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FEATURED Q&A

Will Venezuela's Petro-Diplomacy Survive?

Q Henrique Capriles, the Venezuelan opposition leader running for president against Hugo Chávez, said on Aug. 1 that he would scrap preferential oil deals with foreign allies including Argentina, Cuba and others, Reuters reported. Capriles said the country would save $6.7 billion annually under his plan, money that he would use for domestic social spending. Meanwhile, state-run oil company PDVSA reportedly will need to set aside between $4 billion and $7 billion annually for the next five years to make payments on its heavy debt burden, analysts have forecast. Has Venezuela's petro-diplomacy run the end of its course? Which countries would suffer the most from an end to PetroCaribe and Venezuela's other preferential oil deals? If re-elected, will Chávez be able to maintain the agreements? How serious of a problem has PDVSA's debt burden become?

A Carlos Bellorin, senior petroleum analyst at IHS in London: "Venezuela's 'petro-diplomacy' hasn't run its course, but under a hypothetical Capriles administration, it will certainly be reduced to the necessary minimum and won't have the same relevance it had for the incumbent administration. Although, Capriles' approach suggests a strong focus on domestic affairs, Venezuela will still be a player in the region and the country will need international allies in order to secure a smooth transition and international recognition. I think Capriles and his petroleum policy advisors are smart enough to play this card wisely, placing internal rather than external affairs at the top of the agenda without isolating the country. However, Capriles has stressed that resources being used in 'petro-diplomacy' will be destined to tackle internal needs. The closest allies will suffer the most. Cuba and Nicaragua are the most exposed; they receive significant amounts of oil under very attractive conditions, thus helping their weak economies. All 'energy

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Unasur Nations Express Support for Ecuador in Assange Case

At a special meeting, members of Unasur voiced support for Ecuador in its standoff against Britain in the case of Julian Assange. The WikiLeaks founder spoke Sunday from the balcony of Ecuador's embassy in London, where he has lived for two months. See story on page 2.

Photo: Associated Press.

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NEWS BRIEFS

FARC Suspected of Attack on Colombian Pipeline

Colombian officials blamed the FARC for a pipeline attack on Sunday near the city of Tumaco, which had already been without power for more than a week after an attack on its electricity grid, the BBC reported. "We don't know why our town has been hit by this wave of violence, and we don't know what to do to combat it," said the mayor of Tumaco, where residents protested in the streets against a rise in attacks.

Diageo Eyeing Acquisition of Jose Cuervo for $3 Billion

London-based alcoholic beverage company **Diageo** is nearing a deal to acquire Jose Cuervo for $3 billion, according to a report in Britain's *Sunday Times*. The deal could be announced as early as Thursday and would be funded at least partially by shares, the newspaper reported without citing its sources. The tequila brand is currently owned by Mexico's Beckmann family. A Diageo spokeswoman declined to comment on the report.

Batista's EBX Group Struggling to Meet Goals

Brazilian billionaire Eike Batista has seen major losses from his energy and mining companies, jeopardizing his ability to meet his promised goal of generating earnings before interest, taxes, depreciation and amortization of $1 billion this year, Bloomberg News reported Friday. Analysts expect that the six companies that make up his **EBX** group will post a combined loss of 111 million reais. Batista's wealth reached a peak at the end of March at $34.5 billion, but declining stock prices plunged that figure to $20.6 billion last week.

Political News

Unasur Expresses Support for Ecuador in Assange Case

In a special meeting Sunday, the Union of South American Nations, or Unasur, expressed support for Ecuador amid its standoff with Britain in the case of Julian Assange. Ecuador's government on Thursday granted asylum to the WikiLeaks founder who has been holed up in the South American country's embassy in London since June. However, Britain has said it will not grant Assange safe passage out of the country and has threatened to revoke the embassy's diplomatic status, which could subject Assange to immediate arrest. Assange faces extradition to Sweden where he faces sexual assault allegations that he denies. "[Unasur] manifests its solidarity and backs the government of the Republic of Ecuador before the threat of violation of its diplomatic mission," Unasur nations said in a resolution issued after a special meeting in Guayaquil, Ecuador, *The Santiago Times* reported. Unasur's statement also said it urged "the parties to continue dialogue and direct negotiations in pursuit of mutually acceptable solution under international law." Although the Unasur nations condemned Britain's threat to enter the embassy to arrest Assange, they did not formally endorse Ecuador's decision to grant asylum to the WikiLeaks founder, the Associated Press reported. On Saturday, Argentina, Bolivia, Cuba, Nicaragua and Venezuela said they supported the asylum decision. However, Brazil, Chile, Colombia and Mexico are among the nations that have not chosen sides in the matter. On Sunday, Assange spoke from a balcony of the embassy, his first public appearance since entering the embassy two months ago. "I ask President Obama to do the right thing. The United States must renounce its witch hunt against WikiLeaks," he said, adding that the United States risks "dragging us all into a dark, repressive world in which journalists live under fear of prosecution." Assange and his backers claim that Sweden's attempt to extradite him is part of an effort to eventually bring him to the United States to face prosecution related to his secret-spilling Web site. Sweden denies the characterization. The White House did not comment on Sunday, but it said Saturday that the matter is an issue that Ecuador, Britain and Sweden should resolve, the AP reported.

> "I ask President Obama to do the right thing. The United States must renounce its witch hunt against WikiLeaks."
>
> — *Julian Assange*

Economic News

Venezuela's Economy Grew 5.4 Percent in Second Quarter

Venezuela's economy experienced 5.4 percent growth in this year's second quarter, more than twice the rate in the same period last year, Reuters reported Friday, citing the country's central bank. It was the seventh consecutive quarter of growth for Venezuela, where the government of President Hugo Chávez has boosted state spending ahead of the country's October presidential election. The non-oil sector grew 5.7 percent, while the oil sector rose 1 percent from April through June. A government-led program to build houses led the construction sector to post growth of 17.6 percent. "The economy is beginning an important reactivation and it's reflected in this figure. All economic activities grew during the second quarter, except mining," central bank chief Nelson Merentes told reporters Friday. In addition, Venezuela's government revised the first-quarter growth figure upward, to

Chávez

File Photo: Venezuelan Government.

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5.8 percent from 5.6 percent. Venezuela has outpaced the growth rate of approximately 5 percent that it budgeted for in 2012, said Finance Minster Jorge Giordani. Critics of Chávez's government have said that high oil revenues mean the economy should be doing even better and that high levels of government spending ahead of the election could lead to a "hangover," consisting of soaring debt and inflation and a potential currency devaluation. A poll by Venezuela-based **Varianzas** showed Chávez with a slim lead ahead of his challenger, Henrique Capriles. In the survey, Chávez had 49.3 percent support, as compared to Capriles' 47.5 percent, with 3.5 percent undecided, EFE reported. The poll of 2,000 respondents was conducted from Aug. 2-15 and had a margin of error of 2.16 percentage points. Opinion polls in Venezuela have varied widely, with most polls showing Chávez with a 15 to 20 percentage point lead over Capriles. Last Thursday, **Hinterlaces** released a poll showing 48 percent support for Chávez and 30 percent backing for Capriles, with 18 percent not answering and 4 percent saying they preferred neither candidate.

Company News

Banco Santander to Sell Shares in Mexican Unit

Spain's **Banco Santander** is planning to sell as much as 25 percent of its Mexican unit through a dual offering in Mexico City and New York, the bank said in a filing Thursday with the Mexican Stock Exchange, Dow Jones reported. Santander intends to sell as many as 422.5 million shares in Mexico, representing 6 percent of the unit, and as many as 1.27 billion shares in New York, representing 19 percent. Each American Depositary Share placed in New York would represent five Mexican shares. Santander is planning to retain control of the Mexican unit. In May, Dow Jones cited people familiar with the share sale as saying Santander wants to raise approximately $4 billion through the offering, which would value the bank's Mexican unit at more than $15 billion.

Featured Q&A

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cooperation agreements' (especially the one with Cuba) will be either broadly renegotiated or terminated. A total withdrawal of PetroCaribe won't be the right policy decision but a renegotiation of its conditions needs to be on the agenda. If Chávez is re-elected, I think he will be able to maintain the agreements since his administration gives a lot of weight to geopolitics and assuming a leadership role in the region. However, it is not and won't be sustainable to maintain all of them. PDVSA's debt burden is a serious issue because is increasing very fast. However, at this point, although the debt burden is significant, it is still manageable for a company the size of PDVSA under the current oil prices. The problem resides with channelling the majority of the debt generated to financing massive social spending instead of being used for oil industry investments. PDVSA's poor record of increasing production under this administration is well-known. Part of this problem comes from the lack of funding combined by sub-standard managerial capabilities, corruption and an erroneous operational lay-out."

Dan Hellinger, professor of political science at Webster University in St. Louis: "Capriles' figures are disingenuous. Most of the 'free' oil is sold to selected countries (and some poor communities in the United States) at discounted financing that kicks in when the price exceeds $40/barrel. In many cases, this involves barter arrangements, and both Chávez and Capriles can be creative in calculating the monetary value of discounts. In addition to approximately 70,000 barrels sold to Cuba under similar terms, about 98,000 barrels are sold at $27, mostly in exchange for services, which include thousands of Cuban medical personnel working in Barrio Adentro, the health care program. If elected, Capriles must choose between keeping his promise to maintain this program or ending the Cuban deal. Pedro Pérez, runner-up to Capriles in the opposition primary, said during his campaign that he would revise, not end the Cuban agreement. Capriles would face immense pressure on his right, but renegotiation would not surprise me. Cuba is clearly moving toward a mixed economy, and Venezuela might want a presence. Though he seemed to promise to end all oil discounts, Capriles did not explicitly promise to terminate agreements with Caricom nations. Oil discounts aimed at increasing Venezuelan influence in the Caribbean and Central America are not new; Carlos Andrés Pérez took a similar initiative during his first presidency, during the 1970s oil boom. Capriles surely would renegotiate and in some cases end oil discount programs, but his promise 'not to export one drop of free oil' is a populist ploy unlikely to be fully implemented, should he become president."

Risa Grais-Targow, Latin America associate at the Eurasia Group: "Between heavy domestic subsidies, oil-for-loan deals with China and petro-diplomacy programs like PetroCaribe, Venezuela is currently giving away around one third of its oil production at below-market prices. Among these programs, PetroCaribe and other foreign aid would be the least politically costly to cut. In the likely event that Chávez is re-elected, he will likely maintain these agreements. If, however, Chávez's health forces him to step aside and appoint a successor or the opposition manages to eke out a win, PetroCaribe's future would be in question. Whether PetroCaribe outlives Chávez will depend on his successor, but given that the program has been driven mostly by Chávez's own foreign policy preferences, the growing problems facing Venezuela's economy and the lackluster performance of state oil company PDVSA reduce the incentives for a future PSUV government to maintain the program. Should Capriles win, he has already indicated

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Featured Q&A

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that he would axe the program. The dismantling of PetroCaribe and other Venezuelan aid programs would significantly affect a number of recipient countries that depend on concessional financing and have avoided making politically unpalatable economic adjustments, with Nicaragua, the Dominican Republic and especially Cuba being the hardest hit. Venezuelan aid has helped enable the Castro regime gradually implement economic reforms while keeping a tight lid on any political opening. Without financing from Venezuela however, the Castro regime would likely be forced to speed up the pace of liberalization, which in turn could make it more challenging to contain demands for political reforms as well."

Asdrúbal Oliveros, director of Ecoanalítica in Caracas: "The first thing to analyze is the credibility of PDVSA's oil production goals. In the company's 2006 report, it set a goal of producing 5.8 million barrels a day (mb/d) of crude oil and liquid natural gas by 2012. Well, 2012 is here, and the most recent official oil production figures (from 2011) put oil production at 3.1 mb/d. This falls short of the goal by 2.7 mb/d, and there is no way that the company can increase oil production by this amount in what's left of the year. As long as PDVSA has to continue dabbling in the activities of other sectors, thereby neglecting its oil industry operations, its ambitious oil production goals will become less and less realistic. The only way PDVSA will even get close to meeting these oil production levels, and be able to regain any sort of credibility among oil industry players, is to totally focus all its energies on oil industry operations, eliminating all other distractions. Another point that has to be analyzed is PDVSA's financing capacity. Does the company have enough resources available to cover the investments it says it is planning?

> "[PDVSA's] ambitious oil production goals will become less and less realistic."
>
> — ***Asdrúbal Oliveros***

Looking at PDVSA's financial balances between 2006 and 2011, we have calculated incoming revenue and subtracted costs and spending (not including investment) and transfers made to the executive office (formal as well as social contributions). The resulting figure is the amount of resources available to the company to cover its investment projects. PDVSA had available resources enough to finance up to 74 percent (on average) of its investment plans; these resources coming from its main activity, the oil industry. This leaves 26 percent that the company was unable to cover by itself. This forces PDVSA to look to the foreign capital markets for financing, or as a last option, associate itself with private capital and creating a mixed company."

The Advisor *welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.*

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