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Inter-American Dialogue's Latin American Energy Advisor

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Q and A: Is Peru Making Inroads in Oil & Gas Development?

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One of the Humala administration's priorities when coming into office was to accelerate oil and gas development. Peru has seen both successes, such as a large gas find in the Amazon earlier this month, and conflict, including attempts this month by indigenous groups to stop production at nine oil wells operated by Maple Energy. How successful have the country's efforts to develop the oil and gas sector been? What policies, models or strategies should the government consider implementing? Is the administration likely to make inroads with local communities that stand in opposition to such projects and will new consultation laws be effective?

A: Eleodoro Mayorga Alba, partner at L&Q Consultores y Abogados and former general manager of Petroperú:

"The government has focused on 'social inclusion' rather than developing a sustainable energy sector. The project for 'Masificacion del gas' is designed to supply the residential requirements of the low-income population. Without heating or A/C use, the penetration of gas will be slow and require government support forever. There is no policy to increase upstream investments. The first person nominated as president of Perupetro did nothing to increase the capacity of this key institution; not one additional contract was signed. Moreover, after adopting a controversial regulation, the government is starting a first prior-consultation process for the communities along the rivers of Block 1AB. Although the regulation indicates that the entire process should not take more than 120 days, this first attempt risks needing more time. If that is the case, production will drop, necessitating imports. The policy to revamp Petroperú is facing difficulties. There has not yet been closure for the financing of the Talara Refinery modernization project nor a return to upstream operations. Instead, efforts are concentrated on distributing liquid petroleum gas subsidies and developing 'virtual pipelines' for the 'Masificacion del gas.' The proposed ethane pipeline to supply a future petrochemical complex has not had a basic technical, commercial or economic feasibility evaluation and consequently has not received support from any political group. Instead, the proposal is undoubtedly causing delays for the next pipeline to transport gas to markets outside Lima. Gas supply is tight due to a lack of infrastructure to transport supplies to markets. The government should seriously consider modifying its policies or risk a major energy deficit. Actions should be taken to 1) Improve conditions for accelerating upstream investments; this should comprise the development of heavy crudes and opening new natural gas markets. 2) Develop the gas infrastructure required to meet long-term energy needs in parallel with sound environmental and social policies. The impacts of the hydrocarbons sector are quite

different from those of mining. Inclusion policies and projects should be left as a task for the social inclusion and development ministry. 3) Dedicate resources to increasing the capacity of the notoriously weak government institutions in this sector."

A: Emilio Zúñiga, vice president of Latin Pacific Capital S.A.:

"The country has a big challenge in making the acceleration of investment in the oil and gas sector a reality. The main constraint is political fragmentation (parties with poor regional presence) that affects the implementation of environmental policies and more recently with the claims of indigenous populations. State bureaucracy also is weak and insufficient to live up to the tasks demanded by the sector. Low salaries, poor training and easy prey for corruption compounds problems. The positive side is that oil and gas laws and regulations are market friendly and transparent. But the political parties should be able to deliver on social demands by setting aside partisan politics and concentrating on serious and permanent contact with the populations that will be impacted by the exploitation of natural resources. We all know that this exploitation has hidden costs to the environment and people's way of life, but also that the benefits far outweigh these costs. We can say that the issue is not the model of exploitation of our natural resources as stated in the laws, but in the poor management at the political and technical level. For the consultation laws to be effective, the state should be thoroughly prepared. They should address all issues brought to the debates by the incumbents with knowledge, transparency, honesty and patience and deliver on agreements once they are made. The national government must take the lead since the regional governments are politically fragile and poorly prepared, although they are close to the population's demands."

A: Aaron Goldzimer, consultant in international development and environmental issues and Cesar Gamboa, director of public policy at Derecho, Ambiente y Recursos Naturales (DAR):

"The Ollanta Humala administration has distanced itself from many of the reforms that Humala had previously sought, and both his speeches and policies have moderated. He now has no clear opposition to exports of natural gas or any other natural resource (such as electricity to Brazil); he is going slowly with regard to strengthening public companies (Petroperú and Electroperú) for participation in upstream exploration/development and power generation; and he does not seem to intend to make major changes to the energy sector's heavy promotion of gas, oil and hydroelectric projects in the Peruvian Amazon, which has created conflicts with indigenous peoples. The government has taken initiative with regard to prior consultation of communities affected by such projects; but, because of issues with the regulations, distrust continues between the authorities and indigenous organizations. Urgent next steps for energy sector reform include the following: 1) Peru needs planning processes between the national and regional governments linking energy planning with the granting of oil contracts and electricity concessions. Peru has received several loans from multilateral banks for this ('New Sustainable Energy Matrix', or NUMES), but so far there have been few results in terms of strengthened planning capacity. 2) Environmental and social standards for energy and extractive projects must be improved, including environmental impact assessments (EIAs), which, because of their low quality, contribute to social and environmental conflicts. In this regard, the Humala's government is aiming to create an autonomous institution under the Ministry of Environment to evaluate the

EIAs of high-risk projects. Reforms like these have the potential to lead to greater legitimacy for these investment projects."

A: Carlos Paredes, director of Inteligencia Financiera in Peru:

"Humala's government has not been successful in fostering the development of the oil and gas sector thus far. On the contrary, the signals of stronger state interference in exploration and exploitation activities, coupled with increased social unrest, are deterring the entry of major oil companies while some middle-sized ones (like Talisman) are leaving the country. The proposal that state-owned oil company Petroperú will become a forced partner of future concessionaries in exploration and production is discouraging potential investors, as this amounts to covert added taxation. In the case of natural gas, my perception is that the government is trying to come forward with short-term policy initiatives (mostly political) aimed at showing that the electoral promise of massive gasification is an around-the-corner reality rather than focusing on medium- to long-term economically sound options. In the last year, we have witnessed mainly political gestures rather than real development of natural gas projects. The government's stop-and-go behavior will only exacerbate social conflicts (in particular in the southern part of Peru) as frustrated voters realize that not much is happening. The negative effects of the recently approved consultation law on the timely implementation of investment projects remains to be seen. Although it is too early to fully evaluate the new law's impact, it is clear that the government is fostering a more active role of indigenous communities in the process of approving both environmental and social licenses, and that these are taking longer than ever."

The Energy Advisor welcomes responses to this Q&A. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.