LATIN AMERICA ADVISOR

ENERGY ADVISOR

A WEEKLY PUBLICATION OF THE DIALOGUE

www.thedialogue.org

July 26, 2019

FEATURED Q&A

How Much Have Six Months of Sanctions Hit Venezuelan Oil?

Venezuelan state oil company PDVSA's exports have fallen by more than one-fifth since January, when U.S. sanctions against it came into effect. // File Photo: Venezuelan Government.

Q **Nearly six months after the administration of U.S. President Donald Trump slapped sanctions on Venezuelan state oil company PDVSA, the South American country continues to struggle to find new buyers, with PDVSA's exports plummeting by more than a fifth since January. What are the most important ways in which U.S. sanctions have affected Venezuela's oil sector, and what other indirect consequences have they had for the country and for global oil dynamics? To what extent have the U.S. sanctions succeeded at advancing the Trump administration's objectives in Venezuela, and how much are they responsible for the oil sector's decline? What are the prospects for PDVSA's production and sales in the months ahead, and what measures can the company take to boost its performance?**

A **Francisco Rodríguez, managing director and chief economist at Torino Economics in New York:** "The evidence indicates that the bulk of the decline observed since January in oil production is due to U.S. oil sanctions. The data shows a very clear change in trend in January, with the rate of decline tripling since then. The 36 percent drop is in line with estimates of the effects of oil sanctions on production obtained from panel data estimates (41-45 percent). Its absolute magnitude of 422,000 barrels per day (bpd) is also similar to the loss in the U.S. oil market (426,000 bpd). I have recently studied the effect of the 2017 financial sanctions using several econometric methodologies, valuing the resulting loss in production at $17 billion a year. This year's oil sanctions will add another $10 billion a year in losses to an already decimated oil industry. The Trump administration's

Continued on page 3

TOP NEWS

RENEWABLES

Bunge, BP to Team Up With Ethanol Venture in Brazil

Bunge and BP announced that they will merge their sugar and ethanol operations in Brazil.

Page 3

OIL & GAS

Projects Awarded Under Mexico Reform Show Output Growth

Projects contracted after Mexico's 2013 energy reform have been showing a steady growth in oil and natural gas production, according to CNH figures.

Page 3

ELECTRICITY

Maduro Blames U.S. For Massive Power Outage

Venezuelan President Nicolás Maduro claimed the United States caused a nearly nationwide power outage on Monday through an "electromagnetic attack," without providing further details or evidence. At least 19 of Venezuela's 23 states, were left without electricity for several hours.

Page 2

Maduro // File Photo: Venezuelan Government.

POWER SECTOR NEWS

Cuba Says Fuel Shortages, Outages Are Temporary

Cuba is temporarily experiencing fuel shortages due to higher consumption and an increase in the number of cars on the road, state-run oil company Cubapetróleo said on July 19 following denials by the government last week that the Caribbean nation was suffering outages due to a lack of fuel on the island, Reuters reported. A shortage of regular and special gasoline, mostly concentrated in Havana, have led to long lines at gas stations as a result of problems with distribution, said Tomás Pérez Álvarez, who heads the sales division at Cubapetróleo, Reuters reported. The shortages were due to consumption increasing as much as 10 percent as compared to the summer period last year and a greater number of cars on the road, he said, adding that the distribution of diesel and motor gasoline remains stable. Pérez said he expects normal distribution to resume this week. The shortages come as Cuba has been facing a steady decline in supply since 2014, given the ongoing economic crisis in key ally Venezuela, as well as increasing economic pressure from tightened sanctions under the administration of U.S. President Donald Trump. Energy and Mines Minister Raúl García said earlier last week that the sporadic blackouts, which were registered in several of the island's provinces, had nothing to do with fuel shortages. García said breakdowns in three of the country's power plants were responsible for the blackouts, in addition to two other plants being down for maintenance, the Associated Press reported.

Maduro Blames U.S. For Massive Power Outage in Venezuela

Venezuelan President Nicolás Maduro on Wednesday blamed the United States for a nearly nationwide blackout in the South American country, which left millions without electricity and paralyzed Caracas' metro system, the Associated Press reported. Maduro claimed the United States had carried out a "high-tech electromagnetic attack" to undermine his government, which the administration of U.S. President Donald Trump, alongside some 50 countries, views as illegitimate. The Venezuelan president did not provide any details or evidence linking the United States to Monday's outages. Maduro's opponents have said Venezuela's outages are a result of corruption and inadequate management over two decades. Power had been restored to most of Venezuela following the Monday afternoon blackout, the latest outage to hit the crisis-stricken South American country, The Wall Street Journal reported. At least 19 of Venezuela's 23 states were without power beginning at around 4:45 p.m. local time on Monday, with around 94 percent of Venezuela's telecommunications infrastructure down and Internet connectivity running at 10 percent nationwide, according to Netblocks, a nonprofit organization that tracks outages, CNN reported. Electricity had been restored in Caracas, and the states of Mérida, Trujillo, Barinas and Aragua had seen a partial return of power by Tuesday morning, according to the government, which also suspended all work and educational activities for the day. There have been some intermittent, short outages in several states since then, including in Caracas and Zulia State near the Colombian border, EFE reported. Maduro said the armed forces had been mobilized to help deal with what he called a "criminal attack against the tranquility and the peace of the homeland." The nationwide blackout is the fourth such outage this year, after three blackouts in March alone left most Venezuelans in the dark for days. [Editor's note: See related **Q&A** in the March 29 issue of the Energy Advisor.]

Maduro claimed the outage was a result of an "electromagnetic attack."

NEWS BRIEFS

Brazil's Bolsonaro Seeks Tighter Control of Deforestation Data

Brazilian President Jair Bolsonaro on Monday called for tighter control of official deforestation data, slamming the government's space research agency, INPE, Reuters reported. The president on Friday had accused INPE of falsifying data after satellite imaging released by the agency showed a surge in the clearing of the Amazon rainforest this year. According to INPE figures, Brazil's Amazon this month has seen the fastest pace of deforestation in years.

Spanish Authorities Investigating Death of Former PDVSA Executive

Authorities in Spain are investigating the death of a former executive at Venezuelan state oil company PDVSA, Juan Carlos Márquez, who had appeared in court last Friday over allegations that he was involved in a money laundering scheme, BBC News reported Tuesday. Márquez was found hanged in the outskirts of Madrid on Sunday, according to Spanish police. He was due to appear in court again on Monday. He had reportedly agreed to collaborate with a probe into corruption at PDVSA.

Mexico Arrests Former Pemex Head of Security on Allegations of Fuel Theft

Mexico has arrested a retired general and former head of security at state oil company Pemex during the administration of former President Enrique Peña Nieto for allegations of fuel theft, the country's attorney general's office said last week, Reuters reported. The office said it had detained "Sócrates H," whom a government source told Reuters was Brigadier Gen. Sócrates Herrera. Reuters was unable to reach him for comment. Herrera's supervisor, Gen. Eduardo León, has also been accused of fuel theft.

RENEWABLES NEWS

Bunge and BP to Merge Ethanol Operations in Brazil

U.S. commodities trader Bunge and British energy company BP will merge their Brazilian sugar and ethanol operations, creating the world's third-largest sugar cane processor, the companies said Monday, Reuters reported. In total, Bunge and BP will manage 11 cane processing plants in Brazil with capacity to crush 32 million metric tons of cane annually. The joint venture opens the door for BP to have a role in Brazil's ethanol market before a new federal policy comes into effect next year with the aim of encouraging the use of biofuels, which can be used interchangeably with gasoline in cars, Reuters reported. "Brazil is the Saudi Arabia of biofuel," Dev Sanyal, BP's head of alternative energy, told Reuters, adding that the new venture was cash-flow positive. The joint venture is the biggest deal in Brazil's bioenergy sector since Royal Dutch Shell teamed up with Cosan to form Raízen in 2011. Only Raízen and Biosev, which is controlled by commodities trader Louis Dreyfus, have a higher processing capacity per year. As part of the agreement, Bunge, which has unsuccessfully attempted to sell its sugar operation in Brazil in the past, will receive cash proceeds of $775 million, which it said it plans to use to cut debt.

OIL AND GAS NEWS

Contracts Under Mexico's Energy Reform Show Growth

Projects contracted after Mexico's 2013 constitutional energy reform are showing steady output growth, Natural Gas Intel reported Wednesday, citing data from Mexico's hydrocarbons agency, or CNH. The agency has so far approved 133 work plans from exploration and production contracts that were awarded under the framework of the reform, which opened up Mexico's energy sector and ended the upstream monopoly of state oil company Pemex, between 2015 and 2018. Investment in the approved projects totals $35.9 billion, according to the report. As of May, crude oil production from the contracted projects amounted to 74,000 barrels per day (bpd), up from an average of 43,000 bpd last year. Meanwhile, natural gas output was 176 million cubic feet per day (MMcf/d), as compared to an average of 54 MMcf/d in 2018. Oil production from these contracts is expected to reach 341,000 bpd in 2026 at its highest point of production, while gas output will peak at 371 MMcf/d in 2012, Natural Gas Intel reported. President Andrés Manuel López Obrador has

FEATURED Q&A / Continued from page 1

strategy of using oil sanctions to prompt regime change was obviously a short-run strategy. It cannot be sustained over time without severely worsening Venezuela's already fragile humanitarian situation. While personal sanctions have contributed to bringing the regime to the negotiating table, economic sanctions, if anything, have had the opposite effect. Opinion surveys strongly show that the majority of Venezuelans oppose economic sanctions, which have enabled the government to shift part of the blame for the country's crisis to the opposition. In coming months, we should see production extend its decline as logistical problems and a lack of foreign currency take an additional toll. In the medium to long term, if the current political status quo remains, the Chinese and Russians are likely to move heavily into the oil industry, including by taking up operations of U.S. and European firms that leave. This may help to stabilize and even achieve a modest recovery in production by next year, but output will at best remain at one million bpd by 2020."

A **Francisco J. Monaldi, fellow in Latin America energy policy and lecturer in energy economics at Rice University's Baker Institute for Public Policy:** "The sanctions implemented in January have had a very significant effect on PDVSA's exports, production and cash flow. Venezuela produced around 1.3 million barrels per day (bpd) in the last quarter of 2018, and it is currently producing around 750 thousand bpd (tbpd) and exporting around 800 tbpd, of which close to 600 tbpd goes to China and India (Venezuela imports more than 100 tbpd). Oil exports to the United States were around 550 tbpd at the end of last year and have dropped to zero in the last couple of months.

> **"The falling trend will continue and could worsen if U.S. companies leave..."**
> **— Francisco J. Monaldi**

PDVSA has had a hard time finding buyers for its extra-heavy crude. Its cash flow has dramatically declined by a combination of the collapse in exports, lower margins in Asian markets and costlier imports of refined products. In addition, most exports to Asia are to repay loans and do not generate cash. Although, after the initial sharp drop, production has had a more gradual decline trajectory, the falling trend will continue and could worsen if U.S. companies leave, in case their U.S. government license to operate in Venezuela is not renewed before the end of July. Since Venezuelan imports of food and medicine depend on oil export revenues, the humanitarian situation has worsened, and the massive emigration to neighboring countries will continue. If there is no positive resolution to the Venezuelan political crisis, the deterioration of the Venezuelan oil industry will persist and will be harder to reverse. However, in case of a swift political transition, production would recover and could go back to three million barrels within the next decade. That would require a successful oil opening to private investment."

Continued on page 6

criticized the energy reform in the past, instead favoring a strategy to strengthen the highly indebted state company. Last week, Pemex announced a new business plan that in part aims to deal with the firm's nearly $106 billion in debt. However, the plan failed to impress analysts, with Citi Research saying the announced capital injections were "highly underwhelming," Reuters reported.

POLITICAL NEWS

Governor of Puerto Rico Resigns, to Step Down Aug. 2

Puerto Rico Governor Ricardo Rosselló late on Wednesday bowed to several days of protests against his administration and calls from other politicians that he step down, announcing in a video posted online that he would resign, effective Aug. 2. "I was willing to face any challenge, fully understanding that I would prevail against any accusation or process," Rosselló said in the video posted on Facebook, The New York Times reported. However, the governor said he had "heard the demand of the people," adding that continuing in office "would endanger the successes we have achieved." He added, "I hope this decision serves as a call to citizen reconciliation." Before Rosselló's message was broadcast, hundreds of protesters gathered outside the governor's official residence, La Fortaleza, but they suddenly went silent, gathering around cellphones to listen to it, the newspaper reported. The moment that Rosselló said he would step down, the demonstrators erupted into applause and waved Puerto Rican flags. In his resignation speech, Rosselló said the U.S. commonwealth's secretary of justice, Wanda Vázquez, would succeed him when he leaves office on Friday of next week. Vázquez is next in line constitutionally to succeed him because the secretary of state, who would have stepped in as governor, resigned last week due to his involvement in the governor's chat scandal. Rosselló left open the possibility that someone else could be in place to succeed him by the end of next week. In the chat scandal,

ADVISOR Q&A

What Factors Are Holding Back Latin America's Largest Economy?

Q: The lower house of Brazil's Congress on July 10 advanced legislation to overhaul the country's pension system, with a final vote in the chamber expected in August. Lawmakers estimate that the overhaul could save the government $265 billion over 10 years. Just days later, economists in a central bank survey cut their forecast for the country's economic growth next year to a new low of 2.10 percent, with anemic growth of 0.81 percent expected this year. Why are expectations for growth ebbing as the pension reform is advancing? What factors are still holding back Brazil's economy? Which industries will struggle most in coming months, and which will gain strength?

A: Peter Hakim, president emeritus of the Inter-American Dialogue: "The overwhelming support of pension reform in Brazil's lower house was a critical victory for both the Bolsonaro government and the nation's economic prospects. Aside from Dilma Rousseff's impeachment in 2016, no legislative action has gotten more attention in recent years. This was a must-win for the government. Defeat would have signaled to markets worldwide that Bolsonaro's plans to revamp the country's unproductive economic policies were dead in the water and that the recharging of the economy, after a half dozen years of virtually no growth, would again be postponed. Brazilian business leaders along with foreign investors view pension overhaul as a bellwether of the country's economic future. Although three additional congressional votes are needed for this constitutional change, it is widely anticipated that final approval is just a matter of time and that the broader economic reforms essential for stable, long-run growth are now within reach. The immediate reaction to the legislative victory was a jump in the value of the Brazilian real and a new high for the stock exchange. Still, expectations should be held in check. Brazil's mediocre economic performance for much of the last three decades is reason enough for skepticism. The Brazilian Congress, despite its solid backing of the pension legislation, is an erratic institution that could readily change direction. Public reactions to the loss of anticipated retirement benefits remain uncertain. The reform effort could also be upended by the Bolsonaro government's fading support, mostly reflecting the country's sluggish economy and elevated unemployment, but also driven by unpopular policies, offensive statements, questionable choices of senior officials and a few scandals. Nonetheless, the opening legislative success for pension reform should be welcomed, even by those strongly opposed to Bolsonaro and most of his agenda for Brazil."

"Brazil's mediocre economic performance for much of the last three decades is reason enough for skepticism."
— Peter Hakim

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

NEWS BRIEFS

Iran May Reconsider Brazilian Imports Over Ship Refueling Spat

Iran could rethink imports from Brazil if the South American country continues to refuse to refuel two Iranian vessels that have been stuck in Paraná State since early June, Iranian Ambassador to Brazil Seyed Ali Saqqayian said Wednesday, the Associated Press reported, citing Iran's semi-official Fars news agency. Brazilian state oil company Petrobras has declined to supply fuel for the vessels to avoid risking U.S. fines, saying the ships fall under U.S. sanctions against the Middle Eastern country, which Brazilian President Jair Bolsonaro has said he supports. Iran is the largest importer of Brazilian corn.

Cuba Dismisses Study on 'Sonic Attacks'

Cuba's government on Wednesday dismissed a U.S. academic study that showed physical changes in the brains of diplomats who experienced so-called "sonic attacks" while in Cuba, BBC News reported. The study was led by professors at the University of Pennsylvania and published in the Journal of the American Medical Association. Cuba has denied involvement in the incidents.

Mexico's Rate of Inflation Slows in Early July

Mexico's inflation slowed in early July, closer to the central bank's target, with consumer prices moderately higher as compared to the end of June, amid increases in food and transportation costs, the National Statistics Institute said Wednesday, The Wall Street Journal reported. The consumer price index rose 0.27 percent in the first half of the month, pushing annual inflation down to 3.84 percent from 3.95 percent at the end of June. Food and beverage prices were up 0.54 percent as compared to the end of June.

hundreds of pages of messages between Rosselló and his top aides were leaked, in which officials were seen making homophobic, misogynistic and other crass comments, including jokes about victims of Hurricane Maria, which killed nearly 3,000 people on the island in 2017. In recent weeks, federal authorities have also carried out raids targeting associates of the governor, CBS News reported. Even before those incidents, many Puerto Ricans had expressed frustration about ongoing problems, including years of economic weakness. Earlier this week, Rosselló announced that he would not seek re-election next year and that he would step down as the president of his political party. However, that proved not to satisfy protesters, who continued taking to the streets to call for his resignation. [Editor's note: See related **Q&A** in Tuesday's Latin America Advisor.]

ECONOMIC NEWS

Brazil Giving Workers $8 Billion in Effort to Boost Growth

Brazil's government will give workers early access this year to as much as 30 billion reais ($8 billion) in funds usually earmarked for the unemployed as it aims to resuscitate the country's sluggish economic growth, Economy Minister Paulo Guedes said on Wednesday, The Wall Street Journal reported. As of September, the measure will allow Brazilian workers to take as much as 500 reais of money currently in accounts known as FGTS that employers set up by law for workers who lose their jobs. Additionally, as much as 12 billion reais will be released from the accounts in 2020, Guedes said. The government estimates the move could add 0.35 percentage point to GDP growth through next year and that GDP per capita will increase by 2.5 percentage points over 10 years, Reuters reported, citing the economy ministry. "It's a permanent pay rise if you are employed, fight to do your job well and stay employed," Guedes said during a ceremony at the Planalto presidential palace alongside President Jair Bolsonaro and his economic team, Reuters reported. He refuted concerns that Brazilians won't use the funds wisely, saying, "We're giving citizens a choice." He said the initiative is a long-term measure and that individuals will know how best to use the money. The Brazilian economy is growing significantly more slowly than most analysts had forecast, with the International Monetary Fund expecting an expansion of just 0.8 percent this year.

Chilean Lawmakers Ending Codelco's Financing of Military

Chilean legislators on Wednesday passed a measure scrapping a longtime law under which state-run miner Codelco, the world's largest, helped finance the country's military, La Tercera reported. After nearly eight years under review, the approved bill establishes a new financing mechanism for the armed forces through a dedicated fund which Congress will oversee, according to a statement from the Chilean Congress, Reuters reported. Codelco's payments to state coffers will be gradually phased out over a period of more than 10 years. Under a 1958 law, which was strengthened during the dictatorship of Augusto Pinochet in the 1970s and 1980s, Codelco was required to divert 10 percent of its export sales to the military. President Sebastián Piñera, who spearheaded the new legislation and is expected to sign it into law, said it was "absurd" for Chile's military to be affected by fluctuating copper prices, Reuters reported. The state miner did not immediately comment on the passage of the law, but CEO Nelson Pizarro has said Codelco would be better off without the military funding requirement. The law requires Codelco to continue paying the 10 percent tax to the state "for a period of nine years, gradually falling 2.5 percent per year beginning year 10."

The law required Codelco to divert 10 percent of export sales to the military.

FEATURED Q&A / Continued from page 3

A **Jorge Salazar-Carrillo, professor and director of the Center of Economic Research at Florida International University:** "The economic situation in Venezuela will continue to deteriorate until there is an agreement between the people's majority, represented by Guaidó, and the minority (concentrated in Caracas) of Maduro. The latter has been losing support as economic conditions continue to deteriorate, now determined by the most severe inflation in history. This has led to theft in production and distribution of oil derivatives and every other good in the economy. In real terms, wages have lost so much purchasing power that workers are not working. They are trying to find consumables wherever they can and are trying to alleviate the health crisis of their family and friends. The only positive factor are the transfers of money and goods they can get their hands on, mostly from family and friends in the United States. Maduro is facing an increasing economic crisis as oil production continues to diminish and is increasingly stolen. Institutions that hold gold reserves are now freezing them. Cuban relations are being strained by lower deliveries of oil because of U.S. sanctions. And the drug cartel in which the military leadership is involved is increasingly scrutinized. Russia, China and Iran cannot provide the support that a Venezuela in crisis demands. In sum, there is no way out for Maduro to surrender to free and supervised elections that he knows he would lose."

> **"Russia, China and Iran cannot provide the support that a Venezuela in crisis demands."**
>
> **— Jorge Salazar-Carrillo**

A **Gustavo Coronel, a founding board member of PDVSA:** "U.S. sanctions against PDVSA are designed to block 'all property and interests in property of PDVSA subject to U.S. jurisdiction' and 'to prohibit U.S. persons from engaging in transactions with them.' As a result, U.S. cash going into the pockets of the illegitimate Maduro government has come to a stop. It is not easy to estimate the impact of these measures on the Venezuelan petroleum industry, since such an impact runs in parallel with the general situation of disarray that has been taking place within the company due to corruption and mismanagement. The sanctions aggravate the already existing chaos within PDVSA and were meant to accelerate the collapse of the Maduro regime, although this is taking longer than the United States hoped for, due to the temporary relief supplied to PDVSA by China and Russia. The Venezuelan collapse is not having a significant impact on global oil dynamics, due to the modest levels of Venezuelan oil production available for export. The short-term outlook for PDVSA's oil production and sales is dismal, with no improvement in sight. This is an irreversible situation, since boosting PDVSA's performance would require urgent financial and technical international assistance that cannot materialize under existing political conditions. PDVSA is dead in the water. "

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

LATIN AMERICA ENERGY ADVISOR
is published weekly by the Inter-American Dialogue
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Latin America Energy Advisor is published weekly, with the exception of some major U.S. holidays, by the Inter-American Dialogue
1155 15th Street NW, Suite 800
Washington, DC 20005 **Phone:** 202-822-9002
www.thedialogue.org
ISSN 2163-7962

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