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FEATURED Q&A

Could Venezuela's Oil Sector Survive U.S. Sanctions?

Venezuelan President Nicolás Maduro on Tuesday said he would pursue his plan to elect a constituent assembly to rewrite the country's Constitution, despite the United States' threat of sanctions, including on the oil sector, if he does so. // File Photo: Venezuelan Government.

Q **The administration of U.S. President Donald Trump is mulling possible sanctions on Venezuela's energy sector, including on state-run oil company PDVSA, Reuters reported in June. Oil is at the core of Venezuela's economy, with some 95 percent of export revenues coming from the energy sector. Approximately 8 percent of U.S. oil imports in March came from Venezuela, the third-largest oil supplier to the United States. What would happen if the United States stopped buying oil from Venezuela? Would the oil be sold to another country, and, if so, which? What would be the terms for selling the oil that would normally go to the United States to another buyer? How would the U.S. oil sector adapt in the event of such sanctions?**

A **Francisco J. Monaldi, fellow in Latin American energy policy and lecturer in energy economics at the Baker Institute for Public Policy at Rice University:** "U.S. sanctions on the Venezuelan oil sector could include: financial sanctions on PDVSA, limitations on U.S. firms doing business with PDVSA, banning of oil and/or product exports from the United States to Venezuela and banning of U.S. crude imports from Venezuela. The United States exports between 100,000-150,000 barrels per day (bpd) to Venezuela of products and light oil, and imports between 750,000-800,000 bpd of heavy oil. Banning U.S. exports to Venezuela would force Venezuela to import products from costlier suppliers in Europe or Asia, and would affect the diluents required to export between 250,000-300,000 bpd of extra-heavy crude. Banning the imports would have multiple effects. The main U.S. buyer of Venezuelan oil is Citgo, an affiliate of PDVSA, which would be affected by the ban at

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Brazilian oil regulator ANP may allow companies to ease local content rules for pre-existing exploration and production contracts.

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The Likana Solar Energy Project will provide a non-intermittent, 24-hour supply of energy. The plant is SolarReserve's third project to receive Chile's approval.

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Total, YPF Among Investors in Vaca Muerta Project

The investment is expected to double natural gas production at the area to 4.5 million cubic meters per day, up from a current 2.2 million cubic meters per day, according to Neuquén Governor Omar Gutiérrez.

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Gutiérrez // File Photo: Government of Neuquén Province.

OIL & GAS SECTOR NEWS

Brazil May Ease Local Content Rules for Pre-Existing Oil Contracts

Brazilian oil regulator ANP may allow companies to ease local content rules for pre-existing exploration and production contracts, agency Chief Décio Oddone said Tuesday, Reuters reported. The measure would be an attempt to revive projects that have been put on hold due to local content requirements, which can be costly for companies. Local content rules determine the percentage of projects' workers and inputs that must be local in origin. Oddone said the regulator would open a 30-day comment period for the proposal, followed by a hearing and a publication of the ruling in September. Contracts signed between 2005 and earlier this year, when more flexible local content rules were put in place, would be eligible for the new measure. "We believe this new option will unlock investments, attracting capital and generating new hires, jobs and revenue," Oddone said. Many crude projects have been put on hold in Brazil, due in part to the costs associated with local content rules. According to Oddone, ANP has received more than 230 requests for exemptions from the rules by companies that are operating under pre-existing contracts that were signed before ANP enacted more relaxed rules for new contracts starting in February.

Total, Argentina's YPF Among Investors in Vaca Muerta

Argentine state-run oil company YPF, along with France's Total, Argentina's Wintershall Energía and Argentina's Pan American Energy on Tuesday announced they plan to jointly invest $1.15 billion in the Vaca Muerta shale formation in the Neuquén Province of Argentina in order to increase shale gas production, Reuters reported. The investment is the largest in Vaca Muerta since March, and comes as the government of President Mauricio Marci looks for ways to reduce the country's reliance on gas imports. Total will operate in the eastern part of the Aguada Pichana area with a 41 percent stake and is planning to drill 48 horizontal wells in the area through 2021, up from a current 12. Pan American Energy will operate in the western part of Aguada Pichana as well as in Aguada de Castro with a 45 percent stake, and plans to drill 24 horizontal wells. The government of Neuquén Province has agreed to split the Aguada Pichana area into two parts and will combine it with the Aguada de Castro area, according to a statement. The investment is expected to double natural gas production at the area to 4.5 million cubic meters per day, up from a current 2.2 million cubic meters per day, according to Neuquén Governor Omar Gutiérrez. Pan American Energy Executive Director Marcos Bulgheroni said the costs of the logistics of operating at the formation still needed to be lower, but that "the development of Vaca Muerta is on a path of no return." Vaca Muerta and 16.2 billion barrels of shale oil, according to the U.S. Energy Information Administration.

The investment is the largest project announcement in Vaca Muerta since March.

Ecuador Planning to Increase Oil Production

Ecuador has announced it will increase its oil production this month, falling out of step with a decision by the Organization of the Petroleum Exporting Countries, or OPEC, to cut oil production in order to stabilize the global oil market, The Wall Street Journal reported Tuesday. In

NEWS BRIEFS

Vestas Signs Contract to Supply Dominican Republic Wind Park

Denmark-based wind turbine manufacturer Vestas has signed a contract to supply 14 turbines for the 48-megawatt Larimer II wind park, located in the Dominican Republic's Enriquillo region, Windpower Engineering & Development reported Wednesday. The Caribbean nation has set a goal of boosting its share of renewable energy and lowering greenhouse gas emissions by 25 percent by 2030, as compared to 2010. The company "continues to play a key role" as the Dominican Republic transitions toward energy independence, said Marco Graziano, the president of Vestas Mediterranean. The turbines are expected to be delivered in the first quarter of next year.

Mexico Officials Delay Oil Auction for Evaluation of Major Crude Discoveries

Officials in Mexico said July 14 they will delay the next scheduled offshore oilfield auctions by a month in order to allow bidders more time to evaluate recent major crude discoveries, Bloomberg News reported. Last Tuesday, a consortium reported discovering a reservoir with an estimated 1.4 billion to 2 billion barrels of oil in the southern Gulf of Mexico, the same day Italian producer Eni said a March find contained the equivalent of as much as 1 billion barrels.

Value of Renewable Energy Deals in Region Grows 157% Since 2013

The value of renewable energy deals in Latin America increased 157 percent between 2013 and 2016, according to data released July 14 by Mergermarket, growing from $975 million to $2.5 billion. More than a third, or 26 of the 62 renewable energy deals recorded in the region since 2013, involved wind farms.

May, OPEC agreed to extend cuts to oil output among members by nine months to March of next year. The decision to cut production

Pérez // File Photo: Ecuadorean Government.

was first agreed upon last November. In June, Saudi Arabia said it failed to comply with its production allotment, as did Iraq. Overall compliance with the OPEC agreement fell to 78 percent in June, from 95 percent in May, when the extension was enacted. Ecuadorean Energy Minister Carlos Pérez said late Monday that the country could no longer afford the production cuts, "because of the needs that the country has." Last year, Ecuador agreed to limit its output by 26,000 barrels per day, but Pérez said Ecuador's oil sector is in fact only limiting its output by about 16,000 bpd. He did not say whether the country's oil output would increase beyond its current level. An Ecuadorean OPEC official could not be reached for comment. [Editor's note: See related **Q&A** in the June 2 issue of the Latin America Energy Advisor.]

POWER SECTOR NEWS

Argentina's YPF Discussing Sale of Electricity Unit to GE

Argentine state-run energy company YPF is in talks with General Electric to sell the U.S.-based conglomerate a 49 percent stake its electricity subsidiary, Reuters reported July 14, citing Argentine newspaper Clarín. Spokespeople from YPF and GE declined to comment on July 14. The value of the possible deal is unclear, as YPF has not made public the value of its YPF Energía Eléctrica subsidiary. YPF and GE are collaborating on electricity projects in Argentina, including plants in Tucumán province and near the Vaca Muerta shale field. Earlier this month, YPF and GE announced they had received $220 million in financing from Citigroup and Credit Suisse, among other backers, for two jointly owned thermal power projects. YPF Energía Eléctrica first began operating in 2013 after YPF acquired assets from Argentine oil and gas company Pluspetrol, which had spun off its electricity generation business. The asset sale at the time had a total value of $485 million, according to a filing from YPF.

SolarReserve Gets Chile's OK to Build Thermal Station

The Chilean government has granted U.S. solar energy company SolarReserve environmental approval to construct a 390 megawatt solar thermal power station that will have 5,100 megawatt-hours of energy storage, the company said in a statement Wednesday. The plant is SolarReserve's third project to receive the Chilean government's approval. The Likana Solar Energy Project, located in the Antofagasta

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two of its refineries in the Gulf Coast, which refine about 550,000 bpd, of which about a third comes from Venezuela. Other companies affected would be Valero, Phillips 66 and Chevron. The United States would have some difficulty obtaining heavy oil from the hemisphere. Mexico and Colombia can redirect some of their Asian sales to the United States, but it would not be enough. Canada can increase its exports, but transportation problems limit this option. Saudi Arabia might be needed to cover some of the missing oil. In the end, the cost of imports would probably rise, but the needed supply would come. Venezuela will have more trouble finding buyers for all that heavy oil, but in the end it will probably sell a large portion to Asia, at some discount. The combination of both types of sanctions could prove brutal for the already cash-strapped PDVSA, probably forcing it into default. Business sanctions on PDVSA could also affect U.S. companies operating in Venezuela, including Chevron and some large service companies like Schlumberger. Overall, the decline in Venezuela's production would intensify, and future oil production recovery would be harder."

> **"[The] sanctions could prove brutal for the already cash-strapped PDVSA."**
> **— Francisco J. Monaldi**

A **Luis Giusti, senior advisor (non-resident) for energy and national security at the Center for Strategic & International Studies:** "For many decades, PDVSA was the largest supplier of oil to U.S. refiners in the Gulf Coast, over Mexico and Saudi Arabia (the three combined supplied between 5 million and 6 million bpd). Oil from Venezuela and Mexico was mostly heavy and extra-heavy, the best buy for many refiners who years before had invested in conversion capacity so they could buy a cheaper feedstock in the future. Since his arrival, late Venezuelan President Hugo Chávez was aggressive against the United States and the export volumes from Venezuela began to slide (today it's 700,000 bpd), as a result of the shipping of growing amounts of oil supply to China. If the U.S. government were to impose sanctions on Venezuela, those imports would very likely be banned from entering the United States. Several important local refineries would suffer a shortfall of

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region, will provide a non-intermittent, 24-hour supply of energy. It will be comprised of three 130 MW solar thermal towers, which will each contain 13 hours of full load energy storage. The project is expected to generate 2,800 gigawatt-hours annually. "The Likana project will help lower electricity costs for Chilean families and businesses, while safeguarding grid stability," said Tom Georgis, SolarReserve's senior vice president of development. The company will be bidding energy and associated capacity from the Likana project as well as its other two projects in the country in the next annual auction for firm energy supply issued by Chile's power distribution companies.

POLITICAL NEWS

OAS' Almagro Backs Venezuela Sanctions in Hill Testimony

Organization of American States Secretary General Luis Almagro on Wednesday told U.S. lawmakers that he backs targeted sanctions against top-ranking members of Venezuela's government, the Associated Press reported. "The only action of the government we see these days is repression," Almagro told the Senate Foreign Relations' Western Hemisphere subcommittee. "The scenarios that we see are pretty ugly for Venezuela." Almagro, however, also cautioned members of the subcommittee against imposing sweeping economic penalties, which he said could exacerbate the suffering of the Venezuelan people. Almagro, who described Venezuela as the continent's most corrupt country, also questioned whether sanctions would succeed in forcing President Nicolás Maduro to make changes. "There is no way to push a dictatorship down from abroad," said Almagro. "So sanctions may work or may not work. It depends on the internal pressure in the country." Earlier this week, U.S. President Donald Trump warned he may take "economic actions" if Maduro pushes forward with a planned July 30 vote to elect members of a new constituent assembly, which would be tasked with rewriting the country's Constitution. Maduro's supporters want the assembly to grant him broader powers, and Maduro has said the country needs a new Constitution in order to solve its political and economic crises.

Almagro // File Photo: Organization of American States.

ADVISOR Q&A

What Does López's Release Mean for Venezuela?

Q Venezuela's government on July 8 released opposition leader Leopoldo López from prison and transferred him to house arrest. The government said he was released due to health reasons, and the Supreme Court said his release was also due to "serious signs of irregularities" in the handling of his case. Was the decision to release López indeed motivated by concern for his well-being, or did the government have other motives for doing so? How will López's release affect the opposition's strategy in confronting the administration of President Nicolás Maduro, if at all? To what extent will López now have more direct influence over the anti-government movement in the country?

A Luis Vicente León, president of polling firm Datanalisis in Caracas: "Although Leopoldo López wasn't completely freed, it's striking that now the government is open to improving his living conditions by placing him under house arrest. It was done on the basis of human rights in light of his 'precarious health condition.' This is not even remotely the actual reason for López's house arrest. The government is trying to lower the high levels of tension throughout the country. The decision affected the opposition, which is characterized by internal divisions; it's something that we saw evidence of just a day after López was sent home, when ahead of the statement from his wife, Lilian Tintori, in which she thanked Libertador Municipality Mayor Jorge Rodríguez and former Foreign Minister Delcy Rodríguez for their negotiation efforts, the media went crazy attacking López and Tintori, who just hours before had been considered leaders of the country and of the resistance, accusing them of collaborating and negotiating with the government. This sends a clear message. Although Maduro is not willing to risk his position of power, he understands that it is better for him to defuse the conflict, looking for ways to lower tension in the streets, not because he fears an abrupt exit, but rather because doing so obliges the opposition to keep up repressive actions that could generate internal conflicts within itself. Last Sunday's referendum was a new milestone in the opposition's fight against the government, and it's clear that the opposition increased its pressure against the impending constituent assembly, which would signify the end of the republic and the end of what remains of democracy in Venezuela. López is a protagonist of this story and, although he's not alone, he will be influential in the complex decisions, both promising and risky, that will be made in the coming days."

EDITOR'S NOTE: More commentary on this topic appeared in the Q&A in Thursday's issue of the daily Latin America Advisor.

NEWS BRIEFS

Judge Freezes Assets of Brazil's Lula

Brazilian Judge Sérgio Moro, who is leading anti-corruption probe "Operation Carwash," has ordered that the assets of former President Luiz Inácio Lula da Silva be frozen after convicting and sentencing him to prison last week on graft charges, Agence France-Presse reported Wednesday. Lula remains free pending his appeal of the verdict and denies wrongdoing. Lula has said he still plans to run for president in the election set for next year. [Editor's note: See **Q&A** on Lula's conviction and sentencing in Tuesday's Latin America Advisor.]

Uruguayan Pharmacies Begin Selling Cannabis Directly to Consumers

Pharmacies in Uruguay on Wednesday began selling cannabis products directly to customers, Reuters reported. The country's nearly 5,000 registered users will be able to purchase five-gram sealed packets for $6.50 each at pharmacies. In 2013, Uruguay became the first country in the world to legalize the recreational use, sale and cultivation of marijuana.

Brazil's Lower House Aims to Vote on Pension Reform by Late August

The lower house of Brazil's Congress is aiming to vote on a controversial pension reform plan by the end of August, the chamber's leader said in a newspaper interview published today. "We need to start voting it in August," Chamber of Deputies Speaker Rodrigo Maia told O. Estado de S. Paulo. He expressed hopes that the legislation advances to the floor of the chamber by the end of the month. The reform would set a minimum age for retirement and would cut social security benefits. Some economists say the reform is needed in order to avoid a debt crisis. However, labor unions oppose the changes, saying they are unfair to workers.

Maduro's opponents, however, see the effort as a power grab by the president. In his appearance on Capitol Hill, Almagro said more than 100 people have been killed and thousands of others have been injured in Venezuela since a series of anti-government protests began in early April, the AP reported. He added that there are 444 political prisoners in Venezuela. The OAS chief also told lawmakers that other countries' reluctance to "act in defense of democracy has allowed the situation to deteriorate incrementally, but consistently, to the point where today it has become a full-blown humanitarian and security crisis."

ECONOMIC NEWS

U.S. Releases List of Objectives for NAFTA Renegotiation

The administration of U.S. President Donald Trump on Monday released a 17-page list of its objectives for the upcoming renegotiation of the North American Free Trade Agreement, or NAFTA. "Some Americans have benefited from new market access provided by the Agreement," says the document, from the office of the U.S. trade representative. However, it adds that "NAFTA also created new problems for many American workers. Since the deal came into force in 1994, trade deficits have exploded, thousands of factories have closed, and millions of Americans have found themselves stranded, no longer able to utilize the skills for which they had been trained." The document, which the Trump administration sent to Congress, makes reduction of U.S. trade deficits a top priority and also takes elements of the Trans-Pacific Partnership, which Trump abandoned after taking office in January, The New York Times reported. The outline also appears to send a signal to countries other than Canada and Mexico by including concerns about subsidized state-owned enterprises and currency manipulation, which apply more to countries such as China. The White House has said a renegotiated NAFTA will likely serve as a model for trade deals with other countries. The objectives also include elimination of the Chapter 19 dispute settlement panel, which allows Canada and Mexico to appeal duties that the United States imposes. Another potentially controversial proposal would do away with a provision that limits the United States' ability to impose import restrictions on its neighbors.

Argentine Mortgage Loans Grow Amid Gov't Subsidies

Argentina's new subsidized mortgage program is leading to a jump in mortgage loans in the South American country, as well as a boost in construction activity, Reuters reported Monday. Argentines took out mortgage loans totaling 3.7 billion pesos ($219.32 million) in June, up from 558 million pesos in the same month last year, according to central bank data. While the overall amount is still low, it is seen as a significant increase in Argentina, where a high rate of

> **"For the middle class ... all this spurs the economy and generates activity."**
> — Ivan Kerr

inflation discourages would-be borrowers from seeking credit. In March, President Mauricio Macri's government launched a plan to provide 90,000 Argentines subsidized mortgages. Participants must have monthly incomes of between 16,000 and 32,000 pesos ($948-$1,897). About half of the country's economically active population earns less than 10,000 pesos ($593) monthly, according to government data. "For the middle class, which is large, all this spurs the economy and generates activity," Ivan Kerr, the country's national subsecretary of urban development and housing, told Reuters in an interview. Another plan that the government recently launched provides borrowers low-interest mortgage loans that are adjusted for inflation. The programs, put in place ahead of the October legislative elections, primarily benefit the country's urban middle class.

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supply and would have to buy from other vendors to make up for the missing volume. However, there is abundant available oil for sale in the world, and although those refineries would suffer some economic impact because they would likely have to buy more expensive oil, they should survive. In Venezuela, the impact of the sanctions would, no doubt, be a severe blow to the already critical financial situation of PDVSA and the Maduro government; currently, exports to the United States are the only ones that bring cash punctually, and that oil would likely have to be sold to others, perhaps at a discount. However, it cannot be overlooked that the sanctions would bring even more backlash against the already massively impoverished and suffering Venezuelan population."

A **Gustavo Coronel, a founding board member of PDVSA:** "At the rate the Venezuelan crisis is developing, it is very unlikely that the United States will have the time to take effective steps of this type, as the executive branch is showing little signs of moving quickly in this direction. From a political point of view, it would be extremely effective to impose a sanction of this nature, as U.S. importers are probably the only ones that pay the Venezuelan regime in cash and on-time. From a technical point of view, there could be some minor problems, as some U.S. refiners located in the Gulf Coast claim that they depend on Venezuelan heavy, sour crude oil for their needs. However, this type of crude is also available from Canada, Saudi Arabia and Mexico. The volumes of this type of crude oil coming to the United States from Venezuela could rather easily be provided by a combination of these three sources. If this took place, the Venezuelan regime would be in a very difficult financial position, as there are few clients currently ready to absorb the volumes coming to the United States—some 700,000 barrels per day. An equally effective step for the United States in its desire to sanction the Venezuelan regime would be to prohibit the sale of gasoline and diesel to the Venezuelan state oil company, PDVSA, a volume that already amounts to some 100,000 bpd. This is a product sorely needed by the regime, in view of the operational collapse of the Venezuelan refineries."

The Advisor welcomes comments on its Q&A section. Readers can contact editor Gene Kuleta at **gkuleta@thedialogue.org**.

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