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Will Ecuador Be Able to Produce More Oil Next Year?

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Q and A: Will Ecuador Be Able to Produce More Oil Next Year?

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Ecuador's revenue from oil product exports rose 87 percent between January and September to $860 million, compared to the $459 million registered in the same period in 2010, Dow Jones reported Dec. 1. According to the central bank, exports rose 35 percent from 6.73 million barrels in the first nine months of 2010 to 9.06 million barrels during that period in 2011. What is the outlook for Ecuadorean oil production? How well is the government managing the country's oil sector after contract renegotiations earlier this year?

A: René Ortiz Duran, former minister of energy and mines of Ecuador and former secretary general of OPEC:

"Exploration and production contract re-negotiations with international oil companies (IOCs) holding legal contracts lasted longer than expected and companies—those that accepted the so called new contractual modality—ended in 2010 with: a new service contract that extends up to 2017/2018/2019; with an investment commitment of the companies for about $1.2 billion for the next five years; and, for the company, a payment service fee in kind at a rate of about $35 per barrel produced. There is no method for a per barrel payment for new oil discovered. Neither Ecuador's two NOCs—Petroecuador and Petroamazonas—nor the IOCs have been able to increase their oil production significantly in 2011, which might end up around 500,000 barrels a day on average in 2011. Nevertheless, much improved government border controls and a bit more output from the NOCs might have reduced the illegal border outflow of Ecuador's fuels to southern Colombia and northern Peru which amount to 20 percent to 25 percent, as reported by Dow Jones. What is clear is that high oil prices in the markets have played a very important role in increasing government income by about 88 percent, if reported revenues of 2010 and 2011 are compared. The outlook for 2012 is not clear taking into consideration that oil companies are limited to E&P activities within their own respective blocks with already known producing fields, where enhanced oil recovery applications might only help a bit."

A: Héctor A. Paz y Miño, president of Tecnie Oil & Energy in Quito:

"Ecuador's oil exports rose by about 2.3 million barrels during the first nine months of 2011, mostly as a result of the migration of all production sharing agreements to service fee type contracts, which went into effect in late January 2011. All of the production previously exported by private oil companies (roughly 35 percent) was transferred to the government column. Income also rose on account of higher average international oil prices in 2011. Private investment in the sector has remained very modest in 2011, with the bulk of new investment being accounted for by the two NOCs (Petroecuador and Petroamazonas). The country's outlook for 2012 is for a very nominal increase in production (below 4 percent) to about 520,000 barrels of oil per day (bopd), coming mostly from the two NOCs. Ivanhoe Energy, the only private operator who could contribute very significant additional oil production from the Pungarayacu heavy oil field, will not yet be able to do so next year. The challenge for the Ecuadorean government continues to be how to significantly increase production from its sizeable proven reserve base (6-7 billion barrels) under the nationalistic service fee scheme. A valid benchmark is Colombia, with one third of Ecuador's crude oil reserve base, which will top 1,000,000 bopd in 2012, thanks to high private investment prompted by very competitive and stable private contract terms."

A: Mario Alejandro Flor, partner at Bustamante & Bustamante in Quito:

"In the last two years, Ecuador has introduced legislative reforms offering the petroleum industry a new legal framework for carrying out investments in the sector. The most recent amendments in 2010 prompted various oil companies already in Ecuador to renegotiate their contracts, while others decided to leave the country. With the new legislation in place, service contracts seem to be the preferred type of contract. Under service contracts, the state bears the risk of exploration and the investor obtains a steady income without substantial opportunity for upside in the event of an increase in the price of oil. The entire production of the contract area is owned by the state and the contractor is entitled to a fee per net crude oil barrel produced. As a result, the Ecuadorean government's revenue from oil–product exports in 2011 increased dramatically. The changes governing Ecuador's hydrocarbons sector may not very encouraging for certain investors. However it should be borne in mind that since discovering commercial crude oil, Ecuador has struggled to develop it and has always turned to international investors to realize the potential of its oil reserves, therefore opportunities for investment in Ecuador are likely to continue and grow. After the renegotiation of 2010, Ecuador has managed the new services contracts in good terms, and in the upcoming year, I believe, the Ecuadorean government will improve private companies' performance as well as offer new areas to investors, all with the purpose of increasing reserves and production."

The Energy Advisor *welcomes reactions to the Q& above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.*