LATIN AMERICA ADVISOR

ENERGY ADVISOR

A WEEKLY PUBLICATION OF THE DIALOGUE

www.thedialogue.org

May 22, 2020

FEATURED Q&A

Should State Firms Redirect Efforts Away From Oil?

Mexican state oil firm Pemex is moving ahead with plans to drill new wells and speed up development, despite estimates that many are not profitable at current oil prices. // File Photo: Mexican Government.

Q Mexican state oil company Pemex this year seeks to nearly double drilling to 423 wells and speed up development of 15 recent discoveries, despite experts' warnings that many are unprofitable at current international prices, Rigzone reported last month. It also plans to move ahead with a new refinery. Should Latin American states continue to invest money in an industry whose economic profitability has come into question both amid lower prices in the short term and in a context of climate policy in the longer term? Is it economically sensible for governments in the region to keep focusing on national oil companies, or should they redirect efforts toward other sectors? What are the underlying factors influencing governments' decisions to continue supporting state oil firms, and how do resource nationalism and politics come into play?

A Jose L. Valera, member of the Energy Advisor board and partner at Mayer Brown: "The best that can be said about governments' decisions to create and support national oil firms (NOCs) is the belief that NOCs bring revenues that constitute the basis for country's development. Nonetheless, not a single Latin American country has ever demonstrated that this is true. What happens, in fact, is the opposite. Governments place excessive reliance on oil revenues and fail to nurture the development of a broad-based and diversified economy led by the private sector that generates stable tax revenues, creates jobs and attracts capital and innovation. The main export from these countries actually ends up being their own people and capital. Throughout their history, Latin American countries have argued,

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TOP NEWS

OIL & GAS

Petrobras Posts Loss of 48.5 Billion Reais in Q1

A 65.3 billion real ($11.2 billion) impairment on the Brazilian state oil firm's exploration and production assets led to the quarterly loss, Petrobras said.

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POWER SECTOR

Colombian Gov't Warns of Power Rationing Risks

Energy Minister María Fernanda Suárez warned that dry conditions are increasing the risk of power rationing unless hydroelectric generators preserve water reserves, which is currently not the case.

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POWER SECTOR

Brazil Reportedly Eyeing $2 Billion in Aid for Utilities

Brazilian Energy Minister Bento Albuquerque is considering emergency loans of nearly $2 billion to help power utilities navigate the economic downturn brought by the coronavirus pandemic, three sources familiar with the matter told Reuters.

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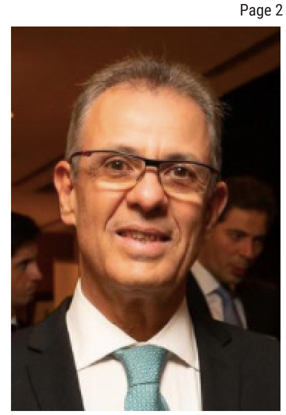

Albuquerque // File Photo: Brazilian Government.

POWER SECTOR NEWS

Brazil Reportedly Eyes $2 Billion in Aid for Power Utilities

Brazil's government is considering emergency loans of 12 billion reais ($2.06 billion) to help power utilities navigate the economic downturn brought by the coronavirus pandemic, Reuters reported May 14, citing three people with knowledge of the matter. Energy Minister Bento Albuquerque said earlier this month that the government was working on an aid package for the country's electricity distribution sector, which he said would be presented by the end of May. He did not give details on how large potential loans could be. Power distribution firms have been pushing for an aid package as electricity demand has plunged amid the Covid-19 health crisis and consumers increasingly default on utility payments. Industry executives estimate they need between 15 billion and 17 billion reais in order to meet their obligations to power generation and transmission companies, the wire service reported. The government has said it is in talks about such aid with state banks BNDES, Banco do Brasil and Caixa Econômica Federal, as well as private lenders Itaú Unibanco and Banco Bradesco. Brazilian utilities are facing surplus energy this year of between 20 percent and 40 percent due to the sharp plunge in consumption during the pandemic, Reuters reported. [Editor's note: See related **Q&A** in the April 17 issue of the Energy Advisor.]

Industry Blasts New Rules Regulating Mexico's Power Grid

The Mexican government last Friday issued new rules for the operation of the country's power grid, affecting dozens of renewable energy projects, The Wall Street Journal reported. Energy companies and local industry groups blasted the new rules, saying they favor Mexican state-owned electricity utility CFE over private developers and roll back the opening of the power market to foreign investors. The Energy Ministry said on Saturday that the reason for halting the entry of solar and wind plants into operation was the plunge in demand due to coronavirus lockdowns, which raised the need for more "reliable and continuous" power supply, The Wall Street Journal reported. Industry associations said the new rules would affect 28 solar and wind projects that were set to go online, as well as 16 others under construction, which together total $6.4 million in investments, much of it from foreign firms, the Associated Press reported. "This represents a frontal attack on legal security for investments in Mexico and causes serious consequences for the country, including the loss of jobs and investor confidence," Mexico's Business Coordinating Council wrote on Sunday. "This does not just discriminate against renewable energy, it also allows authorities to artificially inflate the price of electricity and arbitrarily displace any private sector power generation project," it added. [Editor's note: See related **Q&A** in the May 6 issue of the daily Latin America Advisor.]

OIL AND GAS NEWS

Petrobras Registers Loss of 48.5 Billion Reais in First Quarter

Petrobras saw a 65.3 billion real ($11.2 billion) impairment on its exploration and production assets, leading the firm to register a first-quarter net loss of 48.5 billion reais, the Brazilian state oil company said May 14, Reuters reported. The company warned that changes in consumer behavior resulting from the coronavirus pandemic would likely be permanent. Petrobras wrote off the entire value of its shallow-water assets, saying it did not expect to restart production at six high-cost production assets currently for sale. Total impairments amounted to 57.6 billion reais for its deepwater assets, including the Marlim Sul oilfield, and 6.6 billion reais for its shallow-water fields. The remain-

NEWS BRIEFS

Colombia Energy Minister Warns of Power Rationing Risks During Dry Season

Colombia's government warned last week that dry conditions are increasing the risk of power rationing in the country, unless hydroelectric generators preserve water reserves, Argus Media reported. "We hoped that the hydro generators would be dispatching less electricity to the market, but that is not happening right now," said Energy Minister María Fernanda Suárez. "If the reservoirs remain very low, that could put us at risk during the 2020-21 dry season," she added.

SCOTUS Declines to Hear Venezuela's Appeal in Case Involving Citgo

The U.S. Supreme Court on Monday declined to hear Venezuela's appeal of a lower court ruling allowing defunct Canadian gold miner Crystallex to seize the shares of U.S.-based refiner Citgo, one of Venezuela's most important assets, to collect on an unpaid $1.4 billion arbitration award, Reuters reported. The decision is a setback to opposition leader Juan Guaidó, whom the United States recognizes as Venezuela's interim president and who has sought to protect Citgo from seizure.

Enel Planning $49 Million Investment in Chile

The Chilean unit of Italian company Enel expects to invest about $49 million in the construction of a project that will be part of the country's first hybrid industrial plant, Renewables Now reported Tuesday. The project consists of the Azabache Park solar power plant, which will have the capacity to generate 60.9 megawatts of electricity and is to be located near the city of Calama in Chile's Antofagasta region, the company said. Once constructed, Azabache Park will operate together with Enel's Valle de los Vientos wind farm.

ing 1.1 billion reais of writedowns consisted of other unspecified assets. Even without the impairment, Petrobras reported a loss in the first three months of the year as a result of the oil price shock and the devaluation of the real, which is among the world's worst-performing major currencies this year, Bloomberg News reported. The company's earnings before interest, taxes, depreciation and amortization, or EBITDA, which excludes the devaluation, surpassed expectations at 37.4 billion reais. Despite the losses and low crude prices, which have hit the entire industry, Petrobras benefited from rebounding oil demand in China, which helped drive its total exports up to a record high in April. Since then, there are signs that Petrobras is getting better prices for its oil from Chinese refiners, Bloomberg News reported. The company also said its divestment program remains unchanged, despite delays, adding that it expects to close some refinery sales by the end of 2020. While the company registered a 3.8 percent drop in output in the first quarter, production bounced back in April. However, the company has revised its pricing, assuming long-term Brent oil prices of $50 per barrel, down from a previous assumption of $65. As a result, the company said it was revising all exploration and production projects to ensure they are economically sound given the new pricing assumptions.

Argentine Gov't Sets Local Crude Oil Price at $45 Per Barrel

Argentina's government on Tuesday fixed the local crude oil reference price at $45 per barrel in an effort to protect the country's hard-hit energy sector from the economic fallout of the coronavirus pandemic and low global crude prices, Reuters reported. In a decree, the government of Peronist President Alberto Fernández said the decision was due to "the drastic fall in the international oil price of a barrel of oil, which is seriously damaging the activity of the national hydrocarbon sector." Known as the "criollo barrel," Argentina has previously set local oil prices to offset global price volatility.

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by and large, that the state has to own 'strategic' industries. Under this theory, they took it upon themselves to fund and manage large industries, preempting the private sector. The results are perennial losses, bad services, scarcity, technological lapse and inefficiencies. Against this background and instructive history, now comes AMLO doubling down. He argued against the further implementation of the energy reform that his predecessor initiated, saying that Pemex was going to produce and export more and also import less. He doesn't have the capacity to change course in the face of hard business data and is doing tremendous economic damage to Mexico. Areas that are properly within the state's purview, such as education, public health and security, are underfunded, while at the same time precious resources are spent on inherently risky ventures that can and should be carried out by the private sector, such as drilling oil wells and building refineries."

A **Gilberto Bercovici, professor of economic law and political economy at the University of São Paulo:** "In Brazil, the nationalization of oil has been historically identified with the affirmation of national sovereignty. Petrobras, as a state-owned company, is an instrument of the Brazilian state's national economic policy, acting in accordance with the strategic and social welfare objectives set forth in the constitution, going far beyond the mere pursuit of profitability. The fact that it belongs to the government does not prevent it from being efficient, constituting one of the most dynamic forces in the oil industry. The oil price crisis should not affect Petrobras' performance if it recovers its presence in all segments of the integrated oil industry focused on the domestic market. Oil is not only a source of energy, but also one of the industry's basic inputs. Petrobras is fundamental to the industrial sector installed in Brazil as an integrated supplier of energy, fuels and basic inputs. The necessary sustainability in the development of energy exploration also requires investment in new technologies to produce alternative energy sources, such as biofuels. Petrobras is the largest investor in science and technology in Brazil. Petrobras' role, therefore, continues to be central to energy policy in general, and to the oil sector in particular, serving to curb the economic power of the large oligopolies, to ensure nonpredatory exploration of deposits and to defend the interests of the community, in addition to acting strategically, controlling the supply of oil and oil products in Brazil."

A **R. Kirk Sherr, member of the Energy Advisor board and president of Clearview Strategy Group:** "Occasionally, big bets pay off. Most often, they don't. López Obrador is 'all in' on his Pemex bet, and his odds of winning are not good. AMLO faces long odds (such as other regional countries betting big on the future of their state oil companies) for three main reasons. First, the issue of how close we are to seeing peak demand for oil is ever more relevant. Leading oil company CEOs are musing publicly about whether demand for oil has been permanently lowered by Covid-19 and other factors. Second is the inexorable negative impact on oil demand from declining renewable energy and battery storage costs. (Abu Dhabi just secured a bid for $0.0135/kilowatt-hour for a large PV solar plant—roughly one-third the price of power from the most efficient natural gas combined cycle plant.) Third, Pemex is its own worst enemy. Despite a recent small production uptick and better reserve replacement performance in 2019, the company remains vastly overstaffed and inefficient. It is ill-prepared for the dynamic global competitive environment that lies ahead. In fact, KPMG noted in its recent 2019 audit report that there is 'significant doubt about Pemex's ability to continue as a going concern.' Pemex and select Latin American state-owned companies should

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The decree said the measure would be in place until the end of the year, but the local reference rate will be voided if the international benchmark price of Brent crude surpasses $45 per barrel for 10 consecutive days.

POLITICAL NEWS

Bolivia's Health Minister Arrested in Ventilators Case

Bolivian Health Minister Marcelo Navajas was arrested Wednesday in connection with an investigation into allegations that the government paid inflated prices for ventilators to treat patients suffering from Covid-19, the Financial Times reported. Navajas had been in office for just six weeks. His attorney, Rosario Canedo, confirmed Navajas' arrest, calling it "an infamy." She said to reporters in La Paz, "Are we living under the rule of law, or are we living in a dictatorship and under a totalitarian government?" Local media had reported that the government overpaid for the ventilators, leading Interim President Jeanine Áñez to order an investigation on Tuesday. Bolivian newspaper Página Siete reported that the government paid $4.7 million for 170 ventilators on a contract worth $1.2 million, though other newspapers reported that it bought 179 ventilators, citing different prices. On Wednesday, Áñez tweeted that the contract was worth $4.8 million and that the government had paid just over $2 million of it. She vowed that "every cent that has been stolen will be returned," the Financial Times reported.

Venezuela's Guaidó Accuses Maduro of Staging Incursion

Venezuelan opposition leader Juan Guaidó on Wednesday accused President Nicolás Maduro of orchestrating and financing an alleged failed incursion this month, without providing hard evidence to back up the claim. During an online event hosted by the Inter-American Dialogue, Guaidó accused Maduro's government of being behind the so-called "Operation Gideon," in which a group of apparent mercenaries, including several Venezuelan dissidents and two Americans, purportedly attempted to infiltrate the country by sea on May 3. Guaidó, whom dozens of countries recognize as Venezuela's interim president, accused Maduro of using the incident as a propaganda tool to smear and persecute the opposition. "This has been

ADVISOR Q&A

Will Latin America's Schools Be Able to Reopen Safely?

Q Countries in Latin America are starting to discuss the reopening of schools, which, along with most public places, have been closed for nearly two months during the Covid-19 pandemic. Is now the right time for schools in the region to reopen? What should public officials do to ensure that the health of students and staff is protected as classes restart? Do primary and secondary schools, as well as higher-education institutions, have enough government funding and resources to both educate students and protect their health?

A Ariel Fiszbein, director of the education program at the Inter-American Dialogue: Most countries in Latin America (the exception being Nicaragua) have closed schools in response to the Covid-19 pandemic. In spite of the ongoing efforts to scale up distance-learning approaches, students and their families are struggling to maintain a normal learning environment. The reopening of schools will most likely be a gradual process depending on the evolution of the pandemic and local conditions. Countries will need to develop detailed plans that will typically entail the gradual and possibly partial reopening of schools with rotating attendance in order to enable some social distancing. The state of school infrastructure will be a critical factor. Unfortunately, schools with poor sanitary facilities (for example, no or intermittent running water) and limited space to allow for social distancing will face serious difficulties. Addressing those difficulties will require special efforts to upgrade school infrastructure to accompany procurement of the necessary cleaning supplies and protective equipment. Teachers and directors will need to be prepared to provide remedial education and socioemotional support to students in their return to classes. Moreover, capabilities for distance learning should continue to be upgraded as the emergency may well continue throughout this and the next academic year. All of this strongly suggests that budget demands will be significant. Countries are experiencing the largest negative shock on human capital accumulation in modern times. Attention to immediate needs should not result in underinvestments with dramatic negative long-term effects."

> **"Attention to immediate needs should not result in underinvestments with dramatic long-term effects."**
> **— Ariel Fiszbein**

EDITOR'S NOTE: More commentary on this topic appears in Monday's issue of the Latin America Advisor.

NEWS BRIEFS

Venezuelan Military to Escort Iranian Tankers Delivering Fuel

Venezuela's military will escort Iranian tankers delivering fuel to the Andean nation as soon as they reach Venezuela's exclusive economic zone, Defense Minister Vladimir Padrino said Wednesday, Reuters reported. The military would "welcome them in and thank the Iranian people for their solidarity and cooperation," he said. Opposition leader Juan Guaidó said the shipment should "alarm" Latin America.

Mexico City to Gradually Begin Reopening Economic Activity June 1

Mexico City will begin a gradual reopening of economic activities on June 1, Mayor Claudia Sheinbaum said on Wednesday as the country recorded its largest coronavirus-related daily death toll and cases continue to increase, the Associated Press reported. The number of Covid-19 deaths nationwide rose by 424 on Wednesday to 6,090, well above last week's record of 353 deaths reported in one day. Total confirmed cases of the virus reached 56,594, but experts believe the real number to be much higher due to a lack of sufficient testing.

Costa Rica Reaches Deal to Allow Entry of Panamanian Truckers

Panama and Costa Rica have reached a deal to allow Panamanian truck drivers to enter Costa Rica under strict health control protocols and reopen the Paso Canoas cargo passage at the countries' border, Panama's government said Wednesday, QCosta Rica reported. The announcement followed a blockade by Panamanian carriers in protest of Costa Rica's move to prevent the entry of foreign drivers to curb the spread of Covid-19. More than 60 truck drivers at Costa Rica's southern and northern borders have tested positive for the novel coronavirus.

a huge propaganda apparatus … Not only was this operation infiltrated, but also financed by the dictatorship," Guaidó said. "Given the result [of the incident], which only benefits the dictatorship, this much seems almost obvious," he added. Maduro has said the plot had the goal of killing him. During the event, Guaidó again denied any involvement in the incident. Though some of his advisors, who have since resigned, previously met with those who claimed responsibility for the plan, Guaidó said such "strategy meetings" were held a long time ago and "have nothing to do" with the botched plot. Among the people that Venezuelan authorities arrested in connection with the incident earlier this month is former U.S. Army special forces soldier Luke Denman. In a heavily edited video that Maduro's government released, Denman held up to the camera a contract for the plot purportedly bearing Guaidó's signature. Guaidó has called the contract a fake. U.S. President Donald Trump has also denied involvement in the incident. Venezuela's Ministry of Communication and Information did not respond to an email from the Advisor seeking comment on Guaidó's accusation. [Editor's note: See related Q&A in Tuesday's issue of the daily Latin America Advisor.]

ECONOMIC NEWS

Cuba Asks Paris Club for Delay in Debt Repayments

Cuba has asked the Paris Club of major bondholders for a delay in the repayment of its debt until 2022, blaming the economic fallout of the coronavirus pandemic, diplomatic sources told Agence France-Presse on Wednesday. In a letter to the 14 countries of the Paris Club, which includes Britain, Canada, France and Japan, Cuban Deputy Prime Minister Ricardo Cabrisas proposed "a moratorium for 2019, 2020 and 2021 and return to paying in 2022," the source said. Two other diplomats confirmed the information. The island nation last year missed more than $30 million in payments, which were due under a 2015 restructuring deal that had been considered as a step toward integrating Cuba into the international financial community, Reuters reported. "The agreement is extremely beneficial for Cuba and that they could not pay speaks volumes about how broke they are," one diplomat told the wire service in February, when news broke that Cuba had failed to meet its 2019 payments. Also that month, Cuba committed to settling that debt by May, but the pandemic has hindered that plan, AFP reported. According to one source, the letter says that Cuba would reassess its economic situation in 2021 to determine if it could resume payments then.

Ecuador's Moreno Seeks to Save $4 Bn Amid Pandemic

Ecuadorean President Lenín Moreno on Tuesday announced a series of measures in an effort to save $4 billion in the wake of the coronavirus pandemic, El Comercio reported. Among them, the president said he would cut the salaries of government employees, shut down some embassies and sell off several state-owned enterprises, including a newspaper, a TV station, a railway company and a state-owned airline that has lost more than $400 million over the past five years, the Associated Press reported. Ecuador has been among the worst-affected countries in the region by both the pandemic and the plunge in international oil prices, one of its main exports. Moreno said the spending cuts are necessary to control debt and prioritize health and education. "We are fighting to stop infections and reduce the number of deaths wrought by coronavirus," the president said in a television address, the AP reported. "But at the same time, we need to stop our economy from collapsing," he added.

> "We need to stop our economy from collapsing."
> — Lenín Moreno

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consider how they will remain competitive in coming years without permanent financial support from their governments. Using government funds to develop renewable energy for climate, employment and financial gains is more likely to have the better long-term payoff versus competing with international oil companies."

A **Thea Riofrancos, assistant professor in the Department of Political Science at Providence College:** "The fossil fuel sector is reeling from plummeting demand and crashing prices. The deepening recession has rocked the industry to its core, raising the possibility that it will not recover for years to come—or ever, if governments adopt stringent climate policies. The fallout has devastated Latin American producers, which are vulnerable to global price shocks, and deprived governments of a crucial revenues at a moment when the public sector is more needed than ever. Latin America is at a crossroads: governments can either embrace a just transition to renewable energy, centering workers and frontline communities, or double-down on oil and gas, betting on industries with an uncertain future. Worryingly, administrations have opted for the latter course, propping up financially and environmentally unsustainable projects and shelving renewable energy plans, often under the banner of resource nationalism and energy independence. But leftist goals of equality, sovereignty and environmental sustainability won't be served by extractive sectors. Instead, governments should redefine resource nationalism, using its tools and institutions—state-owned firms, progressive contracts and long-term planning—to empower workers and protect indigenous rights, all while transitioning to a more equitable, low-carbon economic model. Across the Americas, movements and policymakers are pushing for a new 'eco-social pact.' National oil and gas companies could play a key role by transitioning workers to clean energy and environmental remediation, and shifting investment priorities toward the region's untapped potential of wind, solar and geothermal. This is the only path forward for an inclusive and sustainable 21st century economy."

A **Jose Zapata, Bogotá-based partner at Holland & Knight:** "Latin American countries have had a permanent concern of ensuring that local production of oil and gas meets local demand. This historic view has been tied to beliefs that many other countries share, of nationalistic approaches to energy and natural resources as well as national 'security.' While this may have been a valid approach for many years, the pressure of the current oversupply scenario and particular concerns regarding environmental issues clearly demand an objective recognition that the traditional model may simply negatively affect these countries' delicate economic balances. Two aspects are particularly relevant in reassessing the current situation. The first is competitiveness of terms and conditions, which countries can effectively offer where prospectivity is low. Countries must recognize that efforts to achieve such competitiveness cannot be undertaken on the basis of marginal and untimely benefits with respect to an impacted industry that is more likely to seek opportunities elsewhere, in conditions that better reflect market prices and regulatory security. Second, verification of the feasibility of developing a local oil and gas industry amid local regulatory, social and political conditions is merited. Countries must accept that if these conditions are inexistent, the cost of E&P will be unmanageable. Countries need a reality check and must determine if they are willing to pursue the pre-existing model while allowing the renewable energy mix to evolve, or simply be destined to a permanent frustration of having their NOCs seek opportunities outside in an effort to lose less. There is a limit to politics and nationalism when it comes to hard investments and low returns amid the current economic crisis."

LATIN AMERICA ENERGY ADVISOR
is published weekly by the Inter-American Dialogue
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Latin America Energy Advisor is published weekly, with the exception of some major U.S. holidays, by the Inter-American Dialogue
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Washington, DC 20005 **Phone:** 202-822-9002

www.thedialogue.org

ISSN 2163-7962

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