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FEATURED Q&A

What's Ahead for Latin America's Oil Sector This Year?

Q The past year saw a number of major changes in Latin America's oil sector, with Mexico finalizing a long-anticipated reform to open its energy sector to foreign participation and a steep drop in oil prices late in the year putting pressure on major producing countries. What is the outlook for Latin America's oil sector this year? What are the countries and trends to watch in 2015?

A Jed Bailey, managing partner of Energy Narrative: "Latin America's oil sector will face a tumultuous year in 2015 as the events that have recently shaken global markets continue to play out. Most importantly, countries and companies must adapt to lower and more volatile oil prices. A few, including countries in Central America and the Caribbean that rely on imported diesel and fuel oil for electricity supply, will see immediate benefits. Others, most notably Venezuela, will face deep government budget shortfalls and sharply reduced foreign currency earnings, putting their economies under even greater pressure. For most countries, however, lower oil prices will be a mixed blessing. A strengthening dollar will limit the relative local currency decline in the price of imported oil products, and many will also be affected by falling prices in other commodities. Indeed, past periods of low oil prices have seen Latin America underperform relative to the United States and led to defaults on their dollar-denominated debt. Most countries are better prepared today than they were in past decades, but adjusting to their new economic circumstances will still be painful. Lower and volatile oil prices will also complicate efforts to attract upstream investment. This is most important for Mexico's critical Round One auction of upstream blocks, but Argentina, Peru and Colombia also face important tests in attracting and maintaining investor interest. Brazil in particular will face a daunting year as the Petrobras scandal evolves and companies reassess their appetite for high-cost deepwater exploration."

Continued on page 3

Rousseff Starts Second Term With Vows on Graft, Economy

Brazilian President Dilma Rousseff was sworn in on Thursday to begin her second term. In her inaugural address, Rousseff vowed to fight corruption amid the scandal at state-owned oil company Petrobras and also work to revive the economy. See story on page 2.

Photo: Brazilian Government.

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NEWS BRIEFS

Martelly, Parliamentary Leaders Reach Deal Over Extending Terms

Haitian President Michel Martelly has reached a deal with the presidents of the country's Senate and Chamber of Deputies to extend lawmakers' terms amid long-delayed elections, BBC News reported Tuesday. Under the agreement, which is subject to lawmakers' approval, deputies would remain in office until April 24, and senators would serve until Sept. 9. Absent a deal, lawmakers' terms would expire on Jan. 12. Elections have long been postponed due to a stalemate over electoral law. Martelly also has named former radio journalist Evans Paul as his new prime minister to replace Laurent Lamothe, who resigned last month.

Police Reportedly Arrest Dozens of Dissidents in Havana

Cuban dissidents say police arrested dozens of political activists who had been protesting outside of a jail in Havana on Tuesday, BBC News reported. The arrests came just a few hours before an open microphone protest was planned to take place in Havana's Revolution Square. The protest did not occur, but was aimed at testing if Cuba's government was more open to political dissident after announcing renewed diplomatic ties with the United States.

YPFB's VP Takes Control as CEO Seeks Cancer Treatment

Guillermo Acha, a vice president of Bolivia's state-owned oil company, **YPFB**, will take control of the firm temporarily beginning this week as CEO Carlos Villegas leaves the country to seek cancer treatment, President Evo Morales said Wednesday, EFE reported. Acha was previously in charge of **YPFB Refinación**.

Political News

Rousseff Begins Second Term With Vows on Corruption, Economy

Brazilian President Dilma Rousseff was sworn in to start her second term on Thursday, vowing to fight corruption and spur the economy, Agence France-Presse reported. Rousseff's administration has been beset by a widening corruption scandal at state-owned oil company **Petrobras** as well as an economy that has seen little growth during her time in office. The Petrobras scandal and continuing police investigation, known as "Operation Car Wash," have ensnared 39 people, including former directors of the oil company and construction firm executives. In the scheme, some $3.8 billion is believed to have been skimmed through inflated contracts to the benefit of political parties, including Rousseff's Workers' Party. "We are going to rigorously investigate everything that has happened," Rousseff said in her inaugural address. "We must investigate and punish, but without weakening Petrobras or diminishing its importance." The state-owned oil company is also facing legal action in the United States amid investors' losses related to the scandal. The graft scheme and the sluggish performance of Latin America's largest economy led to massive street protests during Rousseff's first term in office. In her inaugural speech, Rousseff said improving the economy is a major goal of her second term. "Brazil must return to the path of growth," said Rousseff, AFP reported. "We'll do this with the least sacrifice possible for the population, especially the most needy." Rousseff vowed to tighten the budget, boost investment and increase productivity, Bloomberg News reported.

> "Brazil must return to the path of growth."
>
> *— Dilma Rousseff*

Since first taking office four years ago, Brazil's budget deficit has more than tripled and economic growth has fallen to near zero, as compared to 7.5 percent growth in 2010. Inflation has also been higher than the midpoint of the central bank's target range throughout Rousseff's first term. Rousseff's new finance minister, Joaquim Levy, has vowed to pursue a 1.2 percent of gross domestic product budget surplus before interest payments this year, to rise to 2 percent of GDP next year and in 2017. On Dec. 29, Rousseff's government announced that it would reduce unemployment and pension benefits in order to save approximately 18 billion reais ($6.8 billion). Thirteen heads of state, mainly from Latin America, attended Rousseff's inauguration, as did the vice presidents of the United States and China, AFP reported.

Economic News

Venezuela's Maduro Promises Steps to Boost Economy

Venezuelan President Nicolás Maduro on Tuesday said his government would launch a "counter-offensive" to boost the Andean nation's economy, Bloomberg News reported. Maduro gave few details of his plan, though he said it would include reforms of the country's foreign-exchange system and also measures to trim unnecessary spending, including the possibility of cutting the staff sizes of foreign embassies. "We have created a new system, and there are many things to adjust and rectify," Maduro said in a televised address. "Plans for the economic recuperation will be revealed later." New measures would be announced on Saturday, he said. On Tuesday, Venezuela's central bank said the country's economy contracted in the first three quarters of 2014, Reuters reported. Gross domestic product shrank 4.8 percent in the first quarter, 4.9

Maduro

File Photo: Venezuelan Government.

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percent in the second quarter and 2.3 percent in the third, all year-on-year, the central bank said. Venezuela also has the world's highest rate of inflation. The annual rate of inflation reached 63.6 percent in November, the central bank said. The government has blamed political opponents for damaging the economy. Four months of anti-government protests in 2014 resulted in violence that left 43 people dead. "These actions against public order blocked the correct distribution of basic goods to the population, as well as the normal development of production of goods and services," the central bank said. "This resulted in an inflationary spike and a fall in economic activity." However, Maduro's opponents say that his socialist policies, along with those of his predecessor, the late Hugo Chávez, led the country into a downward economic spiral. "With one day of the year left, they publish the September, October and November figures. The highest in the world. Economic efficiency Nicolás! Wonderful," opposition leader Henrique Capriles said in a tweet, Reuters reported. Venezuela's government had last published inflation data in August.

Company News

Chile's High Court Won't Hear Barrick's Appeal in Fines Case

The Chilean Supreme Court has declined to hear **Barrick Gold**'s appeal of a lower-court decision involving fines imposed on the company's Pascua-Lama gold and silver project, *The Wall Street Journal* reported Wednesday. Earlier in the year, the country's Environment Court ruled that Chile's environment regulator improperly determined about $16 million in fines imposed on the Toronto-based company for permit infractions in 2013. Barrick appealed the decision to the Supreme Court, saying the fines were based on the law and common legal principles. The Supreme Court declined to hear the case, however, saying that the original action was brought against the regulator, known as SMA, and that Barrick was not a party to the case, Reuters reported.

Featured Q&A

Continued from page 1

A RoseAnne Franco, country and asset risk manager at Wood Mackenzie: "This year will be pivotal for Latin American oil and gas. The region has largely made a break with resource nationalism, with much of the region shifting toward resource maximization as governments focus on boosting value from their oil and gas resources. Mexico's recent liberalization exemplifies the trend, with the country launching its inaugural Round One in 2015. The tender will offer diverse opportunities, including deepwater, tight oil and heavy oil, among others. While Argentina promulgated its own hydrocarbon reform in October, expanding incentives and aligning fiscal terms, much of the industry will await the results of the October 2015 presidential elections; these should provide direction on the velocity of change and more economic certainty, which is critical to propel the country's unconventional segment. Meanwhile, Brazil is expected to be distracted by the recent allegations of wrongdoing against Petrobras and government officials, which will slow decision-making. That said, subsequent improvements in corporate governance could ultimately set the bar for NOCs in the region. Peru and Colombia both announced efforts in 2014 to reduce permitting times, and this year, regulators will focus on attempting to meet these targets. For the region's major oil producers such as Venezuela, the lower oil price environment will stress fiscal accounts, reducing maneuvering room and exacerbating political uncertainty. However, the overall trend for the industry is favorable as developments in Mexico and Argentina will likely cascade into more competitive terms throughout Latin America."

> "Developments in Mexico and Argentina will likely cascade into more competitive terms throughout Latin America."
>
> — *RoseAnne Franco*

A R. Kirk Sherr, president of Clearview Strategy Group, LLC: "Market analysts often seek to sugarcoat bad news, but for Latin America, all angles look bad today as oil prices continue to fall. Lower oil prices mean lower revenues for state-owned companies, pressure (and a likely redo) on their investment budgets, challenges meeting debt payments and less tax resources for the government. This is true from Mexico to Argentina. Lower oil prices also limit foreign investor enthusiasm while everyone tries to determine where the oil price bottom might be. Thus, ambitious sector-opening plans in Mexico may be delayed, and new offshore projects in Brazil look shaky. In this context, smaller producer countries (Colombia, Peru, Argentina) have even less to offer, considering they have few 'mega-projects' and small internal markets. Oil prices below $70 for any extended period will definitely have all but the largest investors looking outside the region—and prices are now trending below $60 for Mexican Maya crude (versus $98 a few short months ago). On top of the oil price issues, both Mexico and Brazil face daunting political challenges that further cloud the picture for investors well into 2015. Brazil is confronting an epic corruption scandal, with Petrobras at the heart of it. Mexico faces its own problems with serious questions about the rule of law emanating from the

> "There is only one big trend to watch in 2015—how low oil prices will go."
>
> — *R. Kirk Sherr*

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Featured Q&A

Continued from page 3

Iguala student teacher debacle. In short, there is only one big trend to watch in 2015—how low oil prices will go."

Luis E. Giusti, senior advisor at the Center for Strategic & International Studies and former chairman and CEO of PDVSA: "The reform of the oil and gas sector in Mexico after almost 80 years of being closed will mark a watershed of historic proportions in that country, but will also have important global ramifications. The bid round will feature 109 exploratory blocks as well as 60 fields that are either in production or have certified reserves. The reform will allow companies to book reserves and carry out both upstream and downstream projects without involving Pemex. Interest in Mexico's auction has been intense, even with oil prices on a downward slide. A timetable from January to September 2015 has been laid out for awarding the projects. The process will open brighter times for the Mexican oil industry, but even if it marches ahead without major hurdles, it will take a few years to turn around the current Mexican oil and gas situation. Meanwhile, the new wave of production increase in the United States is well beyond expectations. The IEA in its World Energy Outlook 2012 predicted that the shale basins Bakken, Eagle Ford, Niobrara and Permian combined would reach 3.2 million barrels per day in 2025. That level was achieved in early 2013, and it now stands at 4.8 million bpd. This revolution is having tremendous implications worldwide, among them major changes in the international supply lines, impact on oil prices and geopolitical implications. In the first half of 2015, Latin American oil and gas exporting countries—Colombia, Ecuador, Mexico, Venezuela and Peru—will suffer large reductions in export revenues and will struggle to keep their budgets in balance. Also, international capital will be more conservative in measuring risk and economic return, so new investment plans will take a hit. Meanwhile, lower oil prices will improve the economies of oil importing countries by improving their trade balances. Although many factors will intervene in the evolution of oil price during the second half of 2015, if prices continue to slide, a production cut will become likely. In addition, the continued fall in prices is reducing the incentive of stockpiling and could translate eventually into an escalation of prices."

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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