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**FEATURED Q&A**

# Can Temer Boost Brazil's Struggling Energy Sector?

Brazilian President Michel Temer has vowed to implement policies with the goal of attracting investment in the energy sector. // File Photo: Brazilian Government.

**Q** **Michel Temer was sworn in as Brazil's president on Aug. 31, replacing ousted President Dilma Rousseff. How will the change in government, which puts Temer in power until 2018, affect Brazil's struggling energy sector? Will the Temer administration be able to work with Congress and turn the page on Petrobras' protracted corruption scandal? What energy policy changes are expected to come from a Temer government?**

**A** **Johanna Mendelson Forman, senior advisor with the Managing Across Boundaries Initiative at the Stimson Center:** "President Michel Temer's business-friendly Brazilian Democratic Movement Party may not be enough to help him rebuild the struggling energy sector in Brazil. Caught in a crisis of legitimacy, Temer's troubles with the Lava Jato legal investigation will not go away just because he was able to rid himself of Rousseff. The investigation has revealed the connections between his party and the Workers' Party to siphon billions of dollars from Petrobras. Future outcomes in the corruption probe ultimately will not only affect the energy sector, but will also further erode the limited legitimacy that Temer and his government enjoy with ordinary Brazilians. Months before Dilma's removal from office at the end of August, many international oil industry analysts thought that a change in government would open a new chapter in Brazil's energy sector. But the scope of reforms needed may far exceed the government's capacity, given the high level of distrust in Congress and in President Temer's capacity to effect change. If Temer is able to set a reform agenda for Petrobras, he will face hostility from the Workers' Party in Congress in making any

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**TOP NEWS**

OIL & GAS

## Lula Charged in Petrobras Graft Case

Brazilian prosecutors on Wednesday filed charges against former President Luiz Inácio Lula da Silva, his wife and six others in connection with the massive corruption scheme at state-run oil company Petrobras.

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## IEnova Plans to Raise Over $1 Bn in Share Offering

Mexican energy infrastructure company Infraestructura Energetica Nova plans to raise more than $1 billion in a secondary share offering next month, which would be one of the biggest Mexican equity placements in recent years.

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OIL & GAS

## PDVSA Proposes $7 Bn Debt Swap

PDVSA President Eulogio Del Pino on Tuesday announced a proposed $7 billion bond swap in outstanding debt in order to ease cash-flow concerns for the state oil company.

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Del Pino // File Photo: Venezuelan Government.

OIL & GAS SECTOR NEWS

# PDVSA Proposes $7 Bn Debt Swap Amid Cash Shortage

Venezuelan state-run oil company PDVSA on Tuesday proposed a $7 billion bond swap in outstanding debt in order to ease cash-flow concerns, Reuters reported. Following PDVSA President Eulogio Del Pino's announcement of the program, the company's bonds surged Wednesday as investors bet that the debt-swap plan would bolster finances, The Wall Street Journal reported. The program would allow bondholders to exchange debt maturing in 2016 and 2017 for debt due in 2020. Detailed terms on the program have not been disclosed. The company had been racing to increase its cash flow amid reduced output, a global decline in oil prices and approximately $8 billion worth of debt maturing in 2016 and 2017, with the majority due later this year. "They are doing this because they don't have other choices," said Russ Dallen, a managing partner at Caracas Capital, an investment bank. The debt swap is expected to reduce the oil company's near-term payments, and may help Venezuela's sovereign standing. It's not clear, however, that the debt swap will be enough to "offset the worsening political situation," when it comes to Venezuela's sovereign rating, said Jaime Reusche, an analyst at Moody's Investors Service. The cash shortage has impaired the company's ability to import much-needed diluents that allow PDVSA to formulate exportable crude as well as produce refined products for the country's domestic market. Delayed payments for crude imports due to cash shortages have been costly for the company, which will have to pay oil major British Petroleum at least $130 million more for planned crude imports than it had originally anticipated, according to internal documents seen by Reuters, the wire service reported Tuesday. Despite holding some of the world's largest crude reserves, Venezuela in March made its first crude purchase from BP in order to dilute its own extra-heavy crude. Venezuela awarded BP a large tender, for which the South American country had expected to pay $230.9 million, or approximately $31 per barrel, in prepaid shipments of 7.4 million barrels. Venezuela's delays in payments, however, had prevented BP from sending its crude to Venezuela on time, which resulted in BP repricing some of its cargoes, as well as charging PDVSA for keeping vessels offshore.

> "They are doing this because they don't have other choices."
>
> — Russ Dallen

# Brazilian Prosecutors Charge Lula in Petrobras Graft Case

Brazilian prosecutors on Wednesday filed charges against former President Luiz Inácio Lula da Silva, his wife and six others in connection with the massive corruption scheme at state-run oil company Petrobras. In a news conference, Public Prosecutor Deltan Dallagnol alleged that Lula was the mastermind behind the scheme that siphoned some 6.2 billion reais ($1.9 billion) from the state oil company, The Wall Street Journal reported. Some of the money, prosecutors allege, was directed to Lula's Workers' Party and its allies in an effort to keep the then-ruling party's coalition in power. "He was the conductor of this criminal orchestra," Dallagnol said Wednesday of Lula, Reuters reported. "The Petrobras graft scheme aimed at keeping the Workers' Party in power by criminal means." Lula has consistently denied wrongdoing, and his lawyers said Wednesday that prosecutors lacked evidence to support the charges. "This Lula-centered farce was trumped up as an affront to the democratic state and intelligence of Brazilian citizens," said one of the former president's lawyers, Cristiano Zanin. The formal charges against Lula and his wife focus on a more narrow allegation—that the former president and his wife illegally received approximately $1.1 million

NEWS BRIEFS

## Argentina's Aranguren Sells Stock in Shell

Argentine Energy Minister Juan José Aranguren has sold his stock in the energy company Royal Dutch Shell, President Mauricio Macri confirmed Tuesday to La Nación. The announcement comes after the country's anti-corruption office called on Aranguren to sell his shares in the company to avoid a conflict of interest, though Macri maintained that the minister sold his shares "by his own volition." Aranguren served two years as head of Shell Argentina until 2015, when he left after 37 years, and later was appointed energy minister by Macri in December.

## Petrobras' Pre-salt Oil & Gas Production Grows 4 Percent

Petrobras' oil and natural gas production in pre-salt fields grew by 4 percent last month to 1.36 million barrels of oil equivalent per day, the state-run oil company announced Monday. The new monthly record was attributed mainly to the connection of new wells as well as increased production in wells already connected to floating production storage and offloading vessels Cidade Maricá and Cidade de Saquarema in the Lula field of the Santos Basin.

## Pemex Discovers Six New Crude Deposits in the Gulf of Mexico

Mexican state-run oil company Pemex has discovered six new offshore deposits of light crude oil, the company announced Tuesday, The Wall Street Journal reported. The discoveries, which are located in the Gulf of Mexico, likely contain between 190 and 220 million barrels of oil equivalent. Pemex did not say when it will begin drilling the new wells. In recent years, decreased revenue due to low oil prices has led to severe budget and production cuts at the company.

in improvements and expenses related to a beachfront apartment, paid for by construction giant OAS, which was seeking government contracts, The New York Times reported. Lula has denied ownership of the apartment. While Lula was previously implicated in the so-called "Car Wash" investigation of Petrobras, Wednesday marked the first time that prosecutors accused him of being anything more than a beneficiary, the Associated Press reported. Judge Sérgio Moro, who has already sentenced several people to long prison terms in connection with the Petrobras case, must now decide whether to accept the charges against Lula and the other defendants in order to proceed to trial.

**POWER SECTOR NEWS**

# IEnova Plans to Raise More Than $1 Bn in Share Offering

Mexican energy infrastructure company Infraestructura Energetica Nova, or IEnova, plans to raise more than $1 billion in a secondary share offering next month, three individuals with knowledge of the matter said, Reuters reported Monday. The offering would be one of the biggest Mexican equity placements in recent years. IEnova, a unit of U.S. energy firm Sempra Energy, has hired Credit Suisse and JP Morgan to underwrite the offer, which will help fund the infrastructure company's major investments. A spokeswoman from IEnova declined to comment. Credit Suisse and JP Morgan declined to comment as well. IEnova is part of a group of Mexican companies that pushed into the country's oil and gas industry after Pemex lost its monopoly in Mexico's 2013 energy reform. Last year, IEnova purchased the 50 percent stake owned by Pemex in pipeline company Gasoductos de Chihuahua for more than $1 billion, as the state oil firm looked to shed its assets amid falling crude prices. IEnova has won other big contracts recently, and CEO Carlos Ruíz in July said the company would fund its expansion through a mix of equity and long-term debt.

**RENEWABLES NEWS**

# Brazil, Panama Ratify Paris Climate Accord

Brazil and Panama on Monday both ratified the Paris agreement to fight global warming and limit greenhouse gas emissions, bringing the international deal closer to implementation, Reuters reported. Brazilian President Michel Temer signed the ratification after both houses of Congress approved it. Panamanian President Juan Carlos Varela called climate change a "threat to the health and wellbeing of society," EFE reported. The two Latin American nations join top polluters the United States and China, which both ratified the deal on Sept. 3. To take effect, the deal must be ratified by at least 55 parties to the United Nations Convention on Climate Change, and the ratifying parties must represent at least 55 percent of global emissions. The United Nations said that by Sept. 7, 27 parties had ratified the agreement, amounting to 39 percent of global emissions. Brazil accounts for approximately 10 to 12 percent of global carbon pollution, while Panama's accounts for only 0.2 percent of global

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major changes. Layoffs in the sector due to Brazil's contracting economy, coupled with external factors such as the continued decline in global oil prices, will make extracting the pre-salt oil even more costly, at a time when Brazil's economy is already in a recession. Without any regulatory changes to allow private-sector companies to work on the pre-salt oil deposits currently managed by Petrobras, there will be little incentive for international companies to expand investments in the short term. Renewable energy, one of the hallmarks of Brazil's energy sector, will also be affected by the poor economic outlook in the coming year. Wind energy, one of the fastest-growing energy sectors, will suffer in the negative investment climate. Temer will have a tough time selling this country to new investors and making good on the country's commitment to reducing greenhouse gases by having 23 percent of its energy coming from renewable resources by 2030, as the economic and political crisis continues to overshadow these types of policy goals."

> **"The scope of reforms needed may far exceed the government's capacity."**
> **— Johanna Mendelson Forman**

**A** **Henrique Rzezinski, vice president of external relations at Parnaiba Gas Natural in Rio de Janeiro:** "President Temer has a historic chance to upgrade his biography, from the most unpopular president in Brazil's recent history to the president who was able to approve the vital reforms the country desperately needed. And this is the one simple choice he has to make: either run for re-election or use all his political capital to pass the reforms in Congress, even if it means paying the price of unpopularity. One of the vital reforms is related to the energy sector. The regulatory and institutional framework has to generally change in the following ways: 1) rebuild Petrobras by selling assets to financially equilibrate the company and changing governance in order to avoid corruption; 2) reintroduce the concession regime in place of the production-sharing regime, as was the case with the very successful 1998 regulatory framework, when important results were achieved for all players like Petrobras, the federal government, the states as well as national and international companies; 3) end Petrobras' obligation to be the single operator in the pre-salt as well as the 30 percent minimum participation requirement of Petrobras in all Joint Operations Agreements (JOA); and 4) change the local content rules and make them more realistic for local industry ambitions. Several regulatory changes have to be approved in order

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emissions. Brazil has previously committed to cutting carbon emissions by 37 percent by 2025 and by 43 percent by 2030, compared to 2005 levels.

## IDB Among Backers of $103 Mn Nicaragua Geothermal Project

The Inter-American Development Bank said Sept. 9 it would back a $103.4 million program to develop Nicaragua's geothermal energy sector and the construction of transmission infrastructure for the Central American country, SeeNews reported. The IDB will lend $51.4 million to the program, and another $25 million will come from the Korea Infrastructure Development Co-financing Facility in Latin America and the Caribbean, which the IDB manages. The Clean Technology Fund and the Scaling Up Renewable Energy in Low Income Countries Program will grant $17 million to the program, with the remaining $10 million covered by local counterpart funds. The money will be used, among other things, to conduct site investigation in order to determine the viability of harnessing the geothermal potential in the Cosigüina field in northwestern Nicaragua. The program will also help develop mechanisms to attract private investment in the country's geothermal sector.

**POLITICAL NEWS**

## Argentina, Britain Agree to Joint Steps on Falklands

Argentina and the United Kingdom on Wednesday agreed to taking joint steps toward removing restrictions on a number of industries in the Falkland Islands, according to a joint communiqué from the two countries, The Guardian reported. Both sides agreed to "take the appropriate measures to remove all obstacles limiting the economic growth and sustainable development of the Falkland Islands," the Argentine foreign ministry said in a statement, adding that the governments will discuss the areas of shipping, fishing and oil and gas drilling. Tensions rose over the disputed islands last year when then-President Cristina Fernández de Kirchner restricted vessels passing through Argentine waters to reach the Falklands and when an Argentine federal judge ordered the seizure of $156 million in drilling equipment belonging to oil drilling companies operating in the islands. But Alan Duncan,

# THE DIALOGUE CONTINUES

## How Will Peace in Colombia Change the Country's Energy Outlook?

**Q** **Colombia's government and the FARC rebels on Aug. 24 announced they had reached final agreement on historic peace accords following nearly four years of talks in Havana. Although Colombian voters must approve the deal in a nationwide referendum, set for Oct. 2, the government says a "peace dividend" could add a percentage point or more to the country's gross domestic product. How would Colombia's peace process change the outlook for the country's energy sector and chances for production gains? Will foreign investors make big bets on Colombia's oil and gas opportunities, or, in a period of low oil prices, will they seek to invest in more predictable environments elsewhere in the world? Will the energy sector, long a target of pipeline sabotage and severe harassment of its employees, see a more favorable security situation as a result of the accords?**

**A** **Jorge Lara-Urbaneja, partner at Arciniegas, Lara, Briceño & Plana in Bogotá:** "The peace process between the Colombian government and the FARC should not substantially change the outlook for the Colombia energy sector. The ELN rebel group, rather than the FARC, has been attacking up the Coveñas pipeline since it was under construction. The ELN is far from even initiating peace conversations. In reality, the energy sector grows only when there is solid exploration activity. But oil exploration was suspended in Colombia a few years ago, even before the peace talks with the FARC started, and not because of the crude price drop. Oil companies reduced their activities due to the cumbersome conditions and requirements officially imposed on them. Besides obtaining governmental and environmental authorizations, which may be very cumbersome, oil companies must secure operative permits from native and Afro communities that, in several instances, lead to endless and costly negotiations. Moreover, there are instances in which the oil authority has withdrawn the operating authorizations under claims that oil exploration activities may damage the subsoil. Evidently, the present oil price structure becomes also a very negative factor. The fact is that oil production in Colombia has been declining for the last two years, and it is calculated that present oil reserves should last around seven years, if no major oil fields are discovered and enter into production by then. Ecopetrol, the state oil company, would not change the picture; it is investing very small resources in oil exploration. But the assumption in the question is correct in that the oil industry must be rebuilt and, for that, the institutions must be back over the whole country."

**EDITOR'S NOTE: More commentary on this topic appeared in the Sept. 9 issue of the Latin America Energy Advisor.**

NEWS BRIEFS

## Restarting Talks May Take 10 Years if Colombians Reject Accords: de la Calle

Top Colombian peace deal negotiator Humberto de la Calle warned Colombians to carefully consider their decision before voting in next month's referendum, saying that if the public votes against the government's peace accord with the FARC rebels, it could take 10 years before new negotiations are started, BBC News reported Wednesday. "The 'no' camp's idea of renegotiating seems like a massive mistake to me," he said. "The risk is that if people vote 'no', thinking this will bring about a renegotiation, it is certain that nothing will happen."

## FIFA Suspends Guatemalan Soccer Federation

World soccer's governing body, FIFA, has suspended the Guatemalan football federation, or Fedefut, over political interference, BBC News reported Thursday. FIFA said local authorities had intervened in undermining a local committee that FIFA had put in charge of running the game there, following a corruption scandal. The national team and all of the Central American country's clubs will be barred from participating in international competitions, though senior FIFA official Primo Coravo said the ban might not be immediate.

## Santander Rio Denies it's Purchasing Citi's Argentina Operation

Banco Santander Rio on Wednesday denied earlier newspaper reports that it had purchased Citibank's retail business in Argentina, according to a letter from Santander to the Buenos Aires Stock exchange, Reuters reported. "Banco Santander Rio S.A. has not reached any agreement to buy the retail operations of Citibank in Argentina," Santander said in the letter.

Britain's minister of state for foreign and commonwealth affairs, hailed the agreement as a victory for Argentina's new diplomatic approach. "The measures agreed today demonstrate we can make progress through dialogue," Duncan said in a statement, Reuters reported.

**Duncan** // File Photo: British Government.

The countries also agreed to allow more flights between the Falklands and Latin America. The nations have disputed the islands for more than a century and fought a brief war over them in 1982. On Wednesday, the countries said they will speed up the process of DNA identification for unknown Argentine soldiers buried on the islands who were killed in the war.

ECONOMIC NEWS

## Chile to Limit Investment to Boost Spending on Health, Education

Chile's 2017 budget will limit state investment in public projects and increase funding to health care and education reform, said Finance Minister Rodrigo Valdés, Bloomberg News reported Wednesday. Overall fiscal spending will increase from last year, and investment in public projects will not necessarily be cut, but some projects may be reassigned or others will not start next year, Valdés added. The government under President Michelle Bachelet has expanded public spending since 2014, but the announcement reflects the government's efforts to cut the so-called structural deficit by 0.25 percent of GDP every year in order to balance it by 2020. Low copper prices have added a strain to government income and have led to a widened budget gap, despite announced spending cuts in March. Chile is experiencing its third year of sluggish economic growth, and the economy contracted for the first time in six years during the second quarter of this year, when GDP shrank by 0.4 percent over the period. Fiscal spending rose by 2.7 percent during the same period, in an effort to counteract a 0.4 percent drop in household spending. Fiscal spending will not be cut next year, but the government is hopeful that private investment will help drive growth in the coming months.

## Brazil's Temer Launches Privatization Plan

Brazilian President Michel Temer on Tuesday announced a sweeping privatization plan in an effort to revive the country's economy, which is suffering its worst recession in decades. Under the initiative, the government plans to sell licenses to operate energy and infrastructure projects, Reuters reported. By March, Temer's government is also planning to sell operating licenses for the airports in Porto Alegre, Salvador, Fortaleza and Florianópolis. "We need to open up to the private sector because the state cannot do everything," Temer told cabinet members during a discussion of the plan, which is called "Project Growth." Privatizations that will include the construction and management of airports, roads, railways, oil fields and mining facilities will occur by 2017 or 2018, Temer said, the Associated Press reported. The plan encompasses an "extraordinary opening" of the country's infrastructure, he added. The government's concessions for the projects will have long-term financing from state-run banks or will be financed through bond sales on capital markets, Wellington Moreira Franco, the government's top official for increasing private sector investment in the country's infrastructure, said Tuesday, Reuters reported. "We will restore confidence by expanding the legal security for investors," he said. Moreira Franco added that the concessions will offer "realistic" rates of return.

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to approve different modes of gas monetizations such as gas to wire and others. In other words, it is a task for a statesman, not a regular politician. History will tell us what kind of man Michel Temer is."

**A** **Isabella Alcañiz, assistant professor of government and politics at the University of Maryland:** "One of the areas that will require the immediate attention of the controversial new president of Brazil, Michel Temer, is the country's embattled energy sector. Even before the impeachment against Dilma Rousseff was finalized, Temer signaled that he would attempt to open the sector to foreign investment in order to pay staggering debts and revitalize energy giants Petrobras and Eletrobras. These companies have been deeply troubled by corruption scandals and falling international oil prices. But signals that Brazil is cleaning up shop have been mixed. Temer placed a young politician with no technical background and little political experience in energy policy—albeit from a powerful family—at the helm of the Ministry of Mining and Energy. There have been few serious attempts to push forward the investigation of corruption in Petrobras, and Temer himself has been implicated in the scandal. Temer will probably soon learn that with a small percentage of seats in Congress, it was much easier to whip up votes against an unpopular president in her second term than it is to pass legislation on deregulation. With a significantly polarized and tight domestic front, Temer will want to go abroad to seek foreign investment in the sector—in fact he has done already, with one trip to Asia under his belt, and another planned for the near future."

> **Signals that Brazil is cleaning up shop have been mixed."**
> — Isabella Alcañiz

**A** **Clarissa Lins, founding partner of Catavento Consultancy in Rio de Janeiro:** "The minister of energy that President Temer appointed in May, Fernando Bezerra de Sousa Coelho Filho, was unknown to the sector. At 32 years old, he is very young and has spent the last decade as a congressman, following the steps of his father, an influential senator. His nomination was definitely seen as a political one, losing space to more technical appointments that were expected in a sector devastated by the previous government. Nonetheless, Coelho Filho has positively surprised energy experts. He nominated renowned executives to the boards and management of the two largest state-owned energy companies, Petrobras and Eletrobras, on top of appointing respected officials to technical positions at the ministry of energy. Additionally, he initiated a very proactive dialogue with key stakeholders in order to establish a roadmap for the energy sector. New priorities are being set: the financial restructuring of Petrobras, including divestments and partnerships; the end of the obligation of Petrobras to be the sole operator of the pre-salt, which the Senate is likely to approve in late September; a new bid round for offshore fields in the first half of 2017 and the revision of the rules for local content. These initiatives represent a completely different scenario from the one in place until May—they require both that Petrobras have sufficient room to maneuver, and that the private sector trust a government sometimes tempted to act more politically than technically. I believe that the urgency of the facts will be decisive in turning the Brazilian energy sector into one of the most attractive in Latin America."

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

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