&A about the biofuels outlook in the Feb. 13-17 issue of the *Energy Advisor*.]

The government will invest 52 billion reais to revive ethanol production and attract private sector investments

Political News

Mexico's Presidential Race Tightening Ahead of July Vote: Poll

In Mexico's presidential race, Josefina Vázquez Mota of Mexico's ruling National Action Party, or PAN, is gaining ground against her rival, Enrique Peña Nieto of the Institutional Revolutionary Party, or PRI, according to a new poll released Thursday, the Associated Press reported. Peña Nieto's lead has narrowed to 7 percentage points, with 36 percent of voters favoring him and 29 percent supporting Vázquez Mota, according to the poll by GEA/ISA. In January, the same polling firm showed Peña Nieto had a lead of 20 percentage points ahead of Vázquez Mota. The poll also showed that Andrés Manuel López Obrador of the leftist Party of the Democratic Revolution, or PRD, had 17 percent support. Peña Nieto, a former governor of the State of Mexico, is seeking to return the PRI to Mexico's presidency, which it held for 71 years until the election of Vicente Fox in 2000. However, Peña Nieto has made many verbal gaffes while campaigning and top PRI figures have faced allegations of links to organized crime and financial wrongdoing. By contrast, Vázquez Mota has been seen as confident during campaign appearances and has made few missteps since she last month became the first woman to win a major party nomination for Mexico's presidency. Peña Nieto pointed out to reporters that he maintains a lead in polls, while Vázquez Mota said in a posting on Twitter that she was "very excited" about the latest survey. A poll released Thursday by Parametria also showed Peña Nieto's lead narrowing. It put Peña Nieto 17 percentage points ahead of Vázquez Mota, 4 percentage points less than its poll in January.

Vázquez Mota

File Photo: Vázquez Mota campaign.

Correa Pardons Newspaper Columnist, Executives in Libel Case

Amid growing international criticism, Ecuadorean President Rafael Correa announced Monday that he is pardoning three newspaper executives and a columnist as well as forgiving millions of dollars in fines against a major opposition newspaper in a libel case that he won. Correa had sued *El Universo* over an opinion piece by the columnist, Emilio Palacio, which called Correa a dictator and accused him of allowing soldiers to fire on a hospital during a police uprising in September 2010. Correa denied the allegations and won his libel suit after personally attending court proceedings. In announcing the pardons on Monday, Correa said he had proven his point. We never sought to bankrupt anyone or take anyone's money ... The only thing we were seeking was the truth," he said at the presidential palace, *The New York Times* reported. The case drew condemnation from human rights and press freedom advocates. Carlos Lauría of the Committee to Protect Journalists expressed relief at the pardons, but added Correa "is acting more like a king instead of an elected president," the Associated Press reported. Palacio, who has been seeking political asylum in Miami, said Correa was under international pressure to quash the defendants' three-year jail sentences and the $42 million in fines against *El Universo*. Correa also announced Monday that he would pardon two other journalists who were fined $1 million each for writing a book claiming that Correa's brother had won millions of dollars in government contracts, the AP reported. Correa has denied knowing anything about the contracts.

Colombian Court Removes Chief Prosecutor From Position

A top Colombian court on Tuesday removed from office the country's chief prosecutor, Viviane Morales, who has been under scrutiny because of her marriage late last year to a former congress-

man with links to drug lords, the Associated Press reported. The court ruled that Morales was improperly elected to the post, having failed to receive enough votes. Colombia's Supreme Court selected her in December 2010 among four candidates named by President Juan Manuel Santos. It is possible that Santos could re-nominate Morales, Guillermo Mendoza, a former acting chief prosecutor, told the AP. For now, Morales' deputy will replace her. Morales has been under fire since she married Carlos Alonso Lucio, a former congressman who was an M-19 rebel as a youth. In recent years, Lucio has advised far-right paramilitary groups and has been in contact with extradited drug lords. In 1996, the United States revoked his visa over ties to leaders of the Cali drug cartel. In addition, Morales has had strained relations with Colombia's right wing through her criminal conspiracy prosecutions of former associates of ex-President Álvaro Uribe. Morales was originally married to Lucio in 2000 before separating. She has not publicly commented on their relationship other than to say they did re-marry each other. Lucio is not known to be under any criminal investigations.

Economic News

Argentine Government Calls on Companies to Halt British Imports

Argentina's government is urging the country's largest companies to stop importing goods from Britain in the latest salvo over the nations' dispute over the Falkland Islands, BBC News reported Tuesday, citing Argentine state news agency Telam. Argentina's industry minister, Débora Giorgi, contacted the leaders of 20 companies, calling on them to replace British imports with ones originating elsewhere. The industry ministry wants to lower Argentina's trade deficit with Britain and give preference to countries that support Argentina's claim over the islands, reported Telam. Tensions have been rising between Argentina and Britain ahead of this year's 30th anniversary of the Falklands War. On Monday, authorities in Argentina refused to allow two cruise ships to dock at Ushuaia, apparently because they had earlier made a call at the Falklands.

Venezuela's Government Announces Price Cuts on Basic Goods

Venezuela's government is lowering price caps on several basic goods by 25 percent on average, Vice President Elías Jaua announced Monday, saying the move would help lower inflation, Dow Jones reported. "We have not messed with profit margins," Jaua said in a televised speech. "We have only taken out the costs that should not be included in a cost structure." The price cuts include 19 products, mainly hygiene and other household items. The government will put the price cuts into force on April 1 and Chávez has threatened to nationalize the property of any company that resists. As part of a law approved last year, a new government agency known as Sundecorp will examine the books of some 16,000 Venezuelan companies in order to determine a "just" level of profits the companies should be receiving. Affected companies include **Alimentos Polar** as well as the Venezuelan units of **Colgate-Palmolive** and **Unilever**.

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A review of the Featured Q&As in the *Energy Advisor* in the month of February.

Subscribers may pose questions to the Board of Advisors for the Featured Q&A by contacting Editor Gene Kuleta at gkuleta@thedialogue.org.

POLITICAL & ECONOMIC BRIEFS

Venezuela's Chávez Says He's Recovering Well From Surgery

In his first public comments since undergoing cancer surgery earlier this week, Venezuelan President Hugo Chávez said Thursday that he is recovering quickly and getting official business done, the Associated Press reported. Chávez flew to Cuba a week ago for what he said was urgent surgery to remove a growth in his pelvic region, the same location where a larger tumor was removed last year.

Brazil to Take More Measures to Stem Real

The Brazilian government on Thursday imposed a 6 percent tax on foreign loans and bonds of three years or less and is ready to take additional measures to stem the surging real, Bloomberg News reported, citing Finance Minister Guido Mantega. The real is the world's second-best performing currency this year and Brazil has the highest inflation-adjusted benchmark interest rate in the G-20. "The government won't be a passive observer in this currency war," said Mantega.

Fire Destroys Brazil's Antarctic Research Station

A fire on Saturday destroyed Brazil's research station in Antarctica on Saturday, killing two navy personnel, Dow Jones reported. President Dilma Rousseff said the station would be rebuilt and offered condolences for the victims. Also on Saturday, Brazil's navy confirmed that a resupply barge to the station had sunk less than a mile from the base while carrying more than 2,500 barrels of fuel but said the incidents were unrelated. *O Estado de S. Paulo* alleged a cover-up, saying that the ship sank a month ago.

Featured Q&A

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tial investors think twice about making heavy investments. In particular, the suspension of the Petróleo Plus scheme is a blow for many operators in Argentina and could hinder future investment. The government is likely to continue to put pressure on oil and gas operators in an effort to mitigate the issues created by its past energy policy, which has been dominated by years of regulation and price caps."

A Gianna Bern, president of Brookshire Advisory and Research in Flossmoor, Ill.: "The Argentine government's increasingly contentious relationship does indeed threaten future development of Argentine shale resources. Shale hydrocarbons can be a game changer for Argentina. However, the wild card remains the investment climate in Argentina. Currently, it is still a challenging environment for outside investment given the energy policies put forth by the current administration. If the Argentine government continues to establish policies that are not business friendly, growth investment will stagnate. In recent years, the Argentine energy sector has been subject to considerable under investment from the global oil and gas sector. Both domestic and foreign producers are reacting to an investment climate characterized by high levels of regulation, taxes and an inability to structure crude oil, gasoline and natural gas pricing to global markets. For many producers, this continues to result in less-than-stellar investment returns. These producers will quite simply invest elsewhere. Both domestic and foreign and gas companies need to have a viable business model and generate sustainable profitability in Argentina. The 'under investment' in Argentina is a result of its inability to compete with other countries that have implemented investment friendly energy policies. Argentine shale will get developed if business friendly investment policies are instituted. Shale development is a high-cost proposition necessitating state-of-the art drilling technology and considerable financial resources. In the end, Argentina is going to have to compete with both Poland and the United States for those same investment dollars in similar shale projects."

A Michael Underhill, chief investment officer of Capital Innovations LLC: "As a portfolio manager overseeing assets for large pension funds and managing a mutual fund, seeing this happen is not encouraging. Foreign direct investment will dry up immediately, and the emotional table tennis that Kirchner is playing causes guys like me to abstain from investing millions of dollars in their publicly traded securities market with the expropriation/government counter party risk. Political risk is something we always consider, but what Cristina is doing is setting up the country for a higher-risk scenario and increasing the overall cost of financing at exactly the wrong time. With that scenario, Argentina's bonds will need to be priced with higher yields, equities will be more volatile, less liquid and the capital markets will not be orderly. Money will instead flow to Brazil and Chile where there is lower political risk."

> "What Cristina is doing is setting up the country for a higher-risk scenario and increasing the overall cost of financing at exactly the wrong time."
>
> — ***Michael Underhill***

The Energy Advisor *welcomes responses to this Q&A. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.*

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