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How Would the Sale of CITGO Impact Venezuela?

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Q and A: How Would the Sale of CITGO Impact Venezuela?

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Venezuelan President Hugo Chávez has raised the possibility of selling Venezuela's U.S.-based oil company, CITGO Petroleum Corp., to finance ambitious state programs. Chávez has said the company's sale could raise at least $10 billion for the state's stretched coffers, though many analysts suggest it is valued at far less. Is Chávez likely to sell CITGO and, if so, how much would the company reasonably fetch? What impact would the sale have on the Venezuelan economy in the near future? What effects would it have on Venezuela's long-term interests?

A: Luis E. Giusti, senior advisor at the Center for Strategic & International Studies and former chairman and CEO of PDVSA:

"Buying and selling refineries is a normal activity in the oil industry. Different from the production segment, the refining business is one of small margins and it tends to be cyclical. Building a grassroots refinery takes four years, making investment decisions difficult because it is not easy to estimate market risks. With oil prices of $90/barrel, the refining business is undergoing a rough ride and refiners are struggling to maintain their profits. On the other hand, this is a bad time to sell refineries. In addition to those fundamental issues, there is another angle to the ownership and operation of refineries. Big players on the upstream normally operate refining networks in order to have a vertically integrated business from the well to the sales of refined products. This will provide them with guaranteed niches for their oil and help them optimize profits. It was along those lines that in the 1980s, Petróleos de Venezuela began acquiring, at very good prices, refinery installations abroad, first in Europe and later on in the United States, in what eventually was amalgamated under CITGO. The discussion about a possible sale of CITGO is not easy, because there is no reliable information available about the motivations and conditions. During the current administration, CITGO has already sold its participation in CITGO-Lyondell in Texas and in two asphalt refineries in the east coast. A refinery in Chicago has always been a candidate for sale, because of oil supply restrictions. But the core of CITGO is in the large refineries in Lake Charles and Corpus Christi, in addition to the joint venture with Chevron in Pascagoula. The relevant questions to ask are: What is the sale price? Why sell at this bad moment? What are the implications for oil supplies and sales, especially concerning price?"

A: Jorge Piñon, former president of Amoco Oil Latin America and research fellow at Florida International University:

"From 1986 to 1998, PDVSA acquired a number of U.S. oil refining assets, eventually controlling more than 1.3 million barrels per day, or 8 percent, of the United States total operable refinery capacity. In 2005, President Hugo Chávez announced the start of a divestment initiative of its overseas oil refining investments and a reversal of the earlier strategy of vertical integration established by PDVSA. We believe that, even though the refining business has been characterized by its rollercoaster profit margins, the possible sale of CITGO follows more a central government political directive rather than an economic or business strategy set by the national oil company. The sales by PDVSA of its equity shares in U.S.-based Lyondell in 2006 and its Ruhr Oel German assets earlier this year set a market price range of around $5,000-6,000 a barrel per stream day. New grassroots complex refinery capacity construction costs are estimated to be around $15,000-20,000 a barrel per stream day. We estimate that the sale of CITGO could generate $4.5 billion to $7.5 billion for Venezuela and most probably would also require a long-term supply of Venezuelan crude equal to its current levels of around 400 mbd. A combination of factors such as complexity, cash flow (income), replacement value and, most importantly, the intangible strategic value assigned by the future buyer, will determine the final sale price of CITGO. The most important impact to PDVSA's short-term financial position will not be the sale of CITGO, but the 26 percent increase in its crude oil export prices from an average of $57.01 per barrel for 2009 to $71.67 per barrel in 2010, well above the $40 per barrel price level set for the 2010-2011 national budget."

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

"Hugo Chávez will attempt to sell CITGO for three main reasons: (1) He needs money urgently to finance his drive for re-election in 2012, (2) He worries about having important assets on U.S. soil, vulnerable to potential legal action by the U.S. government or companies, and (3) The sale would be one more way to show his contempt for the United States. PDVSA's commercial strategy is totally subordinate to Chávez's political strategy and he will try to sell CITGO at almost any price, but in cash. Pemex could be interested but might not have the money. Price will not be dictated by the true value of the company, which is between $7 billion and $8 billion, but by Chávez's political urgency. CITGO could go for $4 billion to $5 billion if they find a buyer willing to face the associated legal, political and supply risks of the transaction. The impact of the sale of CITGO in the near term would be psychological and financial. It would represent a new step in the progressive liquidation and collapse of the Venezuelan oil industry and would leave Chávez without one of the few clients that pay cash for Venezuelan oil. The injection of cash from the sale of the company would soon evaporate and the country would lose long-term, steady income. The sale would accelerate Venezuela's loss of the U.S. oil market, a process that has been going on for some time now. Only a political change in Venezuela will reverse this trend."

A: Alberto Cisneros Lavaller, CEO and president of Global Business Consultants:

"The eventual sale of the CITGO refinery complex raises a number of issues, specifically the impact on the oil industry, economic repercussions for the country and political implications. With regard to the impact on the industry, there are at least two significant questions to review. First, this refining complex has deep conversion capacities perfectly suited and fitted to adequately process Venezuelan extra heavy grades. Currently, between 550,000 and 700,000 barrels per day from Venezuela are processed by CITGO. The other significant issue is the eventual price of the refinery complex. Usually Venezuelan government estimations are much lower than market value because they tend to make reference in their transactions to book values (not commonly used in the industry). With relation to the economic repercussions, the country will receive lower oil revenues. Official figures suggest that dividends after taxes are very low and, therefore, not worth it to have such investment in the United States. But oil revenues by and large would endure significantly due to the relevance CITGO has within all downstream international integration that Venezuela has nurtured abroad over the years. Last, but not least, is the question of where the sale proceeds would go. Would they be reinvested in other industry projects or used to cover government expenditures, completely diluting its effect? With regard to the political implications, it seems that the sale of CITGO is motivated by Venezuela's desire to get away from an eventual embargo if ExxonMobil and Conoco win their claims against the Venezuelan regime. In this consideration, Venezuelan authorities have had a double discourse: one of harsh ideological rhetoric against 'Yankee imperialism' and another of sustained commerce and oil trade with the United States. That rhetoric also advances ideas of market diversification, which would be impossible overnight because of the mutual dependence enjoyed by both countries (75 percent of Venezuela's exports and 10 percent of U.S. imports). In a nutshell, if the selling of CITGO would take place, Venezuela would have to close long-term processing deals with new owners."

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