INTER-AMERICAN DIALOGUE'S
LATIN AMERICA ADVISOR ▸ ENERGY

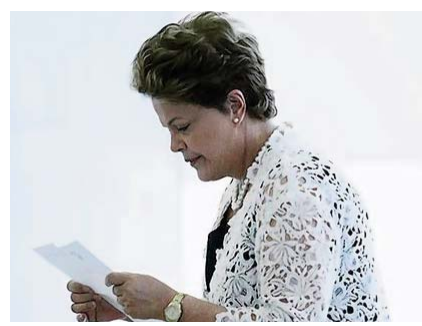
FEATURED Q&A

Will Investment in Argentina's Energy Sector Improve in 2013?

Q **Argentina's government on Nov. 28 said that, after years of frozen prices, it will let oil and gas companies triple current prices for new natural-gas production. The CEO of recently nationalized state oil company YPF, Miguel Galuccio, hailed the news, saying it will help fund the company's ambitious exploration and production plan and make YPF more attractive to foreign investors. Will the move be enough to help the country improve its natural gas output, and will foreign investors jump in? Has YPF found its bearings after its contentious nationalization earlier this year? Where do you see the country's energy sector headed in 2013?**

A **José Valera, partner at MayerBrown LLP in Houston:** "After years of subsidizing foreign exporters, Argentina has decided instead to incrementally subsidize local producers. The price increase announced by the president is from $2.50-$5 to $7.50 per MMBtu for new production over existing levels. Existing production will still fetch the low prices. So far, this increase applies only to recently nationalized YPF pursuant to a direct agreement between the government and the company. Consumers will not see a tariff increase. The difference between the existing ultra-low residential tariffs and the new price at the wellhead will be borne by the treasury. Considering that imported gas costs between $12 and $20 per MMBtu, the government will save some money if this measure actually has the effect of increasing domestic production. And that is a big 'if.' Argentina's energy policies have turned the country from an exporter of electricity, natural gas and oil into an energy importer to the tune this year of about $10 billion. Add to this insufficient electric generation capacity resulting in frequent blackouts. Interventionism, protectionism, populism and outright disregard for established laws and regulations killed econom-

Continued on page 6



Brazil: Rousseff Signs New Oil Revenue-Sharing Law

Brazilian President Dilma Rousseff last Friday vetoed parts of a hotly debated bill that will give a greater share of oil royalty revenues to states in the federal republic that do not produce oil. The law mandates new oil revenues go to education. See story on page 2.

File Photo: Reuters.

Inside This Issue

ENERGY SECTOR BRIEFS

Chile's Enap, BG Reach Agreement on LNG Deal

Chilean state oil and gas company **Enap** and Britain's **BG Group** have reached an agreement over prices and volumes of a liquefied natural gas contract, Dow Jones reported last Friday. BG, which sought to renegotiate the conditions of contracts signed in 2007, is in the process of divesting its Chilean assets.

IDB Loans Uruguay $108 Million for Wind Farm Construction

The Washington-based Inter-American Development Bank said Thursday it is lending $107.7 million to finance construction of two wind farms in Uruguay, El Libertador and Palmatir. The funds will help **UTE**, the state-owned electricity company, get private-sector participation into the renewable energy sector. Brazil's **WPE** (a fully-owned subsidiary of **IMPSA**) will provide 44 turbines for El Libertador. The Palmatir farm will be developed by Spain's **Abengoa**.

Trinidad Looking to Africa, Asia in Response to Shale Boom in U.S.

Trinidad & Tobago Finance Minister Larry Howai said his country may start investing in Africa in response to the shale gas boom in the United States and its impact on the global liquified natural gas (LNG) market, the local *Daily News* reported Thursday. "We've started to look at the possibility of investing in Africa ... Whether we make the money by oil and gas in Trinidad, or oil and gas somewhere else, the fact is that it will increase our cash flows," Howai told a guests at a conference in Port of Spain. A wider Panama Canal now saves Trinidad some $1 million per LNG shipment to Asia, he added.

Oil & Gas News

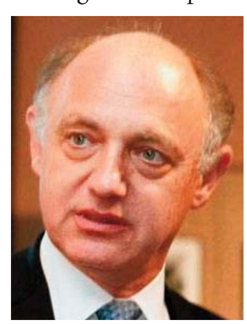
Brazil's Rousseff Vetoes Key Items in Oil Revenue-Sharing Law

Brazilian President Dilma Rousseff last Friday vetoed parts of a hotly debated bill that will give a greater share of oil royalty revenues to states in the federal republic that do not produce oil, the Associated Press reported. Officials from the state of Rio de Janeiro had warned that without a veto, the measure would deprive Rio of $1.7 billion in 2013 alone. State Gov. Sergio Cabral had threatened to appeal to Brazil's Supreme Court if the state's royalties were reduced. But Brazil's lower house of Congress voted in early November to approve legislation for distributing oil royalties more evenly among all of Brazil's 27 states instead. At a news conference Friday, Rousseff's chief of staff, Gleisi Hoffmann, said the legislation's royalty-sharing formula will be applied only to future drilling and production concessions. "Rio thanks President Dilma," Rio's governor said in a statement. Rousseff's changes to the law also mandate that all royalties from future production contracts be used to fund educational programs, Reuters reported. Investors and oil companies have been waiting for years for Brazil's government to decide how it would regulate the industry after the discovery of huge deposits of hydrocarbons in its offshore pre-salt layer, which have yet to produce commercial oil. In related news, Brazil's national oil company, **Petrobras**, said on Wednesday it had discovered a new light-oil find in ultra-deep waters off Brazil's northeastern coast, EFE reported. The find was discovered 53 miles off the coast of the city of Aracaju at a depth of 8,470 feet, more than a mile below the surface of the ocean. The discovery was the fourth the company has announced thus far this year in that region.

> ***Rousseff's changes mandate that all royalties from future production contracts be used to fund educational programs.***

Spain's Repsol Takes Case Against Argentina to ICSID

Spain's **Repsol** has taken its dispute over Argentina's seizure of the company's **YPF** subsidiary to the World Bank's International Center for the Settlement of Investment Disputes, BBC News reported Monday. The government of President Cristina Fernández de Kirchner nationalized YPF earlier this year, claiming the company was investing too little in oil production in the South American country. She blamed Repsol for draining YPF's resources and underinvesting in the unit at the same time that Argentina was experiencing increased internal demand for fuel. Repsol rejected the argument and has been in talks for six months over adequate compensation, estimating that the 57.4 percent stake it had in YPF was worth approximately $10.5 billion. The lawsuit also alleges that the expropriation violates a bilateral investment protection treaty from 1991. On Tuesday, Repsol also sued **Chevron** in a U.S. court in a bid to prevent the company from partnering with YPF, arguing that it has a "rightful interest" in the assets that the companies could jointly develop, Bloomberg News reported. YPF needs expertise and funding from major oil companies to help it develop major finds of unconventional resources in the southern part of the country. Chevron has signed a preliminary agreement to develop the Vaca Muerta reserves, which are estimated to hold 23 billion barrels of oil equivalent. In yet another development this week, Argentina's government on Wednesday lodged a complaint with the World Trade Organization over European Union trade barriers related to biofuels, the Associated



Timerman

File Photo: Government of Argentina.

Press reported. Foreign Minister Héctor Timerman said Spain's decision to end imports of Argentine biodiesel, made in retaliation for Argentina's decision to seize YPF, runs afoul of WTO rules and is "proof that a double standard exists between developed and developing countries when it comes to trade," said Timerman.

Upgrades to Peru's Talara Refinery to Overrun Original Budget

The modernization of **Petroperu**'s Talara refinery in northern Peru will cost more than the originally estimated $1.7 billion, company president Humberto Campodonico said Nov. 30, Dow Jones reported. He also said that the company had not settled on a date for when it would begin selling shares. Peruvian President Ollanta Humala made domestic oil production one of his administration's goals, and Petroperu plans to take stakes in already operating wells to do so. However, it is waiting on the costs of the refinery upgrade and other plans for upstream developments before issuing shares. "Investors want to know what will happen with a company for the next two, three, four or five years," Campodonico said. French bank **Société Générale** is working with the company to determine the financial framework needed to bring Talara from a capacity of 65,000 barrels per day today to its goal of 95,000 barrels per day, according to the report.

Power Sector News

BNDES to Raise Local Content Requirement for Wind Turbines

Brazilian development bank BNDES is planning on raising the local-content requirements for makers of wind turbines, said Elbia Melo, the head of trade-group Associação Brasileira de Energia Eólica, or ABEEólica. "The 60 percent requirement wasn't a sufficient incentive mechanism," she said, Bloomberg News reported Wednesday. According to Melo, BNDES will change the current requirement of 60 percent of domestic components to a "qualitative" method of meas-

In Profile

Mexico: Peña Nieto Names Energy Minister, Pemex Chief

Name

Pedro Joaquín Coldwell, Energy Minister

Background

Born the son of a Cozumel businessman in 1950, Coldwell studied law at the Universidad Iberoamericana and entered politics at age 24 as a state legislator. By 1981 he was governor of the state of Quintana Roo, a post he held for six years. In the 1990s, he was secretary for tourism (1990-93) and Mexico's ambassador to Cuba (1998-2000). He also held posts in the Interior Ministry. Over the last decade, he has been a professor, from 2000 to 2006, at his alma mater, and was active in party organization with the PRI in several key states. For the last year, he has been the chairman of the PRI's national executive committee.

Coldwell

Notes

Peña Nieto made reform of Mexico's monopoly hydrocarbon laws a hallmark of his campaign, but opposition within his own party has scuttled past efforts at reform. Observers are wondering whether naming a party operative like Coldwell to the energy post implies the president's proposed reforms will get pushed through Congress effectively, or whether, being successful at politics through alliances with entrenched interests, the decision to name Coldwell will prove to be an obstacle to deep reforms.

Name

Emilio Lozoya Austin, CEO, Pemex

Background

The son of a former energy minister, Lozoya studied economics at Mexico's Instituto Tecnológico Autónomo de México (ITAM), and law at the Universidad Nacional Autónoma de México (UNAM). He holds a masters in economic development from Harvard University. Over the past two years, he was executive director and co-founder of an investment fund, JFH SA, and before that was head of Latin America at the World Economic Forum. From 2003 to 2006, he was an investment officer at the Inter-American Investment Corporation. Born in 1974, he is the youngest member of Peña Nieto's new cabinet.

Lozoya Austin

Notes

Lozoya was the coordinator for international relations with Peña Nieto's transition team, and had been mentioned in media reports as a potential candidate to take over the foreign ministry. One of Peña Nieto's 95 "policy commitments" is to give Pemex the "capacity to compete as a world-class company," but industry observers note that few specifics have been provided by the transition team on how that might happen. The need for public oversight of Pemex's deepwater operations and deciding how shale gas deposits will be developed are two other areas that will need to be defined soon, George Baker, the publisher of *Mexico Energy Intelligence*, wrote this week.

Sources: Mexican Government, Mexico Energy Intelligence, El Universal, *CNN.*
Photos: Government of Mexico.

uring local usage. She did not say by how much the new local-content requirement would be increased, though the new rules will be issued before a Dec. 14 auction. In related news, **General Electric** estimates that its annual turbine sales to Brazil will reach $1 billion over the next decade. "What you'll probably see is fewer, but more mainstream, players in Brazil over the next couple of years … Wind is going to be a large chunk of the installs going into that country between now and 2022," said Vic Abate, the vice president of renewables at GE. In its latest deal, the company, which is the biggest U.S. wind manufacturer, signed a $394 million agreement on Monday to provide 386 megawatts for **Renova Energia**. It will provide 230 turbines for a wind farm in Bahia state.

Chile Approves Plan for Coal-Fired Power Plant in Mining Region

Chile's government has approved plans by **Endesa** to build a coal-fired thermal power plant in the southern part of the copper-rich Atacama Desert, EFE reported Tuesday. Environmentalists have criticized the plant, known as Punta Alcalde. It will require $1.4 billion in investment and have an installed capacity of 740 MW. Facilities will include a mechanized pier to unload coal and five sewage treatment plants, according to the report. In a statement released Monday, Endesa said it will be the first electrical company in Latin America to use domes to cover the two fields that will be used for the stockpiling of coal. A system of sleeve filters also will be employed to reduce emissions, according to the company. But a group of demonstrators protested against the project outside the Economy Ministry in Santiago Monday, saying they will continue legal efforts to prevent the plant from being built, according to EFE.

Advisor Q&A

Will Correa Coast to Victory in Ecuador's 2013 Elections?

Q Ecuadorean President Rafael Correa, who formally launched his bid for a third term last month, is polling well ahead of his opponents in advance of the Feb. 17 election. Do any of Correa's rivals stand a chance of defeating him? What issues will matter to Ecuadoreans when they go to the polls? What would Correa seek to do in a third term?

A Andrés Mejía Acosta, research fellow at the Institute of Development Studies at University of Sussex: "President Correa is on a secure path to consolidate a third electoral victory in the 2013 general election. The electoral and institutional reforms adopted in recent years have ensured that Correa controls the playing field, the referees and the competitors before the presidential race. Not only are the different opposition parties fragmented and have limited access to state resources and media exposure, but the government is free to use state resources for its re-election campaign. The electoral body, which remains loyal to the president, has no ability to oversee or enforce campaign regulations and level the playing field. Even if opposition parties are able to secure smaller wins in the legislative or subnational arenas, they will have a limited scope for influencing the government. The National Assembly has lost any meaningful policy making or oversight functions vis-à-vis the president, and city mayors are increasingly dependent on the president to gain access to important state resources, thus ensuring their compliance with government policies. The imminent exploration and exploitation of mineral resources and the new round of concessions of oil fields will continue to provide the Correa administration with plenty of fiscal revenues during his third term in office. Paradoxically, Mr. Correa appears determined to follow the same extractivist model that was so toughly fought against during the early days of the Citizens' Revolution."

"The new round of concessions of oil fields will continue to provide the Correa administration with plenty of fiscal revenues during his third term."
— *Andrés Mejía Acosta*

Editor's note: See more Q&A on this topic in the Dec. 3 issue of the daily Advisor.

Political News

Colombia Peace Talks Resume After Weeklong Break

Peace talks between Colombia's government and the FARC rebels have resumed in Cuba after a week's break, BBC News reported Wednesday. Rebel negotiator Andrew Paris refused to comment on how last weekend's killing of some 20 rebels by Colombian troops would affect the negotiations, however. The talks, which the government wishes to conclude by next November, are focusing on five issues: land reform, ending armed conflict, guarantees for political opposition and citizen participation, drug trafficking and the rights of victims of the conflict. Investors in the energy sector are hoping peace talks will improve security in the country, where oil pipelines have been regular targets of guerrilla attacks.

Peru Asks World Court to Set Maritime Border With Chile

Peru's government on Monday formally asked the United Nations' International Court of Justice to delineate its maritime border with Chile, which Peruvian officials hope will expand the ocean territory under its control, the Associated Press reported. Peru brought the case to the World Court in 2008, claiming that the two countries never established a maritime boundary. They signed treaties in 1952 and 1954 that Chile argues set the maritime border. However, Peru argues the accords only identified fishing zones. Peru and Chile are top producers of fishmeal and their waters produce significant income for the two countries. A ruling in Peru's favor could give it control of more than 60,000 square kilometers of ocean that have been under Chile's control for 60 years. Alain Pellet, the lawyer representing Peru's government, told the court Monday that there is "a flagrant lack of any maritime delimitation" and that the border Chile has proposed "radically cuts off Peru's access to the high seas." Peru wants the World Court to equally divide the maritime territory in accordance with international law, said Pellet. "Peru asks neither more nor less than the laws of the sea grant to all coastal states," he said. Chile maintains that its 20th century treaties with Peru set the maritime border, said Maria Teresa Infante Caffi, a Chilean government representative who spoke to reporters outside the courtroom. "The central point for Chile is the existence and validity of the limits that were established through bilateral agreements between the two countries," she said. Last week, Chilean President Sebastián Piñera said the case amounts to defending "a cause that belongs to us all, such as defense of our oceans ... and our sovereignty." A ruling by the World Court would be binding.

Pellet

File Photo: La Tercera.

Economic News

Brazil's Economy Cools More Than Expected in Third Quarter

Brazil's economy expanded just 0.6 percent in the third quarter compared to the second quarter, state statistics agency IBGE said on Nov. 30. That rate of growth was only half of what most market analysts expected. The third quarter data marked the seventh consecutive quarter of sluggish and "below-trend" real GDP growth, **Goldman Sachs** analyst Alberto Ramos wrote in a research note. The sequential real GDP growth for the first and second quarters this year were revised down, as well. Brazil's once-hot services sector especially disappointed market watchers by posting zero growth. The industrial sector grew 1.1 percent compared to the previous quarter, however, and the agricultural sector grew a high 2.5 percent. Aggregate investment declined to a low 18.7 percent of GDP in the third quarter, down from 20 percent of GDP in the second quarter. The national savings rate remains "very low" at 15.6 percent of GDP during the third quarter, Ramos said. Economists now expect Brazil's real GDP to grow just 1 percent for the full year 2012. Brazil's real currency tumbled after the announcement to a three-year low on speculation that the weaker-than-forecast economic growth may prompt the central bank to allow the currency to weaken further to support exporters, Bloomberg News reported.

Argentina Wins Second Reprieve From U.S. Court on Debt

Argentina's government on Tuesday won a second reprieve in as many weeks from a U.S. court as it seeks to avoid paying bondholders who refused to accept restructurings after the country's massive default a decade ago, Reuters reported. In the latest development, a U.S. appeals court refused to order the South American country's government to post a security deposit as it fights a ruling to pay $1.3 billion to so-called holdout investors. The bondholders attempted to force the government to post $250 million while it appeals an order last month by a U.S. district court judge that it pay the holdouts at the same time it makes a payment to creditors who accepted restructurings. Argentine Economy Minister Hernán Lorenzino welcomed the court's decision. "It's a positive ruling," he told reporters in Buenos Aires. Argentina won another reprieve on Nov. 28 when the U.S. Second Circuit Court of Appeals in New York ruled that the government need not set aside $1.33 billion in an escrow account by Dec. 15 to satisfy the claims of the holdouts, a move that threatened a default. The holdouts then unsuccessfully sought a court order for the security deposit, arguing the government needed to show it was acting in good faith. The Court has scheduled oral arguments for Feb. 27.

POLITICAL & ECONOMIC BRIEFS

Gunmen Kill Paraguay Land-Rights Activist Ahead of Testimony

Gunmen in Paraguay on Saturday assassinated Vidal Vega, one of the leaders of a peasant movement whose land dispute led to the end of Fernando Lugo's presidency last June, the Associated Press reported. Vega, 48, had lobbied the government for years to redistribute some of the land that Colorado Party Sen. Blas Riquelme began ranching in the 1960s. He was expected to be a witness at the criminal trial this month over violence in June that resulted in the deaths of 11 peasants and 5 police officers. He was among the few leaders who weren't killed in the clash.

Authorities Crack Down on Corrupt Police in Rio de Janeiro

Brazilian authorities arrested 60 policemen, and another 12 are on the run, in a crackdown on corruption in Rio de Janeiro, BBC News reported Tuesday. The officers are accused of taking bribes of between $700 and $1,200 a week, selling weapons to gangs and other criminal activities. The city has been cracking down on its favelas ahead of the 2014 World Cup and 2016 Olympics.

Venezuela's Chávez Will Not Travel to Mercosur Summit

Venezuelan President Hugo Chávez, who arrived in Cuba last week for therapy related to side effects of his cancer treatment, will not attend a summit of the Mercosur trade block this week in Brazil despite earlier reports he would, AFP reported Thursday. "President Chávez will not come to the summit. Venezuela will be represented by [Foreign Minister and Vice President] Nicolás Maduro," a spokesman for the Brazilian foreign ministry told AFP.

Featured Q&A
Continued from page 1

ic incentives for oil companies to invest in exploration and development and for electric companies to invest in new generation capacity. *La Nación* estimates that, as a result of these policies, energy companies in Argentina have lost capital of between $150 billion and $200 billion. That is the root of the problem. Nationalizing YPF and subsidizing domestic production slightly more instead of foreign imports do not address it. Domestic production will only increase meaningfully when the free market is reinstated. The current situation is aggravated by the government's severe restrictions on imports (the development of shale gas in Argentina cannot take place without imported technology and equipment) and the availability of dollars to distribute profits abroad. The government blames the dramatic reductions in the country's reserves and production levels on oil companies not wanting to invest, as if Argentina was the victim of some malevolent conspiracy. The government steadfastly refuses to acknowledge and correct its own errors. Foreign investors will be right to remain cautious. Nothing major will happen in 2013."

A José Martínez de Hoz, partner at Perez Alati, Grondona, Benites, Arntsen & Martinez de Hoz, Jr. in Buenos Aires: "Last week's announcement that the government will allow price increases (tripling current prices up to $7.50/MMBtu) for 'new' natural gas constitutes a positive signal for attracting and expediting investments to develop Argentina's world-class shale gas formations. The good news comes at a time in which it's important to mitigate the adverse impact caused by the expropriation of Repsol's shares in YPF and the issuance of Decree 1277/2012 which enhanced the government's interference in the industry earlier this year. However, it is a first step which still requires clarification as to its implementation, and much more is needed to reverse a decade of price controls, marketing and export curtailments and contract interferences. If Argentina is to be successful in developing its unconventional resources, the government will need to abandon restrictions on dividend payments and imports of equipment that are essential for hydraulic fracking, as well as restoring a friendly legal framework to enable free price negotiations and marketing and contract sanctity. This should be accompanied with sustainable and clear environmental regulations and stable tax rules."

A Isabella Alcañiz, assistant professor in the Department of Government and Politics at the University of Maryland: "Argentina has been dealing with a steady decline of its oil and gas production in recent years. Because diminished outputs are largely due to disinvestment in the sector, attracting new capital is critical to the Kirchner administration and has been a clear mandate of the new CEO of YPF, Miguel Galuccio. Right now, the government is renewing its efforts to reverse the company's declining trend, but the most recent posting of net profits brings bad news, as they were 51 percent lower than the same quarter of last year. Last month's decision to raise utility prices in electricity and gas probably will do little to reassure potential investors, as the head of the sector, Axel Kicillof, announced that those earnings would go to investment funds to improve infrastructure rather than benefit energy firms. The escalation of litigation between Argentina and Spain will further hinder market investors. Not only are these two countries facing off in the courts because of the nationalization of YPF, but now Argentina has brought a complaint against Spain before the World Trade Organization triggered by Spain's ban on Argentine biofuel for transport. Argentina's broader economic horizon is quite problematic as well. For now, the country has narrowly averted a technical default, given a recent ruling by a U.S. appeals judge in its favor and against holdout creditors. In all likelihood, 2013 will be a difficult year for Argentina and its energy sector. It seems doubtful the country will be able to offer a positive investment climate that can attract needed foreign capital."

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Erik Brand
General Manager, Publishing
ebrand@thedialogue.org

Gene Kuleta
Editor
gkuleta@thedialogue.org

Rachel Sadon
Reporter, Assistant Editor
rsadon@thedialogue.org

Subscription Inquiries are welcomed at freetrial@thedialogue.org

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