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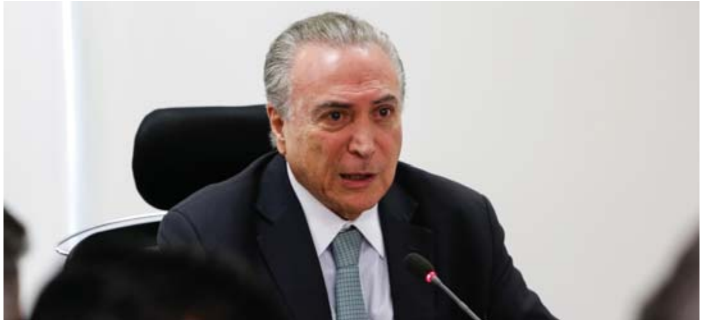
FEATURED Q&A

Are Temer's Reforms Benefiting Brazil's Oil Sector?



Brazilian President Michel Temer has enacted reforms in the oil sector in order to attract foreign investment. // File Photo: Brazilian Government.

Q **In its first oil auction since December 2015, Brazil last month saw mixed results, only selling one out of 76 offshore blocks on offer at the highly productive Santos basin, but selling 10 offshore blocks, including eight in the Campos basin, for a record $1.19 billion, to Exxon Mobil. Six of the blocks were sold to the consortium between the oil major and state-controlled oil company Petrobras. The auction was seen as a bellwether for the country's oil sector following a massive corruption scandal at Petrobras and President Michel Temer's market-friendly reforms aimed at attracting investment. What do the results mean for Brazil's oil sector? Were Temer's reforms successful? What will it take for Brazil to attract even more investment at future oil auctions?**

A **Alexis Arthur, independent energy analyst:** "Brazil's latest offshore auction has closed to mixed reviews. The press and government have been largely positive, noting that low turnout (only 13 percent of blocks were sold) was offset by high investment. Big hitters like Exxon, which purchased 10 blocks, will bring in more than $1 billion—a record for Brazil. It certainly suggests that President Temer's policy changes are enticing investors back to the oil and gas sector. Whether Brazil can replicate this success in the two pre-salt auctions scheduled for this month, however, remains to be seen. While a loosening of local-content laws was welcomed by investors, oil and gas extraction in the pre-salt remains an extremely expensive and risky endeavor. A lot has changed since Brazil discovered the pre-salt in 2006. At the time, President Lula da Silva declared it a 'gift from god,' and

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TOP NEWS

OIL & GAS

Sinopec Eyeing Sale of Argentine Oil Assets

Sinopec is looking to sell its Argentine oil assets, which are mainly in the southern Santa Cruz province, for between $750 million and $1 billion, citing losses and labor issues.

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RENEWABLES

Enel to Divest 80% of Renewables Portfolio in Mexico

Italian energy company Enel will divest an 80 percent stake in a 1,712-megawatt Mexican renewable energy portfolio, selling it for $1.35 billion. It will retain the remaining 20 percent.

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OIL & GAS

Court Freezes Assets of Rousseff, Other Officials Over Refinery Deal

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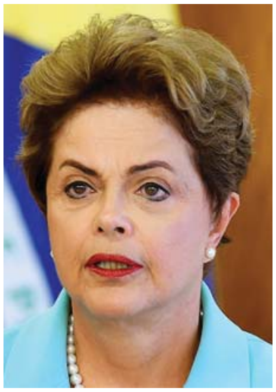


Rousseff // File Photo: Brazilian Government.

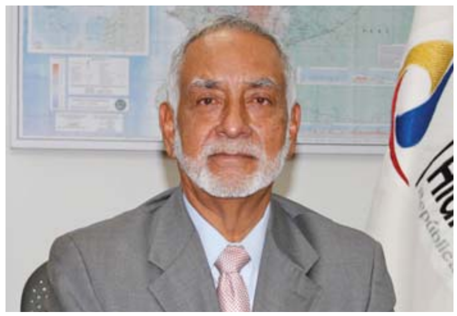
OIL & GAS SECTOR NEWS

Brazilian Court Blocks Petrobras-Total Deal

A Brazilian federal court has blocked part of a $2.2 billion deal that state oil company Petrobras and French oil company Total agreed on in March, Reuters reported Wednesday. Judge Edmilson da Silva Pimenta on Tuesday put a hold on a part of the deal in which Petrobras agreed to sell Total part of its holdings in two promising pre-salt oil blocks. The judge granted the injunction in favor of local oil workers' union members who said that as a government-run company, Petrobras should have had a public tender for the sale of its assets, rather than a private negotiation. Pimenta asked oil and gas regulator ANP to suspend the transfer of stakes after granting the injunction. In March, Petrobras and Total signed a "strategic alliance" that included transferring to Total a 22.5 percent stake in the Lara area and a 35 percent stake in the Lapa field. Both stakes are in the pre-salt area. The deal also included the sale of Petrobras' 50 percent stake in Termobahia, a thermal power complex that includes two plants. On Wednesday, Petrobras said it had not been formally informed of Pimenta's decision and that it would evaluate the decision once it had been officially notified. The state oil company added that it would take actions to defend its interests and those of its shareholders following the evaluation.

Ecuador to Tender Eight Blocks in January Oil Auction

Ecuador is planning to tender oil exploration and production blocks in January under new contract terms, with the goal of attracting more foreign investment and competing with neighboring oil-exporting countries, Oil Minister Carlos Pérez said Oct. 6, Reuters reported. "Ecuador needs to be able to compete now that Brazil and Colombia have changed their contract terms to encourage foreign investment," he said. The new contract terms will allow producers to be paid in oil and will allow them to export or sell the oil to local refineries. Pérez added that the government's decision to switch to production-sharing contracts from service contracts will also help attract more investment than in previous rounds of bidding. Ecuador will tender eight blocks at the Intercampos project in January and expects to see some $1.25 billion in investment. Another auction is scheduled for the second quarter of next year and will offer 16 additional blocks on lots 70s and 80s. Ecuador is seeking capital so that it can replace oil reserves, boost production and invest in infrastructure for its oil sector, but past instances of contract changes have driven potential investors away from the South American country. In 2009, Ecuador also withdrew from the World Bank's arbitration court, which for many oil companies is seen as a preferred mechanism for solving disputes with partners, increasing risk for investors interested in Ecuador's oil sector. Pérez said the government may include Chilean courts in its new contracts, conceding that the lack of international arbitration mechanisms for the sector was an "issue."



Pérez // File Photo: Ecuadorean Government.

Sinopec Eyeing Sale of Argentine Oil Assets for Some $1 Bn

Advisors to Chinese oil company Sinopec have offered its oil assets in Argentina to approximately a dozen potential buyers, according to three sources with knowledge of the matter,

NEWS BRIEFS

Court Freezes Assets of Rousseff, Other Officials Over Refinery Deal

Brazil's federal audit court, known as the TCU, on Wednesday ordered a freeze of former President Dilma Rousseff's assets, as well as those of the former head of state oil company Petrobras, José Sérgio Gabrielli, Reuters reported. The order is over a $580 million loss from the purchase of a Texas refinery in 2006. The freeze also extends to former Finance Minister Antonio Palocci and three members of Petrobras' board, who approved the controversial purchase, in which the company paid more than eight times what the refinery's previous owner had paid just a year before. Rousseff said there is no evidence that any crime was committed by the Petrobras board members who approved the deal.

Chile Power Auction Draws 24 Bids

A Chilean power auction attracted 24 bids to supply the country with 2,200 gigawatts per hour annually for 20 years starting in 2024, a government official said Wednesday, Reuters reported. The winning bidders will be announced on Nov. 3. Among the bidders were Spanish firms Acciona, Cox Energy and Ibereólica and Italian energy company Enel.

Oil Output Down 20% in U.S. Gulf of Mexico

About 20 percent of oil production in the U.S. Gulf of Mexico is offline due to Hurricane Nate, the U.S. Department of the Interior's Bureau of Safety and Environmental Enforcement said Thursday, Reuters reported. The area is currently seeing an approximately 344,000 barrel-per-day loss in output, according to the agency. Several oil companies evacuated staff from platforms in the gulf ahead of the storm. Approximately 12 percent of natural gas production in the area remains offline as well.

Reuters reported Monday. Sinopec is looking to sell its assets, which are mainly in the southern Santa Cruz province, for between $750 million and $1 billion, citing losses and labor issues. The selling price could be less than half the

> **Sinopec's Argentine oil assets are valued at less than half what it paid for them in 2010.**

$2.45 billion the company paid in 2010 as part of an aggressive drive to diversify its oil sources. Worsening economic conditions in the country, as well as social unrest, have "weighed" on operations, Sinopec said last September. Since taking office in December 2015, Argentine President Mauricio Macri has implemented energy-sector reforms in order to attract investment, and last month the government said it had brokered a deal with unions in order to calm labor tensions in Santa Cruz and lower costs. Two of the sources said the assets would be difficult to sell regardless of the Argentine government's efforts to make the sector more business-friendly, due to declining output and persistent labor issues. Sinopec had already considered divesting from its assets in 2015, sources told Reuters last year. "It doesn't have to be [fast], unless Sinopec is willing to lose a huge amount of money," a source said.

RENEWABLES NEWS

Enel to Divest 80% of Mexican Renewables Portfolio

Italian energy company Enel will divest an 80 percent stake in a 1,712-megawatt Mexican renewable energy portfolio, selling it for $1.35 billion to La Caisse de dépôt et placement du Québec, or CDPQ, and CKD Infraestructura México, Energy Business Review reported Tuesday. The renewable assets Enel is looking to sell include five wind farms and three solar projects, of which 1,238 megawatts of capacity are under construction and 429 megawatts of capacity are already in operation. Enel will retain the remaining 20 percent stake in the portfolio and will continue to be the operator of the plants, which are located in six Mexican states. The general manager of CKD, Eduardo Ramos, said the partnership with Enel will help the two companies by drawing on Enel's expertise in project development, construction and operation in Mexico's renewable sector. The five wind farms are the 198-MW Amistad, the 200-MW Dominica, the 129-MW Palo Alto, the 93-MW Salitrillos and the 100-MW Vientos del Altiplano. The solar projects that are part of Enel's investment are the 427-MW Villanueva I, the 327-MW Villanueva III and the 238-MW Don José. Enel expects the divestment to lower the company's consolidated net debt by nearly $1.9 billion. The deal is expected to close by the end of the year, subject to regulatory approvals from Mexican antitrust authorities.

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the pathway out of poverty and toward energy independence for Brazil. This outcome should be celebrated as a win for Brazil's energy sector, which has struggled to fulfill its potential amid domestic political turmoil and oil price volatility at the global level. Still, a rejuvenated oil and gas outlook is just one small piece of Brazil's economic and energy future—one that will be shaped as much by the country's response to the global shift toward renewables and the need to face the very real effects of climate change, as it will by selling its oil and gas prospects offshore."

> **"A rejuvenated oil and gas outlook is just one small piece of Brazil's economic and energy future."**
> — Alexis Arthur

A Edmar Luiz Fagundes de Almeida, professor and member of the Energy Economics Group at the Universidade Federal do Rio de Janeiro: "Brazil's 14th oil auction can be considered a success. The action offered blocks outside the pre-salt area and attracted new players for Brazilian upstream, and the bonus offered for the blocks that have been acquired has reached a record amount. This is surely a sign that recent reforms in the oil sector have been very well received by investors. Nevertheless, 95 percent of the bonuses offered are related to six oil blocks near the pre-salt area. The possibility of pre-salt oil discoveries in these blocks was the main reason for the interest in these blocks. This is good news for the two auctions scheduled for pre-salt blocks in late October. Nevertheless, companies' interest in the blocks offered in basins with no pre-salt prospects was very low. The Brazilian oil and gas industry is more and more focused on the pre-salt geology, and it is easy to understand why. If Brazilian energy policy aims at diversifying the exploratory effort, it will be necessary to review the regulatory framework and government take conditions for the onshore basins, as well as the offshore basins with no pre-salt prospects."

A Mark S. Langevin, director of the Brazil Initiative and research professor at the Elliott School of International Affairs at The George Washington University: "The auction was very successful by most standards. First, the auction attracted 20 firms with 17 acquiring both onshore and offshore blocks from the total of 287 blocks available. There were too many blocks up for bid, but there was significant interest, especially in the offshore Campos basin.

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POLITICAL NEWS

U.N. Calls for Probe of Deadly Mexico Prison Riot

The United Nations is calling for an investigation into Tuesday's prison riot in Cadereyta jail in Mexico's Nuevo León State that left 17 people dead, BBC News reported. The United Nations said the riot and authorities' handling of the disturbance merits a "complete and exhaustive" report, urging authorities "to clarify the tragedy that has occurred and to grant justice to the victims and their families," El Universal reported. State authorities said they are open to cooperating with human rights organizations. "Do you want somebody responsible? I am responsible," state security spokesperson Aldo Fasci said. The riot began early Tuesday, with some 250 inmates ultimately fighting security forces during the melee, according to local media. Negotiations with inmates who had taken three guards hostage and attempts by police forces to use non-lethal weapons to quell the riot proved unsuccessful, Fasci has said, BBC News reported. Authorities saw through video monitors that at least one prisoner had been killed, and guards had been taken hostage and were being beaten on the roof, so police forces decided to use lethal force in order to gain control of the riot and protect further guards and prisoners from injury or death, said Fasci, the Associated Press reported. He added that no direct orders were given to use lethal force, but that officers were following protocol. The U.N. statement calling for an investigation into the violence referred to a riot last year at Topo Chico prison that left 49 people dead, and another at Apodaca prison in 2012 that left 44 people dead. Both prisons are also in Nuevo León State.

Inmates had taken guards hostage during the riot.

NEWS BRIEFS

Federal Relief Workers Can't Stay 'Forever' in Puerto Rico: Trump

U.S. President Donald Trump on Thursday said federal relief workers cannot stay "forever" in hurricane-ravaged Puerto Rico, where most residents remain without power, hospitals are running out of medicines and many are struggling to find clean water, The Washington Post reported. In a tweet, Trump said, "We cannot keep FEMA, the Military & the First Responders, who have been amazing (under the most difficult circumstances) in P.R. forever!"

Brazilian Congressional Report Calls for Shelving Charges Against Temer

A Brazilian congressional report on Tuesday recommended that President Michel Temer not face charges for alleged obstruction of justice or membership in a criminal organization, Reuters reported. The report, which was written by Congressman Bonifacio de Andrada, said the allegations against Temer were unfounded. He also recommended not pursuing charges against two of Temer's cabinet ministers, who were facing allegations stemming from the corruption case involving bribes paid by Brazilian meatpacker JBS.

IMF Expects 2,300% Inflation Rate in Venezuela Next Year

The International Monetary Fund said Venezuela's annual inflation rate may jump to more than 2,300 percent next year, the highest estimate for any country tracked by the IMF, according to the organization's latest World Economic Outlook report, which was published Tuesday, Bloomberg News reported. GDP is expected to contract another 6 percent next year after shrinking an estimated 12 percent this year. Venezuela's central bank stopped publishing inflation data in December 2015.

Mexico's Zavala Eyes Presidential Run as Independent

Former Mexican First Lady Margarita Zavala on Friday resigned from the country's opposition National Action Party, or PAN, and plans to run for president as an independent, The Wall Street Journal reported. Zavala, the wife of former President Felipe Calderón, will have four months to gather 867,000 signatures in at least 17 of Mexico's states in order to be a candidate in the July 1 election, which her aides say will not be difficult due to her popularity, the newspaper reported. Analysts say Zavala's decision

Zavala // File Photo: Mexican Government.

to leave the PAN may help the ruling Institutional Revolutionary Party, or PRI, by fragmenting the opposition, say analysts. "Two years ago, I announced my intention of seeking the presidency of the republic...I would have liked to do it representing the PAN, and did all I could to achieve that," said Zavala. "I'm resigning from the PAN, but not from my duty of doing politics." Zavala has articulated little in terms of her platform, but has said she would make fighting corruption and strengthening the rule of law priorities. In a recent poll by newspaper El Universal, Zavala had 26.6 percent support, behind only leftist Andrés Manuel López Obrador of the Morena party, who had 28.6 percent support. Recent surveys have put Mexican Interior Minister Miguel Ángel Osorio Chong, the PRI's most popular presidential contender, as a distant third. The ruling party has lost popularity during the government of current President Enrique Peña Nieto. Several corruption scandals and rising violence have lowered the PRI's popularity, but Zavala's move could help the ruling party, said analysts. "The PRI is the main beneficiary of the division inside the PAN, as the anti-PRI vote, which is large in Mexico, gets fragmented," political scientist Jesús Silva-Herzog, a professor at Tec de Monterrey University, told The Wall Street Journal.

ECONOMIC NEWS

Ending NAFTA Would Harm U.S.-Mexico Relations: Videgaray

Ending the North American Free Trade Agreement would bring U.S.-Mexico relations to a breaking point and would affect the two countries' cooperation in other areas, such as fighting drug trafficking and stemming illegal immigration, Mexican Foreign Minister Luis Videgaray said Tuesday. Videgaray made the comments after U.S. President Donald Trump said he might want to scrap the accord. The United States, Mexico and Canada began a fourth round of talks Wednesday in Washington as they renegotiate NAFTA. Also on Tuesday, Thomas Donohue, the president of the U.S. Chamber of Commerce, accused the Trump administration of making "poison pill proposals" to sabotage the negotiations. The chamber has argued that NAFTA is critical to U.S. industries, including manufacturing and agriculture.

Brazilian Auto Sector Expecting 10% Boost in Sales Next Year

Brazil's auto sector is likely to see a 10 percent increase in sales and output next year, industry leaders said Monday at an event, indicating optimism that the sector will rebound as Mercedes-Benz announced plans for new investments in bus and truck plants in the country, Reuters reported. The head of Brazilian auto industry group Anfavea, Antonio Meagle, said global automakers are projected to produce some three million new vehicles in Brazil near year, up from an estimated 2.7 million this year but below the peak of 3.7 million in 2013.

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According to Brazil's National Petroleum and Biofuels Agency (ANP), 37 blocks were acquired for exploration and production to bring in more than $1 billion in signature bonuses. The largest signature bonus was the just over $700 million offered for block C-M-346 in the Campos basin by the consortium formed by Petrobras (50 percent-operator) and ExxonMobil (50 percent). ExxonMobil bet big on Brazil by winning 10 blocks. The company secured two blocks with 100 percent stakes in the Campos basin, along with eight others secured through consortia with state-controlled Petrobras, as well as Brazil's private-sector oil company, Queiroz Galvão. ExxonMobil will pay out $600 million in signature bonuses. ExxonMobil's aggressive bidding demonstrates its interest in developing the kind of strategic partnership with Petrobras now enjoyed by Statoil, Shell and Total. Later this month, the second and third rounds of the pre-salt offerings will be held and should also attract substantial participation from Petrobras, ExxonMobil and a host of foreign and small domestic firms. The rising interest in Brazil's oil and gas reserves stems from recent liberalizing reforms, such as lessening local-content requirements. If the pre-salt auctions perform well, then expect another round of reforms and rule-making that focus on making the most from the emerging partnership model that Petrobras is developing with a select set of major oil and gas firms."

> **"The rising interest in Brazil's oil and gas reserves stems from recent liberalizing reforms."**
>
> **— Mark Langevin**

A **John Albuquerque Forman, director of J Forman Consultoria and former ANP director:** "The results for the 14th round represent the answer to changes brought by Temer's government, by reviewing the pre-salt limitations, the demand for local content, the extension of Repetro that reduces taxes on exploration equipment, and by announcing a sequence of bidding rounds. The industry's reaction was very positive, as clear rules and a business-friendly environment, thanks to the changes made, brought international oil companies back to challenging but very promising targets, on deep and ultra-deep waters. It is notable that Petrobras, in association with ExxonMobil, took several blocks and gave the round its best results in terms of bonuses to be paid. The association of the larger international oil companies should also be noted. There was an excess of onshore blocks, where prospects are smaller and appeal to medium or small companies, exactly those that are more affected by the economic and financial restrictions that resulted from the country's crippling recession. The lower oil prices are also a factor that affects smaller productions with higher costs. The good news is that the government has announced that blocks once offered will remain available in the next rounds. The rounds for onshore and offshore will be done separately, as they represent different prospects that appeal to different sized companies."

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

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