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THEDIALOGUE

FEATURED Q&A

Is Ecuador's Energy Policy on the Right Track?

Carlos Pareja was tapped in November to be Ecuador's oil minister at a time when the Andean country's energy sector is under much strain. // File Photo: Ecuadorean Government.

Q Analysts have said Ecuador could be producing twice as much oil as the roughly 550,000 barrels per day it currently produces, but add that it will be difficult to find investors needed to drive increased output, given the global drop in oil prices. Does Ecuador have the right strategies and policies in place to successfully develop its hydrocarbon resources in the current global context? Should the government focus on boosting other areas of the economy instead, as the price slump continues, or will growing oil output take on more priority as fiscal demands increase? How will OPEC's decision on Dec. 4 to maintain current production levels affect Latin American oil producers?

A Abelardo Pachano, president of Finanview in Ecuador, former CEO of Produbanco and former Ecuadorean central bank president: "Under the current conditions, it is quite difficult to find a way to increase Ecuadorean oil production. Since 2006, there haven't been any new developments in this area. In addition, if there are no changes in the energy production market, the government will not have the resources to accomplish the goal of increasing oil production. As of now, there are no clear economic policies for pursuing new private investments in this field. Hopefully, Ecuador is able to maintain the current level of production if the ITT oil field activates its production in early 2017. However, because of the natural decline of oil fields, especially those under private production, net results will offer no more than 470,000 barrels per day by 2020. Exploiting the mineral sector (gold and copper) in the Amazon forest area could be the only solution, with the

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Venezuela's Maduro Seeks Emergency Economic Powers

President Nicolás Maduro's government is seeking emergency economic powers to address the country's deteriorating economy.

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Walmex Planning to Sell Suburbia Clothing Stores

Wal-Mart de México said it is eyeing the sale of its clothing store chain in order to focus more on its core business.

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ECONOMIC

Brazil Won't See Economic Growth Until 2018: IMF

The International Monetary Find said today that Brazil's economy will contract this year and stagnate next year. In the meantime, Brazil's new finance minister, Nelson Barbosa, said the government must shrink its budget in order for the country to emerge from its recession.

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Barbosa // File Photo: Brazilian Government.

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ECONOMIC NEWS

Brazil Won't See Economic Growth Until 2018: IMF

Brazil's economy will not see any economic growth until at least 2018, the International Monetary Fund said today, Bloomberg News reported. A lack of growth until then in Latin America's largest economy would mark the longest period of economic contraction and stagnation in more than a century. The IMF cut its 2017 economic forecast for Brazil to stagnation in an update to its World Economic Outlook report. Previously, the lender had

The IMF said Brazil's economy will shrink 3.5 percent this year and stagnate next year.

forecast 2.3 percent growth for Brazil in 2017. The IMF also updated its outlook for Brazil this year, saying the economy will shrink 3.5 percent in 2016 after a contraction of 3.8 percent last year. A litany of problems, including falling commodity prices and the massive corruption scandal at state-run oil company Petrobras have taken a toll on consumer confidence in the country. "The recession caused by political uncertainty amid continued fallout from the Petrobras investigation is proving to be deeper and more protracted than previously expected," the IMF said in its latest report. "Economic distress" in Brazil and other countries will cause an economic contraction of 0.3 percent this year in Latin America and the Caribbean, the lender added in the report. The IMF also cited Brazil's deep recession as a major factor in its downward revision to its global economic outlook for 2016 and 2017. On Monday, Brazil's new finance minister, Nelson Barbosa, said the government must shrink its budget in order to emerge from the recession and curb inflation, The Wall Street Journal reported. An improvement in Brazil's fiscal situation depends largely on Congress, said Barbosa. Lawmakers, however, have resisted the Rousseff administration's attempts to pass fiscal austerity measures. "Our biggest challenge is the fiscal one," Barbosa told reporters before leaving the World Economic Forum in Davos, Switzerland. "All [politicians] understand its importance." Barbosa became finance minister last month, replacing Joaquim Levy, who was frustrated in his attempts through Congress to control the deficit.

Venezuela's Maduro Seeks Emergency Economic Powers

The government of Venezuelan President Nicolás Maduro on Friday announced a 60-day state of emergency to intervene in the country's worsening economic crisis, BBC News reported. The government made the announcement just hours before Maduro delivered his State of Nation address before the National Assembly for the first time since his center-right opponents took office. The edict must be passed by the National Assembly in order to take effect. The state of emergency would give Maduro

Maduro // File Photo: Venezuelan Government.

wider powers to intervene in companies and to limit access to currency. The edict would also allow for tax increases and would put emergency measures in place to pay for welfare services and food imports. Annual inflation up to September 2014 is said to have reached 141 percent, according to the Venezuelan central bank, and official figures show that Venezuela's economy contracted by 4.5 percent in the first nine months of 2015. In light of the global drop in oil prices, Venezuela's revenues for oil

NEWS BRIEFS

Foreign Govt's Should Boost Colombia Funding: World Bank's Kim

Foreign governments should increase their funding commitments to Colombia as the South American country seeks to end its five-decade armed conflict, World Bank President Jim Yong Kim said Thursday, the Associated Press reported. Other countries should "unfailingly support" Colombia, said Kim.

Mexican Authorities Seek to Question Actress in Case of 'El Chapo'

Mexican authorities have called Mexican actress Kate del Castillo in for questioning over her links to imprisoned drug cartel leader Joaquín "El Chapo" Guzmán, BBC News reported Monday. Del Castillo in October set up a meeting and interview between El Chapo and Hollywood actor Sean Penn, whose interview was recently published in U.S. magazine Rolling Stone. The contact between the cartel leader and del Castillo helped Mexican authorities capture El Chapo, who had escaped from prison some six months earlier.

Chilean Officials Uphold Permit for Hydroelectric Dams Despite Protest

A Chilean ministerial committee on Monday upheld the environmental permit for Energía Austral, a joint venture between mining and trading company Glencore and Australian power company Origin Energy, to continue building its Cuervo hydroelectric dams, Reuters reported Monday. The committee dismissed nearly a dozen complaints that had been filed against the project by environmental and citizens' groups. The groups had argued that the two dams slated to be built in Chile's Aysen region would hurt local wildlife and would inhibit tourism to the region.

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potential of replacing current oil resources lost by price reduction. However, this option would take no less than four to five years. In order to re-establish economic equilibrium, the only option is to reduce fiscal expenditure. The government is too large for the Ecuadorean economy to maintain. Finally, the Dec. 4 OPEC decision confirms the group's strategy to defend market shares no matter what happens with the price. In that sense, petroleum-producing countries in Latin America will continue to face great losses in their economies. For Ecuador, this means no less than 7 percent of GDP."

Jose L. Valera, partner at Mayer Brown LLP: "OPEC's decision on Dec. 4 to maintain current production levels is a hard blow to Ecuador as lower export revenues directly affect government budget revenues. Crude oil and related products account for over 50 percent of Ecuador's exports and one-third of government revenues. Remaining exports are mainly bananas, shrimp, gold and other primarily agricultural products. Given its excessive dependence on the export of commodities and the current down-cycle, Ecuador should both change its present policies for the development of its hydrocarbon resources and boost other areas of the economy away from commodities and toward services and value-added products. Ecuador's current policy to develop its hydrocarbon resources is to use state-owned companies and, to a lesser extent, private sector companies. The latter are currently allowed to operate through service contracts only, pursuant to which the contractor bears all exploration and production risks and costs and is remunerated with a fixed fee on the basis of units of production delivered to the state. Costs are reimbursed out of production. The contractor pays income taxes on its fee income. These arrangements do not offer upsides for the companies. Because the fee is fixed, in the good times they do not benefit from increases in the value of production. Naturally, these arrangements only attract true service companies and not the companies that have the incentive to risk capital in exploration. Exploration, therefore, falls on the state-owned companies, and therein lies the problem: Because of the government's voracious appetite for the money that these companies generate from production and exports, they are not left with sufficient capital and means to acquire operating capacity and technology to properly develop the country's resources and replenish reserves through exploration programs. The law allows for greater incentives to the private sector, but the government's policy remains unchanged."

> **"OPEC's decision on Dec. 4 to maintain current production levels is a hard blow to Ecuador."**
>
> **— Jose L. Valera**

Mario Alejandro Flor, partner at Bustamante & Bustamante: "Although the state-owned petroleum enterprise's installed capacity is good for processing at least 450,000 barrels a day, plummeting oil prices have made it necessary to make decisions this year. The Ecuadorean government has responded by reducing production by 2.6 percent, which is equal to almost 10,000 barrels a day; and by cutting the public petroleum budget by 24.3 percent, equal to a $1.137 billion adjustment, the biggest cut being in investment. The drop in the price per barrel could also mean that the state would seek a renegotiation of the service contracts in effect with private companies. In most cases, the sale price of crude oil is below the agreed tariff. The decision that OPEC made on Dec. 4 merely confirms the prediction that international oil production exports have fallen by 60 percent. Oil exports typically account for as much as 90 percent of Venezuela's annual revenue. Maduro and new Economy Minister Luís Salas have argued for protecting social programs established by Maduro's predecessor, late President Hugo Chávez, and the government has blamed high inflation and shortages of basic goods on its political opponents.

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BUSINESS NEWS

Walmex Eyes Sale of Clothing Store Chain

Wal-Mart de México announced Monday that it is planning to sell Suburbia, its clothing store chain, in an effort to focus more heavily on its core big-box retail store business, The Wall Street Journal reported. Walmex said it will begin considering offers for Suburbia, which has 117 stores in 29 states in Mexico and accounted for 3.5 percent of Walmex's total sales in 2014. The retailer's plan to sell Suburbia is in its early stages and may not even result in a sale of the clothing store chain, Walmex said. In recent years, Walmex has shed non-core assets, including its casual dining chain Alsea and its bank unit to Grupo Financiero Inbursa. Last week, Walmex, Mexico's largest retailer, named Guilherme Loureiro as its new chief executive officer as of Feb. 1. Loureiro, who previously served as Wal-Mart's CEO for Brazil, will take over from Enrique Ostale as chief executive for Mexico and Central America. Ostale will remain CEO of Wal-Mart Latin America, the company said, Reuters reported.

Loureiro // File Photo: Wal-Mart Stores.

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will not decline until the big players (the United States, OPEC and Europe) reach a common agreement. The Ecuadorean government is currently undergoing a financial restructuring for managing the resources obtained because of low oil prices. The idea is to also optimize the technology employed in the production of hydrocarbons. This is the case of the retrofitting of the Esmeraldas Refinery for it to be able to refine up to 110,000 barrels a day, as well as optimizing the generation of the electricity required by oil fields so operations can be sustainable. This will not be enough, though. Ecuador's huge dependence on oil has once again taken its toll."

> **"Ecuador's huge dependence on oil has once again taken its toll."**
>
> **— Mario Alejandro Flor**

Francisco X. Swett, chairman of Pallas Management Corp. and former Ecuadorean minister of finance, member of Congress and central bank president: "Ecuador's oil prospects are about as dark as the color of crude. These days, prices are below the referential $35 per barrel minimum used to construct a budget. Although basing the budget on a low oil price signals a downward trend in fiscal expansion, the budget is still full of assumptions and gimmicks, including using bank and social security reserves to purchase government bonds. Tax receipts have followed the way of the economy and started to fall, adding to pressures. Production has fallen by 17,000 barrels due to lower investment outlays. Yasuní exploration is not feasible. The oil services contracts which replaced the old concession agreements have to be renegotiated to avoid additional negative cash flow. The arbitration award in favor of Oxy will add another $1.6 billion in obligations and has essentially settled the case in favor of Andes Petroleum, the Chinese concern that bought 40 percent of Oxy's interest and unleashed the spat between the government and the company. Lower prices require delivery of more barrels of oil to cover oil-advances made to Petroecuador, and the central government budget has no oil income to support ongoing fiscal programs, adding to Correa's current political woes. Ecuador has received in excess of $120 billion in oil income since 1974, but it does not have a lot to show for it. Except for few manifestations of friendly policies, the period has been marked by hostilities and legal insecurity for investors. The country indeed has the potential to double production, but neither the market nor Ecuador's political establishment support that outcome in the near term."

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

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