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## FEATURED Q&amp;A

# Will Brazil's Oil Sector Weather Political Turmoil?



President Michel Temer is unlikely to weather the current political upheaval surrounding his presidency and other Brazilian politicians, which would make it difficult to pass and maintain his proposed reforms, Isabella Alcañiz says below. // File Photo: Brazilian Government.

**Q** Brazilian President Michel Temer in recent months has initiated a reopening of the oil sector to private investment as part of a series of economic reforms aimed at bringing the nation's economy out of a profound recession. However, political dynamics in Brazil have deteriorated dramatically following recent allegations of corruption against Temer during the course of the ongoing "Lava Jato" investigations, with thousands of protesters taking to the streets, and some turning violent and destructive. Analysts now increasingly suggest that Temer will be forced from office before next year's scheduled presidential election. What are the consequences of Brazil's heightened political drama for the country's energy sector reforms? To what extent have international investors scaled back on plans to invest in Brazilian energy companies and projects?

**A** Cleveland M. Jones, researcher at the National Institute of Oil and Gas, member of the geosciences advisory board at NXT Energy Solutions and professor of geology at the State University of Rio de Janeiro: "There are relatively few major plays available for investors worldwide, that are easily accessible, in relatively safe countries and which can be economically produced with current technology. Despite the momentary political upheaval in Brazil, most analysts recognize that there is likely to be no major impact to oil regulations and operating conditions in Brazil. In fact, there are ongoing initiatives that can even improve the operating environment in Brazil. Brazil's announced upcoming rounds, 10 in all, finally offer a measure of predictability, and allow longer-term planning. Thus, both the concession

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## TOP NEWS

## OIL &amp; GAS

## Three Petrobras Workers Killed in Oil Rig Blast

The incident was Petrobras' most deadly since an explosion on a floating production, storage and offloading vessel in 2015 left nine workers dead and 26 injured.

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## RENEWABLES

## China's State Power Eyes LAP's Chile Assets

Chinese state-owned energy company State Power Investment Corp. is in exclusive talks to acquire the Chilean assets of Latin America Power, or LAP, for between \$325 million and \$400 million.

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## OIL &amp; GAS

## Statoil Seeks to Triple Brazil Oil Production

The Norwegian oil and gas company hopes to become the operator of the entire Caracara discovery, said Anders Opedal, Statoil's head of Brazilian operations.

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Opedal // File Photo: Statoil.

## OIL &amp; GAS SECTOR NEWS

## Three Petrobras Workers Killed in Oil Rig Blast

Three workers of Brazilian state-run oil company Petrobras were killed due to injuries they sustained following an explosion June 9 at an offshore drill rig, The Wall Street Journal reported. The explosion occurred in

“This type of accident has its origins in the workforce reduction that Petrobras has been implementing.”

— Paulo Neves

the boiler room of a drill ship that is operated by Odebrecht Óleo e Gás in the Marlim field off Brazil's southeast coast. The incident was Petrobras' most deadly since an explosion on a floating production, storage and offloading vessel in 2015 left nine workers dead and 26 injured. The incident has raised concerns over whether the firm is able to meet safety standards as it looks to cut costs and pay off some of its heavy debt load. “This type of accident has its origins in the workforce reduction that Petrobras has been implementing,” said Paulo Neves, a director at the national oil workers' federation, or FUP. Petrobras did not provide details as to the cause of the explosion, though it said it would form a commission to investigate the incident.

## PDVSA Relocating Oil From Bahamas Storage Facility

Venezuelan state oil company PDVSA is relocating millions of barrels from a Bahamas storage facility following the termination of a

contract with the facility's owner, U.S. Buckeye Partners, according to sources familiar with the matter, Reuters reported Tuesday. PDVSA has decided to move its oil to the Statia terminal, which is located on the island of St. Eustatius and is operated by U.S.-based NuStar Energy. The termination came after multiple attempts between Buckeye and PDVSA to resolve payment delays and other problems that had stalled oil shipments from the storage facility, highlighting the state oil company's difficulty in maintaining business relationships and in making sure operations run smoothly in order to maximize the income Venezuela can get from oil, its key export. Buckeye and PDVSA did not respond to requests for comment. PDVSA is now paying some \$2.3 million per month to lease storage space for approximately five million barrels of crude at NuStar's Statia terminal.

## Fire at Pemex Refinery Injures Nine

A major fire broke out at an oil refinery run by Mexican state oil producer Pemex on Wednesday, injuring nine people, the Associated Press reported. None of the injuries were life-threatening, and all nine individuals had been released from the hospital, according to Pemex.

**Pemex had been looking for investment partners to help update the aging refinery.**

The fire extended the shutdown of the Salina Cruz refinery, which had been closed the day before due to heavy rains brought by tropical storm Calvin. The rains had flooded part of the plant, and the fire broke out after floodwaters caused waste containment ponds to overflow, spreading oil around the plant, the state oil company said. The fire began at the pump house of the plant, which is located in Oaxaca State, Reuters reported. An official at the Oaxaca State emergency services said some local neighborhoods had been evacuated due to the blaze. Pemex officials said the fire had

## NEWS BRIEFS

## Statoil Seeks to Triple Brazil Oil Production

Norwegian oil and gas company Statoil has set the goal of more than tripling its oil production in Brazil going into 2030, and hopes to become the operator for the entire Caracara discovery, said Anders Opedal, Statoil's head of Brazilian operations, Reuters reported Monday. The company has invested more than \$10 billion into oil production in Brazil and is the country's largest foreign offshore operator.

## Brazil's Raízen Offers \$248 Million for Two Ethanol Mills

Brazilian ethanol and sugar company Raízen, which is a joint venture between Cosan SA Indústria e Comércio and Royal Dutch Shell, has offered to pay 823 million reais, or approximately \$248 million, for two ethanol mills owned by Tonon Bioenergia, Reuters reported Tuesday. Tonon Bioenergia has been going through an in-court reorganization, according to a securities filing from Cosan, and is expected to sell the two mills in an auction.

## Mexico's Pemex Fined \$20 Million for Anti-Competitive Fuel Practices

Mexico's antitrust watchdog, the Federal Economic Competition Commission, or Cofece, fined a division of state-owned oil company Pemex 369 million pesos, or \$20.3 million, for the “possible commission of a monopolistic practice ... in the diesel market,” Reuters reported Monday. Cofece said Pemex's practices constituted a failure to establish a competitive fuel market. According to a statement from the regulator, the unit of Pemex in question did not comply with its obligations from a 2014 energy reform that prohibited it from offering discretionary benefits for selected buyers, and required it to refrain from suspending some sales and marketing contracts.

since been contained. The state oil company has been looking for partners to help invest in updating the aging Salina Cruz facility, though there have been no interested parties, to date.

## RENEWABLES NEWS

## Merkel, Macri Vow to Foster Trade, Protect Environment

German Chancellor Angela Merkel and Argentine President Mauricio Macri vowed June 8 in Buenos Aires to protect the environment and foster multilateral trade relations, the Associated Press reported. The two leaders met on



Macri and Merkel met June 8 in Buenos Aires. // Photo: Argentine Government.

the first day of Merkel's three-day visit to Latin America, which also included a stop in Mexico. Merkel's trip came ahead of next month's G-20 summit in Germany. She has criticized the protectionist trade rhetoric of U.S. President Donald Trump and has called his decision to withdraw the United States from the Paris Agreement on climate change "extremely regrettable."

## China's State Power Investment Eyes LAP's Chile Assets

Chinese state-owned energy company State Power Investment Corp. is in exclusive talks to acquire the Chilean assets of Latin America Power, or LAP, for between \$325 million and

\$400 million, according to two sources with knowledge of the matter, Reuters reported Wednesday. LAP owns more than 300 megawatts of wind and hydropower assets in Chile and Peru, more than 250 MW of which are in Chile, including two large wind farms near Santiago. In 2015, now-bankrupt U.S. energy company SunEdison agreed to purchase LAP for \$700 million. SunEdison later terminated the deal, and LAP received a \$29.5 million settlement in 2016. LAP put its assets back on the market, and companies including Chile's

Colbun, Canada's BluEarth Renewables and State Power Investment Corp. showed interest in acquiring it, though neither BluEarth nor Colbun are still in the running to purchase LAP, according to sources. State Power Investment Corp., along with LAP and Colbun, declined to comment on the matter of LAP's potential acquisition. BluEarth said in a statement that it "is always exploring new opportunities, including the Chilean power market," but added that it would not comment on "rumors or speculation."

## FEATURED Q&amp;A / Continued from page 1

rounds for post-salt areas, and the production-sharing rounds for pre-salt areas, represent exceptional opportunities for major world oil and gas players to participate in large-potential plays in a country that offers a favorable operating environment. Many of these plays have demonstrated the exceptional quality of the discoveries possible, especially in the pre-salt areas. Our research has indicated potentially recoverable resources in the pre-salt alone, of between 176 billion and 273 billion barrels of good-quality oil, and even under a 'lower for longer' scenario, these estimates are only slightly reduced. Obviously, there is

facilities. There are FPSOs operating with merely five wells, when up to 18 wells would otherwise be required. Companies will not ignore these realities when deciding where to allocate their budgets for new exploratory plays. Even Mexico's Gulf of Mexico areas do not match such attractiveness, despite important modernization efforts there."

**A** **Isabella Alcañiz, assistant professor in the Department of Government and Politics at the University of Maryland:**

"The prospects for any significant energy reform in the near future in Brazil are slim. The political crisis is taking precedence over the country's economic recession. Temer's promise of a wave of economic reforms in energy, finance and labor were already on shaky ground, as it seemed at least questionable than an unelected president could pass a number of difficult reforms through Congress, albeit a sympathetic one. Brazil's Bovespa stocks recovered slightly from the plunge they took immediately after a recording of Temer allegedly approving hush money to Eduardo Cunha—the other architect of President Dilma Rousseff's impeachment—was made public. The new corruption allegation feels like a chronicle of a scandal foretold, as Temer has been under investigation for quite some time. To maintain a legislative majority for his reforms and avoid being removed from office on corruption charges, Temer must

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**“The exceptional productivity of pre-salt fields is also an attractive factor for potential investors.”**

— Cleveland M. Jones

much oil to be discovered. The exceptional productivity of pre-salt fields is also an attractive factor for potential investors, since many fields have individual well production of 30,000 to 40,000 barrels of oil per day and more, thus reducing up-front costs for installing floating production storage and offloading vessels (FPSOs) and production

## Enel Completes Installation of 90 MW Brazilian Wind Farm

Italy's Enel Green Power has completed the installation of a 90-megawatt wind farm in Brazil, ReNews reported Tuesday. The Cristalândia project contains 45 turbines and is located in Bahia State. The wind farm is projected to generate some 350 gigawatt hours of electricity per year. Enel is investing approximately \$190 million in Cristalândia, which has 20-year power purchase agreements with several Brazilian electricity distribution companies.

### POLITICAL NEWS

## Former Rio State Governor Sentenced to 14 Years in Prison

Sérgio Cabral, a former governor of Brazil's Rio de Janeiro State, on Tuesday was sentenced to 14 years and two months in prison for his role in the massive corruption scheme involving state-run oil company Petrobras, the Los An-



Cabral // File Photo: Brazilian Government.

geles Times reported. Cabral was convicted of corruption and 12 counts of money laundering in connection with the scandal. Cabral was in office as the state's governor for two terms, from 2007 to 2014. Judge Sérgio Moro found Cabral guilty of receiving approximately 2.7 million reais (\$816,450) in bribes and laundering a portion of the proceeds, The Wall Street Jour-

nal reported. The kickbacks had been skimmed from an inflated construction contract for a refinery that had been built for Petrobras. An attorney for Cabral said the former governor is planning to file an appeal, but he did not say on what grounds. In addition to the Petrobras investigation, Cabral is also under investigation on corruption allegations related to Rio's health

care system, infrastructure projects and public works projects ahead of the 2014 World Cup and the 2016 Summer Olympics. In total, he is accused of diverting more than \$100 million from the state, laundering some of the money, depositing some in offshore bank accounts and buying luxury goods such as diamonds. In addition to the prison sentence, Moro ordered

## ADVISOR Q&A

### Has Brazil Pulled Out of Its Worst Recession Ever?

**Q** **Brazil's economy grew 1 percent in the first quarter as compared with the previous three-month period, officially ending the country's worst recession on record and marking the economy's first quarter-on-quarter growth following eight consecutive quarters of contraction. What factors were behind the return to growth this year, and what challenges lie ahead as Brazil navigates its ascent from recession? How can the government keep the economy from backsliding into recession? How will the current political scenario affect future economic stability in the country?**

**A** **Marcos Vinicius Chiliatto Leite, economic affairs officer at the Economic Commission for Latin America and the Caribbean:**

"The end of the recession is not yet clear on the Brazilian horizon. The 1 percent growth in the first quarter of 2017 after several periods of decline is the result of the external sector, driven by agriculture, which saw 13.4 percent growth in the first quarter. For 2017, the Brazilian Institute of Geography and Statistics projects an almost 30 percent increase in cash crops, mainly because of an abundant rainy season after a dry 2016. In addition to improvements on the supply side, a spike in commodity prices in the beginning of 2017, along with higher demand, drove this growth. Brazil,

with more than 200 million people and an industrialized economy, cannot rely on the export of commodities for its development. Brazil's strongest asset is its own people and domestic and regional markets, which still lack encouraging news. Household consumption and investment continue to fall, and unemployment remains unchanged. These weakening conditions pose a huge challenge to Brazilian industry, which also competes with Asia. In the first quarter, Brazilian industrial production marked a persisting decline of 0.7 percent (12 months accumulates -9.7 percent). Since foreign demand and agriculture explain most of the 1 percent growth, this shouldn't be attributed to economic policy. It is not related to the fiscal austerity or the social security and labor market reforms. Less public spending and labor market flexibility will not solve the industry challenge. It may even worsen the country's situation if it leads to lower wages and even lower household consumption. The country should move toward social equality to drive demand, together with a revitalized industrial development plan for boosting economic growth and structural change."

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

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## NEWS BRIEFS

## At Least Five Killed in Guatemala Earthquake

At least five people were killed and seven were injured by a magnitude 6.9 earthquake that struck western Guatemala early Wednesday, the country's national emergency coordination agency said, the Associated Press reported. A woman in the city of San Marcos was killed by a falling wall, and a homeless man in San Sebastián, Retalhuleu was killed after being hit by part of a church that collapsed. Three other women died from heart attacks attributed to fright caused by the quake. The earthquake also caused moderate damage to homes and some landslides that blocked highways.

## Argentina's Fernández Announces New Political Party, Eyes Senate Seat

Former Argentine President Cristina Fernández de Kirchner on Wednesday announced the creation of a new political party, Reuters reported. The former president, who is reportedly considering a run for a Senate seat in the country's October midterm election said the "Citizens' Unity" party will fight current President Mauricio Macri's "reinstatement of the neo-liberal model." Fernández has not announced her candidacy for a Senate seat, but has until June 24 to do so, Reuters reported.

## Peru to Begin Trade Talks for FTAs With Australia, India

Peru is set to begin negotiations with Australia and India to sign a free trade agreement, Prensa Latina reported Wednesday. The first round of negotiations with Australia will begin in July, and negotiations with India will begin in August. Peruvian Deputy Foreign Trade Minister Edgar Vásquez expressed his confidence in the negotiations, which he said would benefit the country's export sector as well as help create new jobs.

Cabral to pay a fine of \$203,000, the Los Angeles Times reported. The judge, however, acquitted Cabral's wife, Adriana Ancelmo, of related charges.

## Panama Cuts Ties With Taiwan in Favor of Recognizing China

Panama on Tuesday severed diplomatic relations with Taiwan in favor of establishing them with China, a move that further alienated Taiwan from the rest of the world, The Washington Post reported Tuesday. Panamanian President Juan Carlos Varela announced the decision in a televised address, saying the new foreign policy was the "correct path" for the country.

**Oppression and threats are not going to help in cross-strait relations."**

— Tsai Ing-wen

Panama and China released a joint statement announcing the change in diplomatic relations, saying they now recognize each other and were establishing ambassadorial-level relations the same day. "The Government of the Republic of Panama recognizes that there is but one China in the world, that the Government of the People's Republic of China is the sole legal government representing the whole of China, and that Taiwan is an inalienable part of China's territory," the statement said, Taiwanese President Tsai Ing-wen called the move a betrayal and vowed the continue to maintain the island's sovereignty. "Oppression and threats are not going to help in cross-strait relations. It will on the contrary increase the discrepancy between the people" of Taiwan and China, he said. Panama was one of the largest countries in the world to recognize Taiwan, which now has only 20 formal diplomatic partners. Out of all of its diplomatic partners, 11 are in Latin America and the Caribbean. China's policy is not to have diplomatic relations with any

countries that recognize Taiwan, The New York Times reported. "It is very possible that the remaining countries will switch," said Ross Feingold, a senior adviser in Taipei at D.C. International Advisory, of Taiwan's diplomatic allies in Central America.

## ECONOMIC NEWS

## Mexico's Industrial Production Level Falls in April

Mexico's National Statistics Institute announced June 9 that the country's industrial production fell more than expected in April, The Wall Street Journal reported. The country saw gains in manufacturing, though they were outweighed by declines in oil, mining and construction. The Easter holiday falling this year in April also gave the month fewer working days than it had last year. Industrial output declined a seasonally adjusted 0.3 percent as compared to March and fell 4.4 percent as compared to April 2016, according to the statistics institute. Economists in a Wall Street Journal survey had expected production to decline a median 2.2 percent year-on-year. Manufacturing led the sectors that increased output in April, with an increase of 0.6 percent as compared to March and 5.1 percent as compared to April of last year. Mexico's oil production was steady in April as compared to March, but was below levels from a year ago.

## Bancolombia Reduces Rates on Mortgage Loans

Bancolombia has reduced its interest rates on mortgages by as much as 150 basis points, with rates now starting at 9.6 percent on an annual basis, Finance Colombia reported June 9. Bancolombia added that the lower rates apply to the financing of both new and previously occupied homes. The bank so far this year has approved \$480 million in mortgages.

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hold together an electoral coalition between his own PMDB party and the PSDB. For now, the coalition is holding, but there is little expectation among political analysts and

“**Temer himself does not seem too confident in his political future.**”

— Isabella Alcañiz

market actors that Temer will survive this. Temer himself does not seem too confident in his political future, as he unceremoniously just replaced the minister of justice without offering any explanation.”

**A** **John Albuquerque Forman, director of J Forman Consultoria and former ANP director:** “On your questions, starting from the end, on the extension of international investors scaling back possible investments: it varies, depending on the investor. As conditions deteriorate, prices for assets decrease, and that is considered a favorable condition by some seasoned investors who recognize that Brazil will overcome its problems in the future, as has happened before. Others, more conservative, prefer to wait and see what will happen in the future. The main issues that are being considered are the economic reforms being voted upon

in Congress, if the process goes on, as it seems it will by the current developments and are approved, then the conditions for a turnaround are given. As for the energy sector, although the regulatory agencies were created from 1998 on, namely ANP, ANEEL, ANA, etc., with the role of regulating their sectors, they eventually became subordinated to the ministries, starting with the first PT Government in 2006. The Lula government changed the laws to create profit-sharing contracts, to be applied to the pre-salt areas. Also, Petrobras was given the right to at least a 30 percent stake in any block and to be the operator, on the pre-salt areas. The Dilma government gave more emphasis to the ministries and the CNPE, which became the decision-making agency for energy matters, further reducing the regulatory agencies’ role. The Temer government first proposed and Congress later approved changes that now allow Petrobras to decide if it will participate on pre-salt blocks and no longer is required to be the operator. The roles of CNPE and the ministries were enforced and made clear, and the agencies became even more restricted to studies and fiscalization. Any new government, if Temer leaves office or if elections to take place in 2018, will probably bring its own views and will try to impose them, something that is impossible to foresee now. The uncertainties and risk will remain, and investors will have to bear with them. Again, decisions will depend on the investors’ experience and willingness to face risks.”

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