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Q and A: Will PDVSA Be Able to Meet Demand From Asia?

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Venezuelan efforts to diversity oil exports have gained steam in recent months, with new energy sector deals signed with Japan, South Korea and Vietnam and the launch of an $8.3 billion joint refinery project in southern China. Do the deals represent significant confidence in Asia for the Venezuelan government's ability to manage its energy sector? Will PDVSA be able to meet increased demand from Asia? Are the deals and the company's plan to diversify its exports a good strategy?

A: Daniel Hellinger, professor of political science at Webster University in St. Louis:

"In the 1990s, PDVSA executives allowed foreign majority ownership of joint ventures, violating the spirit if not the letter of the 1975 nationalization law. When the Chávez government insisted on re-establishing (with compensation) majority national ownership of ventures in 2006 and 2007, it effectively reasserted state control over subsoil resources. Among the companies forced to comply was a Chinese venture in the Orinoco Belt of heavy oil, but new Chinese investments and loans to Caracas suggest that the nationalization has not shaken Asian confidence about deals with the Chávez government. And they have little fear from any successor. Ironically, the government's drive to expand production and diversify markets resembles the strategy PDVSA followed during the 1980s and 1990s, which failed to produce promised macroeconomic benefits and resulted in a nationalist backlash, including Chávez's election in 1998. By mortgaging the present against future oil earnings, Chávez may be repeating the mistakes of the government of Carlos Andrés Pérez during the 1970s OPEC boom. If prices stay high, he will have little trouble paying off the Chinese and others. But an Asian economic slowdown could send prices downward; increased production out of Venezuela would accelerate the decline. At some point, increasing Venezuelan exports may clash with its OPEC obligations, forcing the government to make hard choices. The most serious risk, and a real one for foreign companies, is that Venezuela would use majority ownership to force production cuts. Debt obligations may deter such a course, confronting a future government with difficult decisions."

A: Carlos Bellorin, senior petroleum analyst at IHS in London:

"This must be seen on a country-by-country basis. However, more than a 'confidence' issue, this is an 'opportunity' issue. The Venezuelan government sees some countries in Asia as the only access to financing and others as expertise and technology providers. In all cases (except Vietnam) these countries are huge petroleum net importers. On the other hand, Asia sees Venezuela as a country with massive hydrocarbons resources, very limited access to traditional financial markets and starving for cash. In the last 10 years, PDVSA's record in increasing, and even maintaining, its production levels is not very good. Not a single major hydrocarbon project in Venezuela of the many signed during President Chávez's 13 years in power has come into stream and are years away from full capacity. This is critical since PDVSA must increase its production to fulfill its obligations in order to keep receiving the much-needed cash, or divert exports destined to other countries. Generally, for a petroleum company, diversifying its exports is always a good strategy since its helps to reduce its exposure, mitigate risks and seize new opportunities. This is especially relevant in the case of Asia, which is the region that will represent the biggest proportion in terms of energy consumption in the coming years. However, a company must to do this with a business sense, taking into account the high costs involved in diversifying its exports to a very distant market in any petroleum price scenario. Also, a company must diversify its exports without losing its traditional markets. In both cases, I think PDVSA has not adopted a very effective strategy. On the other hand, the lack of transparency of the deals makes it very difficult to assess them in a responsible manner. What can be said from the massive size of the deals is that Venezuela's debt level is reaching a worrying point."

A: Gustavo Coronel, former member of the board of directors of PDVSA:

"An analysis of the recent deals and claims by Energy Minister Rafael Ramírez that Venezuela 'is sending 600,000 barrels per day to China' and the country 'gets more from that oil than for the oil shipped to the U.S.' shows several things. The new oil supply to Petro Vietnam is only 23,000 barrels a day or so, really peanuts when compared to the 900,000 barrels per day sent to the United States. The 'deals' with South Korea do not involve Venezuelan oil being sent to that country but work to be done in Venezuela by South Korean construction companies. It is also highly unlikely that Venezuela can engage in infrastructure projects worth $11 billion. The country does not have that kind of money, certainly not for investment in petroleum infrastructure. PDVSA's debt is now of the order of $80 billion and keeps growing fast. The $1 billion loan from Japan to expand the El Palito refinery will probably be dedicated to increasing gasoline production for the domestic market. Venezuela currently imports gasoline to give it away for free in the domestic market. Finally, Ramírez's claims about the volumes being sent to China and their prices are false. According to PDVSA's annual report for 2011, total exports were 2,474,000 barrels per day, which included 415,000 b/d to China. If it was sending 600,000 b/d to China, total exports would be 2,689,000 b/d. Since the domestic market requires at least 600,000 barrels per day, PDVSA would have to be producing almost 3.3 million barrels per day to satisfy supply requirements for export and internal consumption. This is considerably more than the 2.9 million barrels per day PDVSA says it is producing (the IEA estimates production at 2.6 million b/d). There is no real diversification of markets going on. China is playing a political game which might backfire with a change in government. South Korea is trying to get money out of Venezuela and the Petro Vietnam 'deal' is minor."

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