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FEATURED Q&A

Has Puerto Rico Prepared Enough to Privatize PREPA?

PREPA's diesel oil powered, 464 megawatt combined cycle power plant in San Juan is pictured. Fuel oil costs consume the majority of PREPA's expenditures. // File Photo: CIC Construction Group.

Q With nearly one-third of Puerto Rico still without power after Hurricane Maria struck the island last September, Governor Ricardo Rosselló announced in January that his administration would seek to privatize bankrupt public power utility PREPA, the Puerto Rico Electric Power Authority. Will the plan to privatize PREPA succeed? What lessons from past privatizations of state power monopolies elsewhere in the world could help Puerto Rico avoid pitfalls in the process? Will privatizing the utility capture the sort of investment the commonwealth's energy sector needs? Should consumers expect improved services and lower rates soon?

A Rafael Cox Alomar, associate professor of law at the David A. Clarke School of Law at the University of the District of Columbia: "Privatization on its own will not solve Puerto Rico's chaotic energy crisis. Transitioning from a state-owned monopoly to a privately owned one will not by itself generate the required incentives for the structural re-engineering of the island's primitive energy sector. Hence, the success or failure of the government's strategy will depend on the specific privatization model ultimately selected. And by all means, the model Puerto Rico needs is one premised on the vertical unbundling of the system within the context of open-market competition all along the generation, transmission and distribution chain. Robust competition, closely monitored by a wholly independent governmental regulator, should yield the necessary incentives for: (1) diversifying (at last) the island's unbalanced energy portfolio on the basis of a sensible cost-efficiency strategy moving in the direction of renewables; (2) reduc-

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TOP NEWS

OIL & GAS

Mexico Joins the International Energy Agency

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OIL & GAS

Vista Invests $700 Million in Argentina Assets

The deal, which includes an oil and gas platform along with significant interests in exploitation concessions in the Neuquén basin, would make Vista the fifth-largest oil producer and operator in Argentina.

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OIL & GAS

Venezuela Says First 'Petro' Sale Raises $735 Million

Venezuelan President Nicolás Maduro on Tuesday touted this week's pre-sale of the new "petro" digital currency, which is backed by the country's oil reserves, as a big success.

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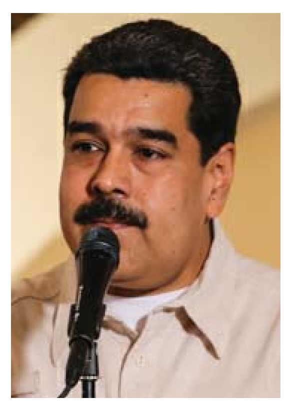

Maduro // File Photo: Venezuelan Government.

OIL & GAS SECTOR NEWS

Venezuela Says First 'Petro' Currency Sale Raises $735 Million

Venezuela's government announced Tuesday that the pre-sale of its new "petro" digital currency raised $735 million on its first day, the Financial Times reported. The petro is backed by Venezuela's oil reserves, and a white paper on the currency said 100 million petro coins will be issued. Of that amount, the government plans to sell 38.4 million through a pre-sale, with a $60 reference price. The pre-sale is scheduled to last until March 19. The government plans to sell an additional 44 million coins in an initial offering, scheduled to start on March 20. In a tweet on Tuesday, President Nicolás Maduro said the currency would be a "big solution" to Venezuela's economic problems. [Editor's note: See Q&A about the petro in the Jan. 31 issue of the Advisor.]

Mexico Becomes First Latin American Country to Join IEA

Mexico on Saturday officially became the first country in Latin America to join the Paris-based International Energy Agency, a move that required ratification by Mexico's Senate. "With this final step, Mexico enters the most important energy forum in the world," Joaquín Coldwell, Mexico's secretary of energy, said in a statement. "We will take our part in setting the world's energy policies, receive experienced advisory in best international practices, and participate in emergency response exercises," he added. The IEA says its 30 members now account for more than 70 percent of global energy consumption, up from less than 40 percent in 2015. "The ambitious and successful energy reforms of recent years have put Mexico firmly on the global energy policy map," said Fatih Birol, the IEA's executive director. Although Mexico ranks as the world's 12th-largest oil producer, output has fallen steadily for years, with monthly crude production from state-run oil company Pemex dropping below two million barrels per day last July for the first time in more than two decades, Reuters reported. But last month, Mexico's government held its most significant oil auction in two years of attempts to open the oil industry to foreign investment. Officials estimated the auction, which featured large bids by the U.K.'s Royal Dutch Shell among other international oil companies, could bring more than $90 billion in investment to the country as firms develop the areas they won.

Vista Buys Oil, Gas Assets in Argentina

Mexico City-based Vista Oil & Gas on Monday announced it had agreed to acquire an oil and gas platform in Argentina from Pampa Energy and Pluspetrol, along with interests in certain exploitation concessions in the Neuquén basin. The deal would make it the fifth-largest oil producer and operator in Argentina. Miguel Galuccio, the chief executive officer of Vista who formerly led Argentine national oil company YPF, said the timing of the acquisition "could not be better suited to start delivering on our

Galuccio // File Photo: Vista Oil and Gas.

plan of becoming the leading Latin American independent oil and gas company." The deal is valued at $700 million, according to the Financial Times, and gives Vista average daily production of 27,500 barrels of oil equivalent per day and 137,000 acres in the Vaca Muerta deposit which the company aims to bring into production next year. Vista estimates that in the next five years it could more than double the current production rate, reaching 65,000

NEWS BRIEFS

Brazil's Petrobras Reports 1 Percent Decline in Oil Production in January

Brazilian state oil company Petrobras reported Wednesday that its total average oil and natural gas production in January fell by 1 percent, to 2.7 million barrels of oil equivalent per day. The average oil production within the country fell to 2.1 million barrels per day, while oil fields abroad produced 61,000 bpd. The company attributed the decline mainly to maintenance stoppages at a platform in the Campos Basin and its sale of 35 percent of the Lapa field in the Santos Basin to France's Total.

Ecopetrol Increases Proven Reserves by 3.8 Percent in 2017

Colombian national oil company Ecopetrol on Monday announced its net proven reserves rose 3.8 percent at the end of 2017 as compared to the previous year, or 73 million barrels of oil, Reuters reported. Net proven reserves totaled 1.66 billion barrels of oil-equivalent, with average reserve life growing from 6.8 to 7.1 years. Reserves increased primarily due to higher recovery factors at mature fields, as well as incorporating new projects. "This result is very satisfactory," the company said.

Sanctions Slow Citgo's Work on Aruba Refinery

Houston-based oil company Citgo said Wednesday that work to overhaul its refinery in Aruba has slowed due to a lack of financing as a result of U.S. sanctions on Venezuela, Reuters reported. The 235,000-barrel-per-day refinery has been leased since 2016 by Citgo, which is owned by Venezuelan state oil company PDVSA, under a 25-year agreement with the Aruban government. The deal also includes an extensive $685 million overhaul of the facility. In statement, Citgo said 600 workers had been hired for the project.

barrels per day of crude oil equivalent, La Nación reported. Backed private equity firm Riverstone, Vista raised $650 million in an initial public offering in August when it was launched as a special purpose acquisition company.

POWER SECTOR NEWS

Puerto Rico's Power Utility Gets Approval for $300 Mn Loan

The Puerto Rico Electric Power Authority has received a judge's approval to get a $300 million loan in order to help pay expenses at the beleaguered commonwealth-owned electric company, Reuters reported Tuesday. U.S. District Court Judge Laura Taylor Swain approved the loan for the utility, better known as PREPA. The federal board that is overseeing Puerto Rico's debt restructuring had originally sought a $1.3 billion loan after Hurricane Maria battered the island last September, cutting off power to much of the territory. However, creditors opposed that initial amount over its size and terms, and the two sides argued the issue in court. The judge reduced the loan amount to $300 million. Puerto Rico has more than $70 billion in debt, and PREPA has in excess of $14 billion in liabilities.

Scatec Picks GE Power for Solar Project in Brazil

Norway's Scatec Solar has chosen Boston-based GE Power to supply solar photovoltaic skids for a 162-megawatt solar project located in the state of Ceará in Brazil, PV Magazine reported Monday. The solar project, near the city of Quixeré, was awarded in an auction process held by Brazil's electricity regulatory agency in 2015. No financial details were disclosed. Brazil aims to bring up to 7 gigawatts of solar generation capacity online by 2024, as compared to the current solar power generation capacity of just above 300 MW, according to a statement from GE.

Emerging Markets and Renewables to Drive Energy Growth Through 2040: BP

British oil company BP on Wednesday released its 2018 Energy Outlook with predictions that emerging markets and renewables will dominate energy sector growth through the year 2040. The report forecasts that faster growth of energy consumption in developing economies will drive up global energy demand a third higher than today, and that the global energy mix will be the most diverse the world has ever seen by 2040, with oil, gas, coal and non-fossil fuels each contributing around a quarter. Renewables will become "by far the fastest-growing fuel source," increasing five-fold and providing around 14 percent of primary energy. The most growth in energy demand will come from Africa and Asia, however, and Latin America as a region garners relatively little attention in the report. However, the authors dedicate a section to Brazil, South America's largest economy. The report says Brazil will continue to use hydro

> **Renewables will become "by far the fastest-growing fuel source" through 2040.**

and other renewable resources for a large part of its energy needs, making greater use of green sources of energy than any other country or region covered in the report. In 2016, 42 percent of the energy consumed in Brazil came from hydro and other renewables (29 percent hydro and 13 percent wind, solar and biofuels). By 2040, this share increases to 47 percent due to a doubling in the use of biofuels, a 30 percent increase in hydro output and substantial increases in wind and solar.

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ing administrative and production costs and passing savings to the consumers (refer to the California model); (3) investing in new solar and wind generating assets while doing away with the obsolete oil-burning plants in Palo Seco and Costa Sur; (4) decentralizing the island's energy grid (essential if we are to successfully survive future natural disasters such as Hurricane Maria); (5) acquiring, on an ongoing basis, new technologies with which to keep up the resilience of the island's energy landscape, among other measures. A close perusal of the region (e.g. Chile and Colombia) shows that a sensible mix between the right type of privatization (if looked at in light of the peculiarities of the specific jurisdiction), and a reasonable amount of regulation, does lead to higher degrees of energy cost efficiency and, thus, to increased levels of investment and ultimately more robust rates of economic growth. Whether Puerto Rico will get there in the near future remains to be seen."

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Efraín O'Neill-Carrillo, professor in the Electrical & Computer Engineering Department and director of the Power Quality & Energy Studies Laboratory at the University of Puerto Rico-Mayagüez: "Strong economic forces have been behind this for years. However, Puerto Rico's credibility is at its lowest point in decades. The threats to dilute the regulatory framework, restructuring plans and the sale of assets have created much uncertainty and have increased investment risk. However, Title V of the Promesa Act, which the U.S. Congress approved, encourages critical projects based on private generation. Financial difficulties have become an excuse to expand fossil-fuel dominance. Two failed privatization efforts in the Puerto Rico Aqueduct and Sewer Authority proved that private management does not necessarily solve infrastructure-related ailments. Even if billions of dollars are poured into the electric infrastructure, the electricity sector

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ECONOMIC NEWS

Argentina's Trade Deficit Widens in January

Argentina's government on Wednesday posted a $986 million trade deficit for the first month of 2018. Exports reached $4.75 billion in January, but imports surged to $5.74 billion, according to state statistics agency INDEC. The trade deficit increased 10.7 percent over the same month last year. The trade gap was larger than expected and suggests the current account deficit could rise above $30 billion, which is approximately 5 percent of the country's gross domestic product. "This would be the highest deficit since the 1990s," Goldman Sachs analyst Alberto Ramos said in a research note. Buoyed by stronger prices for soy and other products, the economy grew "close to 2.8 percent" last year, Guido Sandleris, head of the advisory body to Argentina's Treasury Ministry, told Japanese investors on Monday, Reuters reported. Sandleris said the government expects the economy to grow 3.5 percent this year. INDEC is scheduled to release its final figures for 2017 economic growth in four weeks. However, Ramos cautioned that despite a real business cycle recovery, government spending adjustments are needed in light of the trade data. "The significant deterioration of the current account ... is a source of growing concern and makes it even more imperative to deepen the fiscal adjustment," Ramos said. In related news, tens of thousands of truckers and supporters of Argentina's powerful CGT labor union turned out Wednesday in Buenos Aires to protest government austerity measures being advanced by right-of-center President Mauricio Macri, La Nación reported. Organizers are calling for higher salary increases in the face of persistent inflation and an end to worker layoffs. A key difference between this week's march and similar protests in the previous administration of Cristina Fernández de Kirchner has been the strong presence of leftist groups and social movements in addition to trade unions, the newspaper reported.

ADVISOR Q&A

Would an AMLO Presidency Hurt Mexico?

Q Leftist Mexican presidential hopeful Andrés Manuel López Obrador remains the front-runner ahead of the country's July presidential election, according to recent polls. A survey published in early February by polling firm Parametria showed López Obrador, widely known as AMLO, with 34 percent support, 11 percentage points against his closest rival, Ricardo Anaya of the National Action Party, or PAN. If López Obrador becomes Mexico's next president, what types of economic policies can be expected of his government? What actions would he likely take on energy sector liberalization and on NAFTA, if there is still no deal by then on the trade accord's renegotiation? How would his administration change Mexico's business climate, and how would international markets respond to his election?

A Pamela Starr, senior advisor at Monarch Global Strategies: "AMLO's five-to-11-point lead in five major polls may not be wide enough to ensure his victory on July 1, but it is wide enough that markets should begin to take notice. And yet, markets still have not begun to price in this possibility. Indeed, the vast majority of Mexican businessmen continue to operate on the assumption that he will lose, even as they fear his victory. Should AMLO's lead hold up, capital flight and an associated fall in the peso/dollar exchange rate could be significant in the weeks surrounding election day. But an AMLO government would not necessarily be bad for business. AMLO is not a wild-eyed populist. This was demonstrated by his tenure as Mexico City's mayor. Also, his shadow finance minister is a moderate, and his economic policy platform would have qualified as conservative in Mexico 40 years ago. He has promised to increase the state's role in the economy, but with the aim of strengthening the Mexican private sector within a capitalist context while also fighting poverty and inequality. In the energy sector, he knows he cannot reverse the reform, as much as he might like to. This will generate a lot of noise in the form of a referendum and audits, but the real policy change is likely to refocus the reform away from exploration and production auctions in favor of efforts to revive Pemex's fortunes. On NAFTA, AMLO accepts it as established fact recognizing its importance to the Mexican economy. He is unlikely to intentionally threaten it."

A Tapen Sinha, professor of risk management at the Instituto Tecnológico Autónomo de México and professor at the University of Nottingham Business School: "AMLO has softened his public discourse. In the past, he raved against ending Pemex's monopoly in the oil business, signaled that he would cancel the new airport in Mexico City and the individual pension system introduced in 1997, and cancel NAFTA, among other things. However, his rhetoric is considerably subdued this year. AMLO's picks for his economic team include Carlos Urzua, who has a Ph.D. in economics from the University of Wisconsin, and Graciela Márquez, who has a Ph.D. in economic history from Harvard. AMLO's announced cabinet has equal numbers of men and women. It would be hard to reverse the end of Pemex's monopoly, as he will simply not have enough votes in Congress..."

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

NEWS BRIEFS

Colombian Military Boosts Security After Looting of Supermarkets

Colombia's military on Wednesday stepped up security after mobs over the past 48 hours smashed windows and looted goods at 16 supermarkets that the government has accused of being fronts for hiding assets of former FARC rebels, Reuters reported. Prosecutors on Monday declared they would confiscate 60 Supercundi stores and other assets valued at $228 million that the FARC did not declare when it signed its peace accord with the government in 2016. The stores are located in Tolima, Quindío and Cundinamarca, as well as in the south of Bogotá, El Tiempo reported.

Peruvian Court Orders Fujimori to Stand Trial

A Peruvian court on Monday ordered former President Alberto Fujimori to stand trial in a case involving the killings of six farmers in 1992, during his presidency, Agence France-Presse reported. Fujimori had been serving a 25-year prison sentence when current President Pedro Pablo Kuczynski pardoned him in December, citing his poor health. However, the National Criminal Court ruled on Monday that the pardon did not apply to the case involving the farmers' murders.

Mexico Helicopter Crash Kills 13 People

Thirteen people, all on the ground, were killed Feb. 16 when a military helicopter crashed in southern Mexico as officials were surveying damage from the 7.2-magnitude earthquake that struck the country earlier in the day, The Wall Street Journal reported. Fifteen others were injured. The helicopter, which was attempting to land in the town of Santiago Jamiltepec, was carrying Mexican Interior Minister Alfonso Navarrete and Oaxaca Governor Alejandro Murat. Neither were badly injured.

POLITICAL NEWS

Venezuelan Opposition to Boycott Election

Venezuela's opposition alliance said Wednesday that it would boycott the country's planned presidential election in April, saying the vote is rigged in favor of President Nicolás Maduro and his socialist party, The New York Times reported. With the opposition fractured and its top leaders detained, barred from running for office or driven into exile, Venezuela's pro-government Constituent Assembly last month scheduled the country's next presidential election for April, a decision that the country's electoral commission later confirmed. The decisions also came without any agreement from government and opposition negotiators engaged in talks to determine how to conduct the election fairly. In a statement, the Democratic Unity Roundtable coalition said the election was "premature" and did not have the "proper conditions," adding that it amounted to "a show by the government to give an impression of legitimacy that it does not have in the midst of Venezuelans' agony and suffering." Following the announcement, Maduro vowed to hold the election on April 22 and also said he would ask the Constituent Assembly to call general elections on that date for the election of members of the currently opposition-controlled National Assembly, as well as for municipal and state officials. If the opposition indeed boycotts the elections, Maduro and his party would control virtually all of the country's elected offices. The opposition's boycott has left Javier Bertucci, a little-known evangelical pastor, as the only confirmed presidential candidate other than Maduro, The New York Times reported. Maduro's move to hold legislative, state and municipal elections on the same date amounts to "a total renovation of the institutions, knowing that there is no possibility of the opposition obtaining any relevant position," Luis Vicente León of Venezuelan polling firm Datanálisis, told the newspaper.

> **Maduro and his party would control virtually all elected offices.**

Brazil's Congress Approves Policing by Military in Rio

Brazil's Congress on Tuesday approved a presidential decree to place the military in charge of the security forces in Rio de Janeiro, which has been facing rising levels of crime, the Associated Press reported. The Senate approved the measure shortly before midnight, following similar action by the lower house earlier in the day. President Michel Temer issued the decree last week, and the military took over Rio's police force on Feb. 16, but the action still needed congressional approval. In opening the debate, the lower chamber's president, Rodrigo Maia asked lawmakers to support the measure, the Rio Times reported. "We are living a war on crime, and the Constitution is our weapon," said Maia. However, lawmaker Chico Alencar, a member of the PSOL party and a deputy for Rio, sought to postpone the vote, arguing that there was not enough information about the financial resources available for the operation. The measure was approved following seven hours of debate. On Monday night, the armed forces fanned out in Rio in their first major operation since Temer issued the decree. Soldiers were positioned on major roads that connect the city with the rest of the country as part of an effort to keep illegal weapons, drugs and stolen goods from entering Rio de Janeiro, the AP reported, citing Col. Roberto Itamar, a military spokesman. Some 3,000 members of the military were involved in the operation. Armored vehicles also rolled through at least one neighborhood in Rio, while boats were seen patrolling the waters. Soldiers and police searched people entering and leaving the city on Tuesday morning. By Tuesday night they had detained 11 people and had seized six guns, six grenades and a large quantity of drugs, according to Rio's state security department.

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may end up in the same place, or worse, because the electricity challenge in Puerto Rico is mainly social, not technological or economic. If Puerto Ricans cannot agree on minimal, common principles for the future of the electric power infrastructure, it will be very difficult to establish needed appropriate policies and regulatory framework needed that can withstand changes in the governing party. An alternative to fossil-based privatization is facilitation of an aggressive increase in the use of residential, commercial and industrial rooftops to generate solar power. Those systems would be private, but they would empower users to take hold of their energy future. They support local socioeconomic development, whereas large power plants would continue siphoning money out. Any improvements to generation should be made to existing power plants in places that are already environmentally affected, giving the government leverage in negotiations with potential investors. New, more flexible generators should be placed in existing sites and given a new role: facilitation of an increased use of renewable energy. However, there are no spaces to have a civilized, rational discussion about these and other options."

A **Julián Herencia, executive director at the Association of Producers of Renewable Energy (APER) in Puerto Rico:** "Other than the Puerto Rico Telephone Company, the territory has a dismal record in its attempts to privatize its public corporations. PREPA's privatization will only succeed if it is planned and executed thoughtfully and with utmost transparency. Success is relative to the achievement of its intended goals. As such, a clear vision of the future state of the industry, or what it can't become, should be outlined. First, moving from a public to a private monopoly would be the worst outcome for Puerto Rico. Should we ask why private generation proposals continue to be held back after receiving tacit support from multiple governmental agencies and sectors? Second, the privatization process must occur on a level playing field, enabling a healthy competitive environment and a diverse source of suppliers. Third, we must end up with diversified energy sources and multiple suppliers from which consumers in Puerto Rico can select, including on-site generation. Fourth, the Puerto Rico Energy Commission must be a truly independent body with full authority to regulate the industry and drive change, modernization and continuous improvements. Its authority must not be eroded in any way, much less by political motivations or appointees with minimal credentials. Puerto Rico scored a big win with the creation of this regulatory body. Its independence, the objective designation process, as well as the technical and professional robustness of its commissioners are paramount. Fifth, there can't be automatic price increases. Price determination ought to be the result of due process through the Energy Commission. Finally, with regard to risk and finance, if the mechanisms are not created to bring risk and return on investment to acceptable and competitive levels, privatization will never succeed."

> **"The territory has a dismal record in its attempts to privatize its public corporations."**
>
> **—Julián Herencia**

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

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