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FEATURED Q&A

What is the Outlook for Argentine Energy Company YPF?

Q Spanish-Argentine oil and gas company Repsol-YPF announced last month it was selling a 14.9 percent stake in its Argentine unit, YPF, to Argentina's Petersen Group for $2.2 billion, with the option for the Petersen Group to buy another 10.1 percent over the next four years. What does the deal mean for YPF? Do you expect falling output by YPF to continue?

A Guest Comment: Isabella Alcañiz: "This deal may benefit Repsol-YPF in that the Petersen Group, led by the Eskenazi family, has very close ties with the Argentine government (Enrique Eskenazi, a banker from the province of Santa Cruz, has done business with the Kirchners since Nestor Kirchner was governor of Santa Cruz). The transaction further allows Repsol to pursue its (now quite noticeable) interests in other markets. Direct access to the government of President Cristina Kirchner is a major advantage for YPF, in particular in the current climate of tension between the oil sector and the government—exacerbated by the difficult energy crisis. However, in terms of increasing the productivity of YPF in Argentina, it is not clear how much the Peterson Group will contribute to Repsol-YPF. The Eskenazi family has built its conglomerate on banking and construction, and has no experience or expertise in oil and energy. Repsol-YPF touts the strategic partnership as critical in shoring up the financial structure of YPF in Argentina. Yet this will only be the case if the Eskenazi family contributes its financial means to the oil company. Finally, given the closeness between the Argentine government and the Eskenazi family, some critics interpret the transaction as evidence of increased regulation and even the possible (re)nationalization of YPF in the future."

A Guest Comment: Juliette Kerr: "The deal is good news for YPF, as the entry of a local partner could help strengthen the former state

Continued on page 4

PHOTO OF THE DAY

Mexican President Felipe Calderon (L) was one of several Latin American presidents to attend the inauguration Monday of Guatemalan President Alvaro Colom (R). See story on page 2.

Photo: Guatemalan government.

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NEWS BRIEFS

Bolivia Expects More Than $400 Million in Mining Investment

The Bolivian government said Monday it expects more than $400 million in public and private investment in the mining sector this year, Reuters reported. Bolivia's mine ministry said it expects India's **Jindal Steel and Power** to invest between $250 and $300 million in an iron ore project, and Canada's **Apogee Minerals** to spend $65 million at a mine. It said it also expects $20 million in investments by the US' **Apex Silver** and Japan's **Sumitomo**, and another $11.7 million from Glencore's Bolivian unit, **Sinchi Wayra**. The government said it would spend $53.9 million.

Keiko Fujimori Founds New Party; Leaves Open 2011 Presidential Bid

Peruvian lawmaker Keiko Fujimori, a daughter of former President Alberto Fujimori, said Monday she has founded a new political party, called Fuerza 2011, according to wire reports. The 32 year-old Keiko, who won more votes than any other congressional candidate in the 2006 elections, said she would not rule out her candidacy in Peru's 2011 presidential election. Her father, on trial for corruption and human rights abuses, faces 30 years in prison.

Brazil's Lula to Sign Economic Deals During Visit to Cuba

Brazilian President Luiz Inacio Lula da Silva, who arrived in Cuba on Monday, will sign a series of economic deals and offer the Communist island a $1 billion line of credit for food and infrastructure projects, the Associated Press reported. Under one of the deals, Brazilian state oil company **Petrobras** will be able to explore for deepwater oil off Cuba's shores.

Political News

Colom Takes Office in Guatemala; Vows to Fight Crime, Poverty

Alvaro Colom took office Monday as president of Guatemala, vowing to fight poverty and crime. Colom, who defeated conservative former army general Otto Perez in a November 4 election, became the Central American nation's first leftist president since the government of Jacobo Arbenz, who was ousted in 1954 by a CIA-backed coup. However, Colom said he did not want to be identified with other leftist governments in Latin America, including that of fiery Venezuelan President Hugo Chavez, and said each country must "find its own path," the Associated Press reported. Shortly after his election, Colom said he supports Guatemala's free trade agreement with the United States and that he would ask the US for aid to fight drug trafficking. Colombia has been wracked by crime and violence associated with drug trafficking, with some 6,000 people murdered last year in the country of 13 million people. "You can't run a country if there is no justice," Colom said at his swearing-in ceremony, according to Reuters. Colom said he would use social programs, judicial reform, and a crackdown on money laundering in the fight against crime. The new Guatemalan president also said his inauguration marked "the beginning of privileges for the poor, the beginning of privileges for those without opportunities," the AP reported. To help alleviate poverty and improve the economy of Guatemala, where half of the population lives on less than a dollar a day, Colom plans to ask business leaders to participate in a "Social Pact." Attending Monday's inauguration were several Latin American heads of state, including Chavez, Mexico's Felipe Calderon, Colombia's Alvaro Uribe, Luiz Inacio Lula da Silva of Brazil, Nicaragua's Daniel Ortega, and Ecuador's Rafael Correa.

> "You can't run a country if there is no justice."
>
> *— Alvaro Colom*

Morales, Governors Agree to Recall Referendums if no Consensus

Bolivian President Evo Morales and the country's nine governors agreed early today to submit themselves to revocatory referendums if they could not reach a consensus on a new Constitution and how to divvy up proceeds from the sale of Bolivia's natural gas wealth, state news service ABI reported. The agreement came after an eight-hour overnight meeting between Morales and the governors, including governors from four western provinces that have declared autonomy from the central government, threatening to plunge the South American country into civil war. Talks were expected to continue this afternoon and focus on the compatibility of a draft Constitution approved late last year by Morales supporters and the four provinces' demands for autonomy. According to Reuters, Morales' cabinet chief, Juan Ramon Quintana, said the government would offer during today's meeting to revise the Constitution to legalize some of the provinces' autonomy demands. Ruben Costas, the governor of Santa Cruz province and a leader of the opposition, said the government needed to be flexible or risk losing more support, Reuters reported. Critics say the draft constitution lacks legitimacy because it was passed by a constituent assembly amid a boycott by opposition delegates. The draft of the new Constitution is to be voted on this year in a referendum. [Editor's note: look for related Q&A in an upcoming issue of the *Advisor*.]

Morales

Photo: ABI.

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Economic News

Ecuador's Correa Proposes Elimination of Oil Funds

Ecuadorean President Rafael Correa has introduced legislation to scrap three savings funds and transfer their $1.5 billion in windfall oil revenues to the national budget, government officials said Monday, according to Reuters. Finance Minister Fausto Ortiz later said the money will be used for capital spending and that those funds will be added to the 2008 budget approved last year. "We can reform the budget ... we do it everyday," Ortiz was quoted as telling reporters. The bill is expected to be easily approved by an assembly responsible for rewriting Ecuador's Constitution. The assembly, which has taken over powers from Congress, is majority-controlled by Correa's supporters. The three oil funds are the FAC, or savings and contingency fund; CEREPS, or special account to reactivate social development and production; and FEISEH, or energy and hydrocarbons investment fund, according to Reuters. A fourth fund named FEP, or stabilization fund, receives funds from the CEREPS. Investors worry that elimination of the funds will increase Ecuador's exposure to external shocks.

Company News

Repsol Announces Large Natural Gas Find in Peru

Spanish oil and gas company **Repsol** on Monday announced a large natural gas find in Peru. In a press release, Repsol said the Kinteroni field, located near the city of Cuzco in southern Peru, could hold two trillion cubic feet (tcf) of natural gas. During a meeting with Repsol executives in Lima, Peruvian President Alan Garcia called the find "very important," Reuters reported. Earlier this month, the Peruvian government raised its proven reserves for the Camisea natural gas field, which the Kinteroni field is near, to 13.4 tcf from 10.86 tcf. Garcia has said the field could eventually show proven reserves of 20 tcf, giving the country security for 20 years, according to Reuters. Repsol has 41 percent of the Kinteroni field, which it operates. Brazilian state-owned oil and gas company **Petrobras** has 35.15 percent and **Burlington Resources Peru**, part of US oil giant **ConocoPhillips**, has 23.85 percent. Repsol said it and Petrobras are in the process of buying Burlington's stake. The deal is awaiting approval by the Peruvian authorities. In September, Repsol was awarded a 15-year, $15 billion contract to supply liquefied natural gas from the Camisea field to a plant in the port of Manzanillo on the Pacific coast of Mexico.

The Kinteroni field in southern Peru may hold two trillion cubic feet of natural gas, according to Repsol.

Photo: Repsol.

The Dialogue Continues

How Do LatAm Countries Benefit from Sovereign Wealth Funds?

Q Sovereign wealth funds (SWFs) held by emerging market countries—soon expected to value over $4 trillion—became a controversial topic in 2007, as economists and policymakers in industrialized nations began to worry about their growing influence. What do Latin American countries and markets stand to gain as a result of this trend toward more substantial sovereign wealth funds? What risks do the rise in sovereign wealth funds pose to the region?

A Guest Comment: Geoffrey Milton: "Sovereign wealth funds are not a new phenomenon, but they have recently become a more important part of international investment with the extraordinary wealth created by soaring oil and commodity prices. Countries running substantial balance of payment surpluses are seeking higher risk-adjusted returns than investing all their reserves in foreign government securities and gold. As a result, they have hired fund managers to invest in strategic assets, corporations, natural resources, and real estate in both developed markets and other emerging countries. Recipient countries of this direct investment can be concerned by foreign control of sensitive industries and natural resources (for example, the Dubai Ports case in the US two years ago), but frankly this is usually not valid—it's political, more than anything else. Now 'the shoe is on the other foot;' the industrialized nations are wary of this scale of inward investment and are crying lack of transparency. There were similar concerns in the 1980s with Japan Inc. buying up the United States. Latin America should welcome this investment diversification, provided there are adequate controls, proper licensing, etc. This is a natural result of globalization; the SWFs are seeking fresh sources of natural resources to fuel their expanding economies and a superior return on their funds for future generations. It is far better than the result of the last oil boom, when petrodollars were recycled through western banks and used to finance inefficient regimes and balance of payments deficits."

Geoffrey Milton *is an independent consultant.*

Editor's note: the above is a continuation of a Q&A published in the January 14, 2007 issue of the Advisor.

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Featured Q&A

Continued from page 1

oil company's relations with the government. The government of former President Nestor Kirchner demonstrated a strong preference for companies deemed to be of strategic importance to be controlled by Argentine shareholders, and there have been no clear indications that his successor, Cristina Fernandez de Kirchner, will adopt a different approach. At the same time, the partnership with the Petersen Group will allow Repsol to share the financial burden of meeting its continued commitments in Argentina. However, there have been no indications that the deal will result in any new investments over and above those already planned by Repsol in the country. Instead, the divestment of a stake in YPF will allow the Spanish company to continue its strategy of diversifying its upstream assets away from Argentina. For Repsol, production growth is expected to come from other areas apart from Argentina. However, this does not mean that YPF's production outlook will not improve in the future, especially if there is an improvement in the operating environment for energy investors. Its producing fields are declining, but there is the potential for new discoveries in Argentina, particularly in offshore areas. Ultimately for YPF, as with other companies present in the country, investments in new projects will require government assurances that they will receive favorable returns on their investments."

> "Ultimately for YPF, as with other companies present in the country, investments in new projects will require government assurances that they will receive favorable returns on their investments."
>
> — *Juliette Kerr*

A Guest Comment: Luciano Gremone: "In the past five years, YPF has been able to pay significant amounts of dividends while also reducing its financial debt to very conservative levels. We recognize that the company is currently underleveraged and could potentially raise debt in the future while maintaining strong credit ratios. However, YPF faces medium-term challenges mainly related to sustaining or increasing its production levels and maintaning an adequate average life of its reserve base, currently at 5.8 years (taking into account 2006 production levels). Given that the Petersen Group will finance the acquisition with sizable amounts of debt at a holding company level, this would add certain pressure on YPF to maintain its current aggressive dividend policy. This becomes particularly relevant in light of YPF's capital expenditure needs to maintain an adequate reserve base to avoid increasing its business risk profile. YPF's credit quality evolution would depend on the above-mentioned factors, the company's business plan, and expected financial policy with a new local partner (Repsol plans to announce its strategic plan during first-quarter 2008), and our perception of Repsol's incentives to support its subsidiary."

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