

# INTER-AMERICAN DIALOGUE'S LATIN AMERICA ADVISOR

## BOARD OF ADVISORS

- |   |  |
|---|--|
| <b>Diego Arria</b><br>Director,<br>Columbus Group   | <b>Jon Huenemann</b><br>Principal,<br>International<br>Department,<br>Miller & Chevalier |
| <b>Genaro Arriagada</b><br>Board Member, Banco<br>del Estado de Chile                                 | <b>James R. Jones</b><br>Co-chair,<br>Manatt Jones<br>Global Strategies LLC              |
| <b>Joyce Chang</b><br>Global Head of<br>Emerging Markets<br>Research, JPMorgan<br>Chase & Co.         | <b>John Maisto</b><br>Director,<br>US Education Finance<br>Group                         |
| <b>W. Bowman Cutter</b><br>Partner,<br>E.M. Warburg<br>Pincus   | <b>Nicolás Mariscal</b><br>Chairman,<br>Grupo Marhnos                                    |
| <b>Rui da Costa</b><br>Managing Director,<br>Latin America & the<br>Caribbean,<br>Hewlett-Packard Co. | <b>Thomas F. McLarty III</b><br>President,<br>Kissinger McLarty<br>Associates            |
| <b>Dirk Donath</b><br>Managing Director,<br>Eton Park Capital<br>Management                           | <b>Juan Felipe Muñoz</b><br>President,<br>The Otun Group                                 |
| <b>Jane Eddy</b><br>Managing Director,<br>Corporate & Govt.<br>Ratings Group,<br>Standard & Poor's    | <b>Carlos Paz-Soldan</b><br>Partner,<br>Saul Ewing, LLP                                  |
| <b>Marlene Fernández</b><br>Executive Director for<br>Latin America,<br>The Gallup<br>Organization    | <b>Beatrice Rangel</b><br>Managing Director,<br>AMLA Consulting LLC                      |
| <b>Wallace Gardner</b><br>Vice President,<br>Worldwide Sales,<br>Chubb & Son                          | <b>José Antonio Ríos</b><br>Chairman,<br>Global Crossing<br>Latin America                |
| <b>Javier Garza</b><br>Chairman and CEO,<br>Grupo Domos<br>Internacional                              | <b>Andrés Rozental</b><br>President,<br>Rozental & Asociados                             |
| <b>Peter Hakim</b><br>President,<br>Inter-American<br>Dialogue  | <b>Everett Santos</b><br>President,<br>DALEC LLC   |
| <b>Donna Hrinak</b><br>Director for Corporate<br>and Govt. Affairs,<br>Kraft Foods Inc.               | <b>Roger Scher</b><br>Head of Latin<br>American<br>Sovereign Ratings,<br>Fitch Ratings   |

## Featured Q&A With Our Board of Advisors

**Q From stormy weather and declining output to earnings losses and rebel bomb attacks, Mexican state oil monopoly Pemex has been suffering from a number of headaches in recent months. What is the outlook for the company? Is a brighter future on the horizon? What's needed to get the company on track?**

**A Guest Comment: José Coballasi:** "We do not expect a significant change in the medium term regarding Pemex's relationship with the government, or a material reduction in the government's heavy involvement in the sector or in the company. We believe that any improvement in Pemex's creditworthiness would require a combination of the government contributing sufficient capital to allow for significant deleveraging; the government sharply reducing Pemex's tax burden, so the bulk of capital expenditures (maintenance and expansion) could be internally funded; an improvement in Pemex's operations, particularly in reserve replacement; and a reduction of its growing unfunded pension liabilities. The rating on Pemex could be lowered if debt leverage continues to climb significantly, pension liabilities grow disproportionately, and reserve replacement trends are not improved. The recently approved fiscal reform should allow Pemex to retain a higher amount of internally generated cash (about \$3 billion). Although Pemex has significantly

increased its capital spending relative to the 1990s (in 2007 we expect capital expenditure to reach \$12.6 billion for exploration and production (E&P), \$2.1 billion for refining, and \$700 million for gas and petrochemicals), some industry observers estimate that it might need to increase its investment budget by another \$5 billion (already considering the additional monies from the reform) to adequately meet its investment needs, particularly for E&P."

**A Guest Comment: Maria Velez de Berliner:** "State ownership is not the source of Pemex's decline and problems. Both lie in the govern-  
*Continued on page 4*

## PHOTO OF THE DAY



Chilean President Michelle Bachelet inaugurated the 17th annual Ibero-American Summit in Chile on Thursday. See [story](#) on page 2.

Photo: La Moneda.

## Inside This Issue

- |  |          |  |          |
|--|----------|--|----------|
| <b>FEATURED Q&amp;A:</b> What is the Outlook for Mexican State Oil Company Pemex?..... | <b>1</b> | Petroecuador to Cancel Contract with City Oriente for Unpaid Taxes.....                      | <b>3</b> |
| Ibero-American Summit Underway in Chile .....  | <b>2</b> | <b>Capitol Hill Watch:</b> A Weekly Look at US Congressional Activity on Latin America ..... | <b>3</b> |
| House Approves US Free Trade Agreement with Peru .....                                 | <b>2</b> | Argentina's Banco Macro Posts 17 Percent Decline in Q3 Profit.....                           | <b>4</b> |

## NEWS BRIEFS

**Tabasco Floods Could Cost Insurers \$700 Million**

Insurers could pay out almost \$700 million after floods ravaged much of Mexico's southern Tabasco state, forcing tens of thousands to flee their homes, the Mexican Insurers Association, or AMIS, said Thursday, according to Reuters. "The magnitude of this catastrophe ... could be compared to the dimension of what happened in New Orleans," AMIS President Jose Morales said, referring to Louisiana's Hurricane Katrina in 2005. The flooding damage will be the most expensive insurance payout in Mexico since Hurricane Wilma wreaked havoc on Cancun in 2005, AMIS said.

**Brazil's Petrobras Announces Giant Oil Reserve Find**

Brazil's state-controlled oil and gas company **Petrobras** announced the discovery of a giant offshore crude reserve, Reuters reported. Petrobras said tests at the Tupi field in the Santos basin allowed it to estimate recoverable reserves of between 5 billion and 8 billion barrels, or about half Brazil's existing proven reserves. Officials said production could start in five to six years.

**Coca-Cola, Mexico's KOF Acquire Jugos del Valle**

A joint venture of **Coca-Cola Co.** and Mexican bottler **Coca-Cola Femsá (KOF)** said Thursday it bought juice maker **Jugos del Valle** for \$370 million, Reuters reported. KOF said it and Coca-Cola purchased 100 percent of Jugos del Valle's shares at \$6.3409 per share. KOF is the second-largest Coke bottler in the world. Jugos del Valle is a major juice maker in Mexico and Brazil.

## Political News

**Ibero-American Summit Underway in Chile**

President Michelle Bachelet kicked off the 17th annual Ibero-American summit in Chile on Thursday, calling the meeting an opportunity to promote social justice. "This summit will be a powerful step toward the construction of a new social pact within our countries and between our countries," Bachelet said at an inaugural ceremony to launch the three-day summit, according to the summit's official [Web site](#). "We are in a moment of opportunity that we should take advantage of." The theme of the summit is "social cohesion," but energy and a slew of bilateral issues are also expected to be discussed among leaders. The start of the summit was marked by demonstrations outside of the Venezuelan embassy in Santiago both

“ This summit will be a powerful step toward the construction of a new social pact within our countries and between our countries. ”

— Michelle Bachelet

for and against the government of Venezuelan President Hugo Chavez, with both supporters and opponents of the fiery leftist leader getting into shoving matches, according to Reuters. Chavez, whose attendance at the summit was uncertain amid protests in Venezuela over proposed constitutional reforms seen as consolidating his power, arrived in Chile this morning, Chavez according to Venezuelan state news service ABN. Chavez is expected to meet with Colombian President Alvaro Uribe on the sidelines of the summit to discuss a possible deal for the release of hostages held by Colombia's FARC rebel group. Chavez has been meeting in Caracas this week with FARC representatives in an attempt to broker an agreement. Also during the summit, Brazilian President Luiz Inacio Lula da



Photo: ABN.

Silva is expected to meet with his Bolivian counterpart, Evo Morales, to discuss new Brazilian investments in Bolivia's hydrocarbons sector, while Bolivia and Chile are expected to discuss landlocked Bolivia's demand for access to the Pacific Ocean, according to AFP.

## Economic News

**House Approves US Free Trade Agreement with Peru**

The US House of Representatives approved a free trade deal with Peru on Thursday, handing a rare victory to President George W. Bush in a vote that split Democratic ranks. Lawmakers voted 285 to 132 to approve the pact, the first of four pending trade agreements negotiated by the Bush administration. House Speaker Nancy Pelosi (D-CA) justified her

support for the deal after 116 Democrats rejected it and just 108 supported it. "I absolutely refuse to have the Democratic Party be viewed ... as an anti-trade party," Pelosi said, according to the *Los Angeles Times*. She has argued that the agreement is acceptable because of labor and environmental provisions added earlier this year. However, some critics say the agreement comes up short on protecting workers. "On close inspection, the Agreement's labor provisions lack teeth," said Mark Barenberg, a law school professor at Columbia University, said in a press release Thursday announcing a [report](#) on the trade deal. "There is no meaningful mechanism for continuous verification that Peru is complying with basic labor rights." The US Chamber of Commerce in a press release hailed passage of the agreement by the House, saying it was a vote "in the interests of democracy in the region and economic growth here at home." By the end of the year, the Senate is expected

to approve the pact, which makes permanent Peru's current trade preferences in the US while phasing in duty-free access for US goods to Peru. Many workers in Peru voiced their opposition to the vote Thursday by taking to the streets, Reuters reported. Thousands of teachers, nurses, and construction workers joined a nationwide mining strike, which was into its fourth day, to oppose the pact.

## Company News

### Petroecuador to Cancel Contract with City Oriente for Unpaid Taxes

State-owned **Petroecuador** said Thursday it would seek to end its contract with US-owned oil firm **City Oriente** for failing to pay a windfall tax on oil sales, Reuters reported. Petroecuador President Carlos Pareja said that City Oriente has refused to pay the government \$28 million it owes since Congress last year approved a windfall tax on oil sales by foreign companies above a set benchmark price in their contracts. "City has a big problem with a debt of \$28 million and yesterday I called for the termination of its contract," Pareja was quoted as telling local television. City Oriente, which is based in Panama, filed an international arbitration claim last year against Ecuador contesting the tax. Last month, Ecuadorean President Rafael decreed an increase in the tax from 50 percent to 99 percent. The tax hike came as the government seeks to renegotiate its contracts with foreign oil companies, which account for about half of the 500,000 barrels of oil per day produced in the Andean nation. Through the negotiations, the government is seeking to convert the contracts to deals in which the companies would be paid for their services, but would not be allowed to keep the oil themselves. Pareja said Thursday that Spain's **Repsol** still owes the state around \$2 million, but that the company is willing to settle its debt, while the government has problems calculating if other companies have pending debts. Economy Minister Fausto Ortiz said the government is analyzing whether **Andes Petroleum** and Brazil's **Petrobras** still have debts with the state, according to Reuters.

## Capitol Hill Watch

### A Weekly Look at US Congressional Activity on Latin America

#### Clinton Declares Opposition to Free Trade Deals with Colombia, Panama

Sen. Hillary Clinton (D-NY), the Democratic frontrunner for president, said Thursday she opposes proposed free trade agreements with Colombia and Panama. In a [statement](#), Clinton said she was "very concerned about the history of violence against trade unionists in Colombia" and in the case of Panama cited the election in September of Pedro Miguel Gonzalez, who is wanted in the US for murdering a US soldier in 1992, to head the country's National Assembly. "Accordingly, I will oppose the trade agreements with these countries," Clinton said. Clinton's opposition to the trade pacts with Colombia and Panama could make their passage much more difficult, especially if she remains the frontrunner for the Democratic nomination. In her statement, Clinton said she supported the proposed free trade agreement with Peru, which was approved by the House on Thursday, citing the agreement's "very strong labor and environmental protections."



Clinton  
Office of Sen.  
Clinton file photo.

#### Cuellar Confident Congress Will Pass Counterdrug Aid Package for Mexico

Rep. Henry Cuellar (D-TX) said Thursday he is confident Congress will approve the first phase of a \$1.4 billion multi-year assistance package to help curb the flow of drugs from Mexico. To ensure passage next spring, proponents ought to keep arguing that "it is in our best interest to help Mexico," Cuellar told an audience at the American Enterprise Institute (AEI). "It's a big paradigm change in them [Mexico] asking for assistance," he said. Although other Democrats expressed support for the package at a hearing two weeks ago, they—and their Mexican counterparts—are irked they weren't consulted on the plan's details, which still haven't been made public. The Bush administration is asking Congress to approve \$500 million for Mexico and \$50 million for Central America this year as part of a \$46 billion supplemental bill for the wars in Iraq and Afghanistan. Under the plan, which the governments have dubbed the "Merida Initiative" after the city in Mexico where Bush and Mexican President Felipe Calderon first discussed it, the US would dedicate \$1.4 billion to supply helicopters, border surveillance equipment, and law enforcement training to Mexico. "[The supplemental bill] is a vehicle that's become controversial," Cuellar explained. When questioned by the audience, he didn't dismiss the possibility of instead proposing the legislation in a single bill. But he warned that other subjects, such as immigration, would become issues in a single bill. "For right now, we'll stick to the Iraq supplemental," he said.

#### House and Senate to Hold Hearings on Aid Package Next Week

The House and Senate will hold hearings next Wednesday and Thursday, respectively, during which lawmakers are expected to raise questions about how the plan will ensure accountability and transparency, avoid corruption, and ensure that proper training accompanies equipment, other panelists at the AEI event said Thursday. US Secretary of State for Western Hemisphere Affairs Tom Shannon is scheduled to testify in the House Foreign Affairs Committee on Wednesday at 2:00 pm.

**Featured Q&A***Continued from page 1*

ment's mismanagement of the company and reliance on it for about 40 percent of its operating budget, while an estimated 40 percent of all Mexican companies pay no taxes. Petrobras, Statoil, and PetroChina, whose valuation just became the largest in the world, are state-owned and steady performers under effective management. Another problem for Pemex is that, according to current estimates, Mexico's known reserves will run out in about 10 years, or

“Under present conditions in Mexico and in the world's oil markets, strategic partnerships are the only option for the viable future of the company.”

— *Maria Velez de Berliner*

sooner if the projected annual decline of about 15 percent in Cantarell accelerates due to faster seepage of water and gas. Mexico's Constitution requires an amendment to privatize Pemex or change its basic structure. The amendment would require a two-thirds majority in Congress and approval by more than half of the state legislatures. President Calderon's minority in Congress will need a coalition with the

### Argentina's Banco Macro Posts 17 Percent Decline in Q3 Profit

**Banco Macro**, one of Argentina's largest private banks, reported a 17 percent drop in third-quarter net profit on Thursday due to losses on its investments in Argentine bonds, Reuters reported. The bank said its net profit from July to September was 88 million pesos (\$US 27.5 million), down from 106 million pesos during the same period of 2006. "This result is due to lower net earnings (due to the falling prices of

PRI, the father of Pemex's nationalization under President Lazaro Cardenas. Although PRI leaders recognize the status of Pemex is untenable in the long run, it is doubtful they will let go of their prized political card. But let go they must, if only partially, if the company is to continue transferring revenue to the state. FDI in joint-venture partnership agreements for exploration in strategic energy sectors are necessary for Pemex to meet the challenges. Its reserves of peak oil will run out, and its lack of capital and skills to develop non-traditional oil reserves, such as shale and deep water, are low or non-existent. Saddled with debt and government obligations, Pemex requires FDI to increase capacity, revenue, and profitability. Its agreement with Petrobras for deep-water exploration can serve as a model for agreements with other oil multinationals. Mexico needs a profitable Pemex. Under present conditions in Mexico and in the world's oil markets, strategic partnerships are the only option for the viable future of the company. These can be done without constitutional reform."

**José Coballasi** is a Director of Industrial Ratings at Standard & Poor's.

**Maria Velez de Berliner** is President of Latin Intelligence Corporation.

bonds), which was partially compensated by a substantial increase in earnings from loans," Banco Macro said in a statement to the **Buenos Aires Stock Exchange**, according to Reuters. Argentine sovereign debt suffered big losses during the third quarter as global investors sold off riskier emerging market assets amid concerns about a credit crunch in the United States caused by the subprime mortgage market crisis. Banco Macro reported a nine-month net profit of 326.5 million pesos, up 17.8 percent from the same period a year ago.

**Latin America Advisor**

is published every business day by the Inter-American Dialogue, Copyright © 2007

**Erik Brand,**

General Manager, Publishing

**Robert Simpson,**

Editor

**Elisabeth Burgess,**

Reporter

**Danielle Jetton,**

Computer Services Coordinator

**Katie Buckland,**

Staff Intern

**Inter-American Dialogue:**

**Peter Hakim,**

President

**Michael Shifter,**

Vice President, Policy

**Joan Caivano,**

Director, Special Projects

**Dan Erikson,**

Senior Associate, US Policy

**Claudio Loser,**

Senior Fellow

**Manuel Orozco,**

Executive Director, Remittances and Rural Development Project

**Tamara Ortega Goodspeed,**

Senior Associate, Education

**Marifeli Pérez-Stable,**

Vice President, Democratic Governance

**Jeffrey M. Puryear,**

Vice President, Social Policy

**Viron Vaky,**

Senior Fellow

**Subscription Inquiries** are welcomed at [fretrial@thedialogue.org](mailto:fretrial@thedialogue.org)

**Latin America Advisor** is published every business day by the Inter-American Dialogue 1211 Connecticut Avenue, Suite 510 Washington, DC 20036 Phone: 202-822-9002 Fax: 202-822-9553

The opinions expressed by the members of the Board of Advisors and by guest commentators do not necessarily represent those of the publisher. The analysis is the sole view of each Advisor and does not necessarily represent the views of their respective employers or firms. The information in this report has been obtained from reliable sources, but neither its accuracy and completeness, nor the opinions based thereon, are guaranteed. If you have any questions relating to the contents of this publication, contact the editorial offices of the Inter-American Dialogue. Contents of this report may not be reproduced, stored in a retrieval system, or transmitted without prior written permission from the publisher.