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FEATURED Q&A

Is YPF Struggling Amid Argentina's Economic Turmoil?

Argentine state oil company YPF saw disappointing production results in the first quarter of this year. // File Photo: Argentine Government.

Q **YPF is focusing on shale oil development with the aim of reversing an expected 3 percent decline in overall output this year, the Argentine state-controlled company said in May. The firm's overall hydrocarbon production dropped 11.5 percent in the first quarter of this year, as compared to the same period a year earlier. How is YPF faring amid Argentina's economic turmoil? What are the reasons behind the fall in output in the January-March period and the negative forecast for this year? Will focusing on shale oil be enough to help reverse the expected decline, and what other steps should YPF take to increase production?**

A **Isabella Alcañiz, associate professor at the Department of Government and Politics of the University of Maryland:** "Argentina's economic crisis has been hard on YPF. The devaluation of the peso, the economic recession and rate increases have all led to a contraction of energy demand, which in turn has been particularly hard on the state-owned oil company. As with so many of President Macri's problems, the challenges facing YPF result mostly from the government's own miscalculations and over-optimistic forecasts. The energy sector, especially shale oil and gas, was to be the engine of economic growth and a magnet for investment, according to the Cambiemos administration. Instead, it appears to be a weather vane of Argentina's most recent crisis. In 2017, President Macri adopted a program of selective subsidies to stimulate the sector, which benefited the private Techint over YPF and had the effect of increasing the overall supply of shale oil and (especially) gas. Facing decreased consumer

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Mexico City to Use Solar Power in Bid to Curb Pollution

The capital city's local government launched an initiative to promote the use of renewable resources with the aim of avoiding the emission of as much as two million metric tons of carbon dioxide.

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The Inter-American Development bank will finance and monitor the process to merge Ecuador's state oil companies.

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OIL & GAS

Charges Filed Against Former Pemex CEO

Authorities in Mexico have filed corruption charges against Emilio Lozoya, the former chief executive officer of state oil company Pemex. Lozoya led the company from 2012 to 2016.

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Lozoya // File Photo: Mexican Government.

OIL AND GAS NEWS

Mexican Authorities File Charges Against Former Pemex CEO

Investigators in Mexico said Tuesday that they have filed corruption charges against a former head of Pemex, Emilio Lozoya, The Wall Street Journal reported. The case against Lozoya, who served as CEO of the state oil company from 2012 to 2016, marks the first high-profile corruption investigation launched by the administration of President Andrés Manuel López Obrador, whose term began in December. Last week, Mexico's Secretariat of Public Administration (SFP) slapped Lozoya with a 10-year ban on holding public office, saying he provided "false information" about his assets, El Financiero reported. A Mexican judge on Tuesday issued an arrest warrant for Lozoya, who also faces tax fraud and bribery charges, according to Santiago Nieto, head of the Finance Ministry's financial intelligence unit. Meanwhile, Spanish authorities on Tuesday detained the chairman of a top Mexican steelmaker as part of the probe into Pemex. Alonso Ancira, chairman of Altos Hornos de México, or Ahmsa, was arrested when he arrived on the Spanish island of Mallorca on his company's private jet, according to Spanish media. Part of the probe is connected to the sale of a fertilizer plant by Ahmsa to Pemex in 2014 for approximately $273 million. Mexico's current government says the plant was only worth about $50 million. Investigators allege that, in exchange for a higher price on the plant, Ahmsa funneled some $3.5 million to Lozoya through a shell company set up by Brazilian construction firm Odebrecht. The Brazilian company declined to comment on the case. Ahmsa confirmed Ancira's arrest in a statement, which also denied any wrongdoing by him or the company. Nieto's team also ordered a freeze on the bank accounts of Ahmsa, Ancira and Lozoya, as well as some of Lozoya's family and former aides, The Wall Street Journal reported. In a statement, Ahmsa denied any responsibility for wrongful acts and called the government's action "unprecedented, arbitrary and a violation" of its rights, Reuters reported. The company "denied all responsibility regarding the improper acts" attributed to the firm.

Emilio Lozoya was CEO of Pemex from 2012 to 2016.

Merger of Ecuador State Oil Companies to Cost $20 Million

The process to merge Ecuadorean state oil companies Petroamazonas and Petroecuador into one firm will be financed and monitored by the Inter-American Development Bank, and it will cost $20 million, El Comercio reported Wednesday. The Andean country has created a temporary commission dubbed Unidad Temporal de Fusión to manage the merger, which is to conclude in late 2020, according to Ecuador's oil ministry. The commission, which former energy minister Diego Tamariz will lead, will set up a team of experts in different technical and management areas to lead the process. The team has fewer than 10 people, Energy Minister Carlos Pérez said. Tamariz added that Ecuador would launch an international bid to hire a consulting firm with a specialized focused on company mergers. The $20 million, which the IDB will provide, will go into the hiring costs of such a firm, El Comercio reported. Before 2010, Ecuador had just one state oil company, Petroecuador, of which Petroamazonas was a subsidiary. Petroamazonas currently handles exploration and extraction of hydrocarbons and related substances in Ecuador, while Petroecuador explores for and produces oils, as well as owns and constructs oil pipelines, according to Bloomberg. "The merger of oil companies will be done with an emphasis on areas that duplicate functions and operational activities will not be affected," the ministry said in announcing the move last month, according

NEWS BRIEFS

Petroperú Eyeing Sale of Up to $1 Billion in Assets at Talara Refinery

Peruvian state-owned oil company Petroperú is considering the sale of some units at its Talara refinery, said Carlos Paredes, who was appointed president of the company's board last month, Reuters reported. Petroperú hopes to raise as much as $1 billion to help finance a major, unfinished expansion of the facility to raise its capacity to 95,000 barrels of oil per day (bpd) from the current 65,000 bpd. The company had previously planned to sell bonds to close the financing gap for its $4.7 billion expansion of Talara, but Paredes says the company's debt is too big as it is.

Citgo in Talks With Aruba Over Refinery Contract

Citgo Petroleum, the U.S. subsidiary of Venezuelan state oil company PDVSA, said on Tuesday it's in talks with the government of Aruba over its oil refinery operating contract, Reuters reported. A day earlier, Aruba said it would create a committee to decide on the future of its Citgo refining plant. Aruba Prime Minister Evelyn Wever-Croes said on Monday that she expects to either overhaul or terminate the contract.

Sonnedix Closes Deal to Finance 171 MWp Solar Project in Chile

Independent solar power producer Sonnedix Power said Wednesday that it had closed a $99 million financing deal for a 171 megawatt-peak (MWp) solar project in Chile, Renewables Now reported. The financing was arranged with the CAF-Development Bank of Latin America, Argentina's Development Bank of Investment and Foreign Trade, or BICE, and Chilean bank Banco Security. The photovoltaic plant will be the second-largest of its kind in the South American country. It is expected to generate some 470 gigawatt-hours of electricity per year.

to the Houston-based Energy Analytics Institute. "The optimization of state resources and more efficient work is sought in the merger," it added. Pérez has said the goal is to have one oil company in charge of all exploration, exploitation, production, transport, refining and commercialization of crude and its derivatives by Jan. 1, 2021.

Brazil Supreme Court Judge Suspends Sale of Petrobras Units

A Brazilian Supreme Court judge has issued an order suspending some sales of state oil company Petrobras, Reuters reported Monday, citing a court document. The decision, which Justice Edson Fachin issued on May 24, calls for the suspension of the divestment of Petrobras' TAG pipeline unit and eight of the companies' refineries, as well as the sale of its fertilizer unit, Araucária Nitrogenos. The company said in a statement that it would evaluate the decision and take action to defend its interests and those of investors as necessary, adding that the divestment plans were key to reducing Petrobras' debt. The TAG pipeline unit sold for $8.6 billion, and Petrobras expects the refineries to bring in some $15 billion. Fachin ruled the sale of Petrobras' refineries must be carried out in an auction format and with congressional approval. The decision was in response to a lawsuit brought by an oil workers union, which celebrated the ruling as "a new victory" in its efforts to stop the privatization of Petrobras, Reuters reported.

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demand—because of Argentina's economic crisis—and the loss of its subsidies, YPF responded by shutting down some of its production. As demand has not picked up, YPF continues producing at a loss. The broader situation isn't much better, although YPF should no longer feel singled out by the administration with regard to subsidies. Due to an austerity agreement President Macri signed with the IMF, all subsidies to shale oil and gas companies are being reviewed or outright cut. With a worsening economy and the presidential election in October, YPF has little leeway to navigate its decline in the near future."

A Gerardo Rabinovich, second vice president at Instituto de la Energía "General Mosconi" in Buenos Aires: "The criteria that YPF adopted in its strategic plan privileges the production of shale oil over that of shale gas. This is the correct strategy, given past experience and the development of new areas, where it is obtaining around 50,000 barrels per day, about 10 percent of Argentina's oil production, confirming the quality of the resource. Exporting surpluses to international markets will allow the company to obtain cash flow to finance the massive development of shale fields in Vaca Muerta. Production of shale gas has major barriers, due to the fall in demand in the domestic market and to a lack of competitiveness in international markets. The short-term and interruptible exports to regional markets allow for better commercialization of natural gas production and for higher revenues to continue with the massive development of the Vaca Muerta deposit. A combination of unfavorable prices, a sharp drop in demand and political uncertainty during this election year could explain YPF's declining performance in the first quarter. These are conjunctural phenomena that can be overcome by the company's successful strategy, focused on oil production and the indubitable quality of shale oil deposits, as well as past lessons, which allow for a moderate optimism with regard to the recovery of production. YPF will be in good health within a scenario in which the governing coalition avoids the return of populism and achieves a new period of management."

> **"Unfavorable prices, a sharp drop in demand and political uncertainty ... could explain YPF's declining performance."**
> **— Gerardo Rabinovich**

A Víctor Bronstein, director of the Centro de Estudios de Energía, Política y Sociedad (CEEPYS) in Buenos Aires: "YPF's negative results can't be attributed only to Argentina's economic crisis. The country's energy sector has dollarized prices aligned with those of the rest of the world. Producers' price per barrel of oil use Brent

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RENEWABLES NEWS

Mexico City to Use Solar Power in Bid to Counter Pollution

The government of Mexico City on Saturday announced a new program, called Ciudad Solar, to promote the use of renewable resources with the aim of curbing carbon dioxide emissions, El Universal reported. The program will have a total investment of 12 billion pesos ($626 million) per year. The World Bank will provide nearly 600 million pesos for the project, and the remainder of the funds will come from the Inter-American Development Bank and Mexican government-owned development bank Nacional Financiera, or NAFIN, and the Mexico City government. Mayor Claudia Sheinbaum said the goal was to avoid carbon dioxide emissions of two million metric tons. As part of the initiative, the capital city will add up to 350 megawatts of green capacity over the next five years through the installation of solar heaters and solar photovoltaic systems across homes and businesses between 2019 and 2024, Renewables Now reported. Approximately 10,000 micro-enterprises and homes as well as 300 city government buildings are to be included in the project with installations of photovoltaic systems of below 500 kilowattpeak. In addition, the program will install 150 megawatts of new capacity from photovoltaic systems bigger than 500 kilowattpeak, according to the report. The initiative will also include bioenergy and energy efficiency projects and one three-megawatt mini-hydropower plant.

POLITICAL NEWS

Talks End Between Venezuelan Gov't, Opposition

Talks between Venezuela's government and the opposition ended Wednesday in Norway without any agreement other than both sides saying they were open to future talks, the Financial Times reported. President Nicolás Maduro and opposition leader Juan Guaidó had sent envoys to Oslo to meet face-to-face. The talks were the first since Guaidó swore himself in as the country's acting president in January. The opposition argues that Guaidó, the leader of the National Assembly, is the country's legitimate interim president, saying Maduro's re-election last year was fraudulent. The United States and dozens of other countries recognize Guaidó as president, but Maduro maintains the support of Venezuela's military. "This meeting ended without agreement," Guaidó's team said after the talks ended Wednesday in Oslo. "We thank the government of Norway for its willingness to contribute to a solution to the chaos that our country is suffering." Maduro's government did not comment on the end of the talks. On Tuesday, the E.U. foreign policy chief, Federica Mogherini, named former Inter-American Development Bank President Enrique Iglesias as the European Union's special advisor for Venezuela. Iglesias is an economist and a former Uruguayan foreign minister. In a rare move earlier this week, Venezuela's central bank said the Andean nation's economy contracted 19.2 percent in the first nine months of 2018 as compared to the same period a year earlier, The Wall Street Journal reported. The last time the country's central bank released economic statistics was for 2015. The central bank also said inflation was 130,060 percent in all of 2018. While that figure is the world's highest rate of inflation, it is far below estimates from private economists and the International Monetary Fund. The IMF said in April that Venezuela's inflation totaled 929,790 percent last year, and it said last October that it expected inflation to reach 10 million percent this year. The IMF also said last month that the economy contracted 18 percent last year and would shrink another 25 percent this year. Some economists said

ADVISOR Q&A

Why Does Brazil's Economy Continue to Struggle Along?

Q Brazil's government is cutting its 2019 growth forecast to 1.5 percent, down from 2.2 percent, Economy Minister Paulo Guedes said May 14, adding that it is asking the country's development bank, BNDES, for additional funding of as much as 240 billion reais ($60 billion) in order to meet current expenditures without resorting to issuing debt. Moreover, central bank data suggests real activity in March declined for the third consecutive month and by larger than expected, on top of activity declines in January and February. What is behind the government's lowered forecast for economic growth this year, and why does it differ from previous estimates? Which sectors are most likely to take a hit, and why? Is supplementary funding from BNDES enough to help the government meet its budget goals?

A Armando Castelar Pinheiro, coordinator of applied economics at Fundaçao Getúlio Vargas' Instituto Brasileiro de Economia and former head of the economics department at BNDES: "Three key factors caused the government to lower its growth forecast. One was the weaker-than-expected numbers for the economy in the first quarter, likely a result of tight financial conditions in the last two quarters of 2018. The other is the rise in geopolitical risk, which will further slow the global economy and raise risk aversion, harming emerging markets. Finally, optimism declined about the pace and size of social security reform, lowering consumer and business confidence, leading to a less substantial rise in private domestic demand. Manufacturing and construction are to perform particularly poorly this year—the former due to the combined effect of weak domestic demand and falling exports, on account of Argentina's recession and the slowdown in international trade more generally. Construction is suffering from the drop in public investment and the large inventory of empty houses. The money from BNDES will be used to redeem government debt, thus preventing a sharper rise. It will not be used to directly finance the deficit. The government expects BNDES to pay around 126 billion reais, slightly less than 2 percent of GDP. The overall public sector deficit ranges around 7 percent of GDP."

> **"Optimism declined about the pace and size of social security reform."**
> **— Armando Castelar Pinheiro**

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

NEWS BRIEFS

Judge Rules Bolsonaro's Attacker is Mentally Ill, Shouldn't Be Jailed

A Brazilian judge on Monday ruled that the man charged with stabbing President Jair Bolsonaro during a campaign event last September should not be punished because he is mentally ill, the Associated Press reported. Federal Judge Bruno Savino said Adélio Bispo de Oliveira cannot be jailed and should be put in a mental facility. Bolsonaro suffered serious internal bleeding from the wound in his abdomen. Bolsonaro has said de Oliveira had been part of a plot to stop him from winning the presidency.

Twenty-One Killed in Crash of Bus, Tractor-Trailer in Mexico

A bus carrying Catholic pilgrims collided with a tractor-trailer in the Mexican state of Veracruz on Wednesday morning, killing 21 people and injuring 30, The New York Times reported. The bus, heading to Chiapas from Mexico City, crashed into the tractor-trailer, flipped over and burst into flames. There was some initial confusion over what caused the accident, but the Veracruz Secretariat for Civil Protection said Wednesday that the tractor-trailer's brakes apparently failed. Authorities are still investigating the accident.

Measure to Weaken Amazon Environmental Laws Fails in Brazil

An attempt to weaken protection of the Amazon forest has failed in Brazil, Reuters reported Wednesday. Government whip Fernando Bezerra said that a temporary presidential decree that required congressional approval by Monday will not be voted on before then. The measure would have extended by a year the deadline for landowners to replant minimum forested areas on their properties.

that the central bank's release of the economic data was an acknowledgment that Maduro's government and that of his mentor and late predecessor, Hugo Chávez, decimated the country's economy. Maduro's government frequently blames the opposition and the United States, which has imposed multiple rounds of sanctions on Venezuelan officials and entities, for the country's economic devastation.

Colombia's Supreme Court Orders Release of ex-FARC Leader

Colombia's Supreme Court on Wednesday ordered the release of former FARC rebel leader Seuxis Hernández, also known as Jesús Santrich. Hernández, who is wanted in the United States on cocaine trafficking charges, was released earlier this month by a special tribunal before being immediately rearrested on what the attorney general's office said was new evidence. However, the Supreme Court ruled Wednesday that since Hernández is recognized as a member of the Colombian Congress, the Supreme Court must hear his case.

ECONOMIC NEWS

Nationwide Strike Shutters Businesses in Argentina

Argentine unions held a nationwide strike on Wednesday, causing banks to close, airlines to ground planes and a soccer final to be postponed as anger over the country's dire economic situation grows, The Wall Street Journal reported. CGT, Argentina's largest trade union, launched the one-day strike to protest President Mauricio Macri's economic management, as inflation hit 56 percent last month, among the highest rates in the world. The economy contracted 6.8 percent in March. "Every day, people are worse off ... It's a disaster what's happening," union leader Hugo Moyano told The Wall Street Journal. "If [Macri] doesn't understand that, then it's evident he doesn't have the capacity to govern our country." Public transportation was shut down across the country, and some public and private schools did not open as teachers participated in the strikes, but businesses in several cities remained open as usual, La Nación reported. Outside of Buenos Aires, ports that export grains were closed. The strike, the fifth such nationwide protest since Macri took office in 2015, will cost the economy approximately $900 million, according to finance ministry estimates. Security Ministry Patricia Bullrich said the strike was politically motivated and an attempt to hurt the government ahead of the October presidential election. [Editor's note: See related **Q&A** in Thursday's issue of the daily Latin America Advisor.]

López Obrador Vows to Fight Medicine Shortage

Mexican President Andrés Manuel López Obrador on Monday promised to alleviate a medicine shortage in public hospitals, saying he would purchase essential drugs abroad if necessary, and he blamed the situation on companies upset about his measures against overpricing, Reuters reported. Last week, the government promised to release nearly $126 million to help alleviate shortages at Mexican public hospitals following the resignation of Germán Martínez, the head of the Mexican Social Security Institute, over budget cuts to the public health system, the Associated Press reported. "There is a problem of medicine shortages, but I'd tell you it was worse before," López Obrador said last Friday, adding that his government is reviewing contracts with medicine suppliers for signs of corruption, El Universal reported. López Obrador says the crackdown on overpricing, which he says was rampant under the previous government, has upset some companies. Health Minister Jorge Alcocer said some firms, which he did not name, had not responded to government tenders for drugs. Last month, López Obrador announced that three Mexican companies would be excluded from future public tenders.

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values as reference. Moreover, the value of gas at the wellhead, which the government still sets, has an average value of $4.50 per million British thermal units and $7 for unconventional gas from Vaca Muerta. In any case, the country's situation affected a very small percentage of the results in terms of gas production, since Argentina does not yet have a strong structure with export capacity, and domestic consumption decreased because of the crisis, forcing lower production in the summer months. Downstream saw a decrease in consumption of fuels, and their price in dollars dropped, since the currency's devaluation could not be transferred in its entirety to consumers. Today, the price of naphtha super—which is used as a global reference—is around 93 cents, when historically it has been about $1.10. YPF's production decline occurred mainly in gas production. This is mostly due to the decline of the Loma La Lata deposit, the most important in Argentina, whose production fell from 14 million cubic meters per day to 8.5 million cubic meters per day. In the short term, YPF's strategy to focus on shale development in Vaca Muerta is the correct one, given that, in the last 30 years, no new reserves of conventional resources have been discovered, and the deposits in production are in decline. Since making the correct strategic decision in 2010 when the shale revolution had just begun in the United States, YPF brought many areas of Vaca Muerta under its wing. Today, the company manages 40 percent (12,000 square kilometers) of the Vaca Muerta formation. In the medium term, YPF should be progressing more intensively in the exploration of offshore areas in Argentina—it is forecast to have significant resource potential."

A **Amanda Kupchella, upstream Latin America research analyst at Wood Mackenzie:** "The 11.5 percent decrease in YPF's production in the first quarter of this year in comparison to the same quarter last year was related to an oversupplied gas market. While the company's oil production has held constant in the past year, YPF has been forced to cut gas production due to a lack of demand. The country's unconventional gas production has grown exponentially in recent years, leading to an oversupply during the low demand summer season this year. The national oil company plans to shift investment from unconventional gas to tight oil. It has recently sanctioned several major shale oil projects, including a second phase of development at its flagship Loma Campana. Oil production growth from the new developments will balance decreases in gas production in the medium term. Several new project sanctions per year will be required to maintain growth in the longer term."

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

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