INTER-AMERICAN DIALOGUE'S
LATIN AMERICA ADVISOR ▸ ENERGY

FEATURED Q&A

How Will Energy Partnerships With China Affect the Region?

Q **Chinese Vice President Xi Jinping last week visited Venezuela and Brazil, two countries hoping to boost their oil exports to China in the next few years. How will these energy partnerships develop? Will greater Chinese engagement significantly change these countries' energy sectors?**

A **Guest Comment: Jiang Shixue:** "To a certain extent, the Chinese economy is energy-intensive. On the one hand, China's own energy resource is not enough for its rapid economic growth. So China hopes to import energy from foreign countries, including Venezuela and Brazil. On the other hand, many countries in Latin America have their own relative advantage, *i.e.* huge reserves of energy. In the age of globalization, South-South cooperation has acquired both necessity and momentum of development. China's relation with Latin America is part of South-South cooperation, and this bilateral relationship is mutually beneficial. Both Venezuela and Brazil, along with many other Latin American countries, need foreign capital and technology to develop their energy sectors. Therefore, there is a golden opportunity for China to make more investment in the energy sectors of the region. As a matter of fact, Latin America's energy sectors are open to every country in the world, and China is only one of the partners. Regarding oil exports to China, we have to take the factor of geographical distance into consideration. While an oil tank can reach the United States coast in a week or so, it will take one month to travel across the Pacific. As a result, economically speaking, it might be hard to increase the amount of oil exports to China from Venezuela and Brazil. Moreover, we have to understand that China does not have enough refinery capacity for Venezuela's

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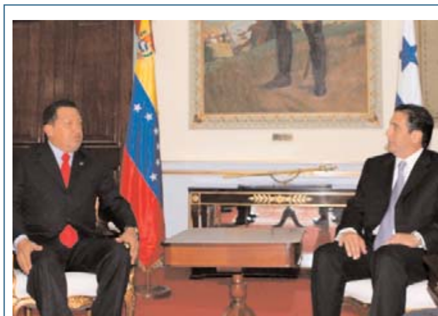

Torrijos to Chavez: Panama Wants to Join Petrocaribe

Panamanian President Martin Torrijos (R) this week asked Venezuelan President Hugo Chavez (L) for entry into Petrocaribe, which would allow Panama to buy Venezuelan oil on preferential terms. See brief on page 2.

Photo: Panamanian Government.

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ENERGY SECTOR BRIEFS

VetcoGray to Supply OGX With Well Heads for Subsea Drilling

Brazil-based **VetcoGray**, a unit of **GE Oil & Gas**, on Monday announced it signed a four-year frame agreement to supply Brazilian oil and gas company **OGX** with subsea well heads and casing strings. The deal, which will cover as many as 50 wells in several offshore blocks in the Campos, Santos, Espirito Santo and Para-Maranhao basins, is one of the largest ever for the company in Brazil, VetcoGray said in a press release. No financial details of the deal were released.

Panamanian President Asks Chavez for Entry into Petrocaribe

Panamanian President Martin Torrijos during a trip to Caracas has asked Venezuelan President Hugo Chavez to allow the Central American country to join discount oil program Petrocaribe, Venezuelan daily *El Universal* reported Wednesday. Torrijos said Panama's membership in Petrocaribe would give the country "enhanced possibilities to propose new agreements and tighten the ties among our countries to seek integration mechanisms," reported Spanish wire service EFE.

Pemex May Look For Up to $10.5 Bn to Fund Investment Plan

Mexico's state-owned oil company **Pemex** is planning to seek up to $10.5 billion in financing to fund spending on exploration and production, Bloomberg News reported Tuesday. Pemex may seek as much as $6 billion from local and international debt issues, $2.5 billion in loans from financial institutions and $2 billion from export-import agency loans, Chief Financial Officer Esteban Levin told analysts Tuesday in a conference call.

Oil & Gas News

PDVSA Seeking to Cut Costs by Renegotiating Service Contracts

Venezuela's state-run oil company, **Petroleos de Venezuela** (PDVSA) said Tuesday that the company plans to cut its costs by 40 percent, the Associated Press reported. Rafael Ramirez, who is also Venezuela's oil and energy minister, said the company will no longer pay the "high prices" that it negotiated with service companies last year when oil prices peaked at $147 a barrel. PDVSA's finances have been hurt by the plunge in the price of crude, which is trading at around $43 a barrel in New York. Ramirez says PDVSA will renegotiate contracts with nearly 250 service providers. Ramirez added Venezuela will call on other OPEC member countries to cut production in order to force prices up to $70 a barrel, the Voice of America and wire services reported. Members of the oil cartel will meet later this month in Austria.

Ramirez

File Photo: Venezuelan Government.

Ecuador Plans to Seize 70 Percent of Perenco's Oil Output in Tax Dispute

Ecuador will keep 70 percent of French oil company **Perenco**'s oil output until the company and the country resolve a tax dispute involving hundreds of millions of dollars, Bloomberg News reported Thursday. Ecuador says Perenco owes $338 million in back taxes plus interest after the country hiked windfall tax rates from 50 to 99 percent on oil companies in October 2007. Ecuador will seize the portion of the company's oil, including 720,000 barrels of oil ready to be shipped from the port of Balao near Esmereldas, said Minister Derlis Palacios. The company will retain the share of Perenco's output until the tax issue is resolved or the debt is paid off, Palacios said. "We're open to any negotiation; what we've withheld up to the date of a deal will be credited to the repayment of the debt," Palacios said. "Ecuador will auction off or sell that oil until the value of the debt has been recovered." A Perenco spokeswoman in London declined to comment. Ecuador and the company have not been able to reach an agreement because of opposition by **Burlington Resources**, a unit of **ConocoPhillips**, Palacios said. Burlington Resources has a minority stake in Perenco's three oil fields in Ecuador. Houston-based ConocoPhillips is seeking relief from the tax hike before the World Bank's International Center for the Settlement of Investment Disputes and has asked the body to prohibit Ecuador from seizing the oil, said company spokesman Charlie Rowton. "We would be happy to find an amicable settlement," he said.

> "Ecuador will auction off or sell that oil until the value of the debt has been recovered."
>
> *— Derlis Palacios*

Colombia's State Oil Company Plans $8.1 Billion Bond Offering

Ecopetrol, Colombia's state-run oil company, is planning an $8.1 billion bond offering to finance its investment plan, reported Bloomberg News. The company's shareholders will consider the bond sale during a March 26 meeting, the company said Tuesday. The bonds would be sold in Colombia and other countries and would fund Ecopetrol's investments through 2011. The company's president Javier Gutierrez, is moving forward with plans to spend $60 billion through 2015 despite the falling price of crude. By next year, Ecopetrol plans to increase its investments by 35 percent to $6.22 billion, which includes refineries and oil fields. The company wants to produce 1 million barrels a day, which would nearly double its production. [Editor's Note: see related Q&A in the Feb. 27 issue of the *Energy Advisor*.] In related news, Ecopetrol said Wednesday it reached a deal to buy out Swiss firm **Glencore**'s stake in the Cartagena refinery for $549 million. Last week, Glencore said it was unable to secure the financing to move forward with an upgrade to the refinery, and would sell its 51 percent stake. Ecopetrol, which already owns the remainder of the refinery, said in a statement that the two companies will complete the sale within 90 days but that the price could change, reported Dow Jones. On Thursday, the executive of the Colombian unit of Brazilian national oil company **Petrobras** said his company was studying whether it might be interested in purchasing the share of the project formerly belonging to Glencore, reported Colombian paper *La Republica*.

Canadian Companies Start Testing on Disputed Trinidad Well

Canadian firms **Canadian Superior Energy** and **Challenger Energy** have begun testing the potential of a natural gas well in Trinidad and Tobago that has been at the center of a dispute with a third partner, The Canadian Press reported Tuesday. Preliminary tests on the Endeavour well, located 58 miles east of the country, indicated it has a peak flow rate of 56.4 million cubic feet daily, said the companies. Canadian Superior had been operating the well with a 45 percent stake, however a court in Alberta last month sided with United Kingdom-based **BG Group** to take control away from Canadian Superior. BG Group had expressed concern that testing on the well would not be completed under the original ownership structure, in which BG Group had 30 percent ownership and Challenger had a 25 percent stake. Last Friday, Challenger sought court protection from its creditors under the Companies' Creditors Arrangement Act. Challenger said it would retain its stake in the well at the same time it continues to seek other alternatives, including selling the company. **Deloitte** was appointed receiver for Canadian Superior's portion of exploration of Block 5c, which contains the Bounty and Victory wells in addition to Endeavour.

Power Sector News

Brazilian Environmental Officials Allow Nuclear Plant Construction

Brazil's environmental regulator Ibama on Wednesday awarded a permit to allow construction of a nuclear power plant along the southern coast of Rio de Janeiro state to resume, Agence France-Presse reported. The plant is the third facility in the Angra complex, and is located on Itaorna beach near the town of Angra dos

Angra complex

Photo: Eletronuclear.

Reis. It will have a thermal power capacity of 3,765 megawatts (MW) and electrical power capacity of 1,350 MW, according to Ibama. In all, Angra I, II and III will generate enough energy to power the city of Rio de Janeiro. Construction of the Angra III plant had been stalled for more than two decades. Now that the institute has approved the permit, the state-run electricity company **Eletrobras Thermonuclear** (Eletronuclear) can restart the project. The environmental permit, valid for six years, comes with a set of 44 conditions that Electronuclear must follow. Among the mandates are requirements for proper disposal of fuel waste. Eletronuclear also has 120 days to submit a plan to improve a road that connects Angra dos Reis to the colonial town of Paraty, a popular tourist site. The improvements are to focus on transit security and monitoring. Route 101 is designated as an evacuation route in the event of an accident. Eletronuclear's president, Otho Luiz Pinheiro said in 2007 that Brazil intends to build eight more nuclear power plants by 2030. The first would be built in 2017 in the northeast part of the country. Angra III is expected to be on line between 2012 and 2013.

Iberdrola to Build 103 MW Wind Park in Mexico's Oaxaca State

Spanish firm **Iberdrola Renovables** said Wednesday it won a contract from Mexico's **Federal Electricity Commission** (CFE) to build a 103 MW wind park in Oaxaca state, Mexico's wind energy capital. Construction of La Venta III is scheduled to begin in May with the park expected to begin commercial operation by November 2010, the company said in a Web site press release. "The start-up of the La Venta III wind farm will contribute to the economic development of the state of Oaxaca, one of the most promising areas in Mexico for the development of wind farms due to its high wind levels," Iberdrola said. The wind farm will rely on 121 G52 turbines built by Spanish manufacturer **Gamesa Eolica**, enough to meet the energy needs of approximately 200,000 people, according to the release. The 20-year contract to supply energy to the CFE follows a public bidding round in which Iberdrola submitted the only bid deemed technically solvent by the CFE. Oaxaca will also be home to the largest wind complex in Latin America, the $780 million La Ventosa project jointly developed by Iberdrola, Spain's **Acciona**, and Mexican cement maker **Cemex**, which was inaugurated in January, reported EFE. In related news, Iberdrola on Tuesday entered into preliminary agreement with Russian electric company **Inter Rao** to collaborate on electric projects around the world, including those in Latin America. Inter Rao currently has stakes in companies in 14 countries across Europe and Asia, but the deal signed this week would allow its first penetration into the Latin American market, Iberdrola said on its Web site. [Editor's Note: see related Q&A in the Feb. 6 issue of the *Energy Advisor*.]

Biofuels News

Unica Says Growth of Brazil's Ethanol Mills Will Slow in 2009

Brazil's main association of sugar producers, Unica, said Tuesday that construction of new sugar mills would slow in 2009 due to the credit crunch, reported Reuters. "We initially expected 35 mills to start this year, but between only 15 and 20 should come on stream, and we don't know exactly in which month," said Antonio de Padua Rodrigues, technical director at Unica. Last year, the industry opened 27 mills out of 80 planned through 2012. Padua said the need for cash could force companies to sell ethanol at lower prices, adversely affecting profits. He also predicted producers will boost the share of their crop that goes toward making sugar from 40 percent last year to 43 percent in 2009. In related news, UK oil giant **BP** and Brazilian state energy company **Petrobras** this week confirmed significant long-term investments in Brazil's ethanol industry. BP CEO Tony Hayward said his company will invest between $5 billion and $6 billion in ethanol production in Brazil over the next 10 years, according an internal BP publication cited on Unica's Web site. Last April, BP entered Brazil's ethanol industry with an investment of $683 million in **Tropical BioEnergia**, its joint venture with Brazilian firms **SantelisaVale** and **Grupo Maeda**. Petrobras on Wednesday provided further details on its biofuels spending under the the firm's five-year strategic plan. The company said its biofuels unit will invest $2.4 billion in biodiesel and ethanol production through 2013, in addition to $400 million set aside for transportation infrastructure like ethanol pipelines, and $530 million for biofuels research, according to a Web site press release. Petrobras said 91 percent of its investments in biofuels production will be made in Brazil, and that it

Padua

File Photo: Unica.

Advisor Q&A

How is the Plummeting Peso Affecting Mexico's Economy?

Excerpted from the Feb. 27 issue of the Dialogue's daily **Advisor**

Q Countries in the Caribbean faced fiscal challenges even during relatively good times for Latin America over the past few years, and the current external crisis adds a downturn in tourism receipts and remittances. Which countries in the Caribbean are better prepared and why? Which nations face the toughest outlook and how bad might it get?

A Guest Comment: Andrés Rozental: "The Central Bank has been defending the peso against what I believe is an unstoppable worldwide flight to quality and investor search for safety. Banco de Mexico has spent close to a third of the country's reserves auctioning dollars without any appreciable impact on the declining value of the currency. What is different this time from previous speculative assaults on the peso is the fact that almost all major currencies, from emerging markets to developed economies, have lost value since the financial crisis began last fall. Paradoxically, the US dollar continues to be the currency of choice for many investors, in spite of negligible interest rates and a seriously wounded economy. For Mexico, the devaluation of the peso has a bright side in that it makes Mexico's exports more competitive and reduces the appetite for imports, paving the way for a more dynamic domestic economic performance once our major export market, the United States, recovers. However, perceptions always play an important role in how public opinion views the peso's 50 percent fall over such a short period of time, bringing back haunting memories of major devaluations in the past. At almost 15 pesos to the dollar today, I believe our currency is now considerably undervalued, given the strength of the country's banking sector and the basic fiscal, economic and energy reforms recently enacted. Although some analysts believe that the peso will stabilize as soon as confidence returns to the global marketplace, experience has shown that once a major devaluation takes hold it is difficult to return to the *status quo ante.* "

A Guest Comment: Pamela Starr: "It's hardly surprising that the Mexican peso has lost more than a third of its value in the past six months given Mexico's enormous economic reliance on the US market. The peso's dive reflects an economy predicted to contract between 1.5 and 2 percent this year, a manufacturing implosion, unemployment levels not seen since 1995 and a rapidly expanding current account deficit. The Central Bank's efforts are focused on the speculative drivers of the peso's fall to thereby moderate its size and pace and to prevent it from metamorphosing into a speculative run. The size of the Central Bank's reserves and its swap line with the Fed suggests it will be successful, but at the price of a large and still increasing peso depreciation that will have serious economic repercussions. The Bank's capacity to stimulate the economy through interest rate cuts is being constrained by the inflationary implications of the peso's fall. Corporate balance sheets are feeling the heat of this unexpected surge in the peso price of dollar debt repayments. And peso instability further discourages already scarce capital inflows. A bad situation indeed, yet with at least one upside: the counter-cyclical stimulus created by a 33 percent increase in the peso purchasing power of remittance flows."

Andrés Rozental *is president of Rozental & Asociados, and former deputy foreign minister of Mexico.*

Pamela Starr *is associate director of the Latin America Initiative at the University of Southern California, where she is a senior fellow at the USC Center on Public Diplomacy.*

aimed through partnerships to increase ethanol production to 3.7 billion liters by 2013, split roughly in half between the foreign and domestic markets.

Economic News

Geithner: Obama Will Move Forward With Colombia, Panama FTAs

US President Barack Obama will work with members of Congress to advance free-trade agreements with Colombia, Panama and South Korea, US Treasury Secretary Timothy Geithner told a congressional committee Tuesday, according to Reuters. "What you can expect is the president and the administration will work carefully with the Congress to find a way to move forward on those important agreements," Geithner told the House Ways and Means Committee. During his campaign, Obama had opposed the trade accords with Colombia and South Korea. However, he has warmed to them since taking office. On Monday, the US Trade Representative office's annual trade report said the Obama administration is seeking relatively quick congressional approval of the agreement with Panama and also hoped to move forward with establishing "benchmarks" for the long-stalled pacts with Colombia and South Korea. During his campaign, Obama said he was looking to Colombia to fight violence against trade union members. Former US President George W. Bush's administration wanted Congress to consider the more-controversial Colombian agreement before the Panamanian one because they were concluded in that order. However, Sen. Charles Grassley (R-IA), the highest-ranking Republican on the Senate Finance Committee, said he would consider looking at the agreement with Panama before the others "as long as we turn to our pending agreements with Colombia and South Korea right afterward." In a letter Tuesday to members of Congress, Lori Wallach, the director of Public Citizen's Global Trade Watch division, said approval of the accord with Panama would hinder congressional efforts to halt abuse of foreign tax havens. "Panama has long been a key target of the Organization for Economic Co-operation and Development and other tax transparency entities for its resistance to international norms in combating tax evasion and money laundering," she said. In a letter last week, 53 Democrats and one Republican in the House of Representatives told Obama they stood opposed to all three pacts.

Geithner

File Photo: US Treasury Department

Despite Economic Slowdown, Lula Vows to Continue Spending

Despite the global economic crisis, Brazilian President Luiz Inacio Lula da Silva said Monday that his government does not plan to slow spending, Bloomberg News reported. "There's no hypothesis under which Brazil will lower by even a dollar planned investments," Lula told business leaders in Sao Paulo, adding state-owned oil company Petrobras will continue with its spending plan. "We won't lower Petrobras investments by a single dollar." Economic growth stalled in the fourth quarter of last year amid slumping demand and falling commodities prices.

Political News

Raul Castro Ousts Several Fidel Loyalists in Cuba Cabinet Shakeup

Cuban President Raul Castro on Monday ousted several cabinet members who for years had been loyal to Castro's brother, ailing former President Fidel Castro, the Associated Press reported. The most prominent cabinet member to be booted was Foreign Minister Felipe Perez Roque, 43, who had served for nearly a decade and had often been seen as a possible future president. He was replaced by his deputy, Bruno Rodriguez, who previously was Cuba's ambassador to the United Nations. The shakeup raised doubts about how much, or how little, power Fidel Castro retains. Vicki Huddleston, a former chief of mission in the US Interests Section in Havana said the changes raise questions about Fidel's influence. "This would seem to indicate this is a consolidation of Raul, which then makes you think, 'What about Fidel?' " she said. Cuban Vice President Carlos Lage was stripped of his cabinet secretary office, which was given to Gen. Jose Amado Ricardo Guerra, who had been a top military official under Raul Castro before he took over as president. Lage had been credited with saving Cuba's economy after the Soviet Union's collapse. On Thursday, Perez Roque and Lage resigned from all government and Communist Party positions. Also sacked was Cuban Economy Minister Jose Luis Rodriguez, who was replaced by Internal Commerce Minister Marino Murillo Jorge. Also Finance Minister Georgina Barreiro Fajardo was replaced by Lina Pedraza Rodriguez, a member of the Central Committee of the Communist Party Secretariat. Jose Miguel Miyar Barruecos, was ousted as secretary of the Council of State but moved to the vacant science and environment minister position. He was replaced by Homero Acosta Alvarez, a close confidant of Raul's from his time as defense minister.

Chavez Orders Troops into Rice Processing Companies

Venezuelan President Hugo Chavez on Saturday ordered soldiers into rice processing companies, stating some of the businesses have refused to produce their product for sale at regulated prices, the Associated Press reported. The companies say price controls set by the government in order to contain inflation have are too low and don't allow for profits. Some had threatened to slow or stop production, but any that do will be expropriated, said Chavez. "I don't have any problem expropriating," Chavez said. "And I'll pay them with paper, too. Don't think I'll pay them with hard cash." On Wednesday, Chavez ordered the expropriation of US-based **Cargill**, alleging it distributed rice without printing the government-mandated price on its packaging, reported wire services. Chavez also threatened to take over Venezuelan company **Polar**, the country's largest food manufacturer, saying, "Get the decrees ready, one after the other."

Featured Q&A

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heavy oil. Oil companies from the United States and other Western countries have been operating in Latin America's energy sector for decades, and China is only a newcomer. So I don't think China's presence will soon change these countries' energy sectors, and the US dominance in Latin America's energy sector will not be challenged."

A **Guest Comment: Nelson Altamirano:** "The energy partnerships between China and the two South American countries cannot be seen independently from the Chinese partnership with Saudi Arabia and African oil partners. Saudi Arabia is the main Chinese energy partner and will remain so because it can satisfy both China and the United States with no conflict at all. Can Venezuela be the second partner? This partnership depends on developing new oil resources in the Faja and refineries in China. These projects may need the influx of a third private partner with technological and financial weight. It is not realistic to think that China National Petroleum Company (CNPC) and PDVSA alone will carry the costs of their ambitious projects. At least, this is not the way CNPC and Saudi Aramco already managed to bring in 1 million bpd into China. In addition, the partnership between China and Venezuela depends on how fast the Chinese convince the Chavez administration that the export target of 1 million bpd by 2012 does not substitute the exports to the United States. There must be a supply and demand balance for the world largest economies. Given the current world economic conditions, low oil prices and big social spending projects in Venezuela, I see the greater involvement of China in the Venezuelan energy sector as a positive element that may bring balance and pragmatism to the Venezuelan energy policy. If played right, the Chinese may be the stone needed to re-launch the development of the Faja."

A **Guest Comment: R. Evan Ellis:** "The recently completed five-nation trip to Latin America by Chinese Vice-President Xi Jinping highlights the diverse basket of investments that the People's Republic of China (PRC) is making in Latin America in support of its global search for energy security, as well as the impact of those bets on Latin America itself. Venezuela is the high-risk, highest-payoff component of China's Latin America energy portfolio. The national oil company PDVSA's plans to increase exports to the PRC from 364,000 barrels per day currently to 1 million barrels per day by 2012. Xi also signed an agreement doubling China's loan to Venezuela's Heavy Investment Fund from $4 billion to $8 billion, to be repaid by future oil deliveries—although few of the 41 projects currently in the fund contribute to the infrastructure needed to produce that oil. The agreement signed by Xi in Brazil similarly expands the PRC's claim on the newly discovered oil in the deep water of the Santos and Campos basins—the other big game in town. By contrast to the Venezuelan agreements, however, the $10 billion line of credit provided to Petrobras actually contributes to its ability to deliver the 160,000 barrels of oil per day which it committed to deliver China, and the track record of Petrobras inspires confidence in its ability to deliver on the assured future supply that China hopes to buy through this investment."

Jiang Shixue *is vice president of the Chinese Association of Latin American Studies in Beijing.*

Nelson Altamirano *is assistant professor of economics at the School of Business and Management at National University.*

R. Evan Ellis *is an associate at Booz Allen Hamilton.*

Latin America Energy Advisor
is published weekly by the Inter-American Dialogue, Copyright © 2009

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Latin America Energy Advisor is published weekly, with the exception of some major US holidays, by the Inter-American Dialogue
1211 Connecticut Avenue, Suite 510
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