KKI POLICY BRIEF

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OIL PRODUCTION IN LATIN AMERICA AND THE RUSSO-UKRAINIAN WAR
PART I

LATIN-AMERIKAI KŐOLAJTERMELÉS
ÉS AZ OROSZ-UKRÁN HÁBORÚ KAPCSOLATA
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Abstract: Latin America has almost one-fourth of the world's oil reserves, although due to the socio-economic collapse of Venezuela, the main producer country, these reserves have been underused for a decade. Other countries, like Mexico and Brazil, are stable producers and exporters, but the ownership of their national oil companies is subject to heated political debates, while the discovery of new oil fields in Guyana might put this tiny country on the list of the biggest producers. This varied landscape of oil reserves and actual production may be changed fundamentally by the Western sanctions that were implemented against Russia as a consequence of its aggression against Ukraine. A quest for new sources of oil might end Venezuela's isolation and provide lucrative business opportunities for the oil companies that operate in Latin America. However, a new boom of oil production would also raise environmental and social concerns. This analysis focuses on the factors listed above in order to present the shifts and possible pathways of oil production in Latin America in an economic and political climate shaped by the Russo-Ukrainian war. The first part provides a general introduction and presents the main producer country, Venezuela, while the second part offers an analytical overview of the other key oil producer countries in Latin America.

Keywords: oil, Latin America, Venezuela, energy, Russo-Ukrainian war

Összefoglalás: *Latin-Amerika rendelkezik a világ olajtartalékainak csaknem egynegyedével, bár a fő termelő ország, Venezuela társadalmi-gazdasági összeomlása miatt ezek a készletek egy évtizede kihasználatlanok. Más országok, mint például Mexikó és Brazília, stabil termelők és exportőrök, de nemzeti olajtársaságaik tulajdonjogai heves politikai viták tárgyát képezik. Eközben a guyanai olajmezők felfedezése felteheti ezt a kis országot a legnagyobb termelők listájára. Az olajtartalékok és a tényleges kitermelés ezen változatos helyzetét alapjaiban változtathatják meg azok a nyugati szankciók, amelyeket Oroszország ellen vezettek be Ukrajna elleni agressziója következtében. Az új olajforrások keresése véget vethet Venezuela elszigeteltségének, és jövedelmező üzleti lehetőségeket kínálhat a Latin-Amerikában működő olajtársaságok számára. Az olajtermelés újkeletű fellendülése azonban felvet környezeti és társadalmi aggályokat is. Ez az elemzés a felsorolt tényezőkre összpontosít, hogy bemutassa a latin-amerikai olajtermelés eltolódásait és lehetséges útjait az orosz-ukrán háború által alakított gazdasági és politikai légkörben. Az első rész általános bevezetőt ad és bemutatja a fő termelő országot, Venezuelát, míg a második rész elemző áttekintést nyújt a többi fontos latin-amerikai olajtermelő országról.*

Kulcsszavak: *kőolaj, Latin-Amerika, Venezuela, energia, Orosz-ukrán háború*

Introduction

Russia's military aggression against Ukraine and its continuous attack on civilians during the brutal war that is raging on for the tenth month at the time of writing has led Western countries to impose economic sanctions on Russia, a top oil exporter[1]. In 2021, Russia was second on the global list of crude oil exporters, with a massive 10.1 million barrels a day, lagging behind the United States only, and outpacing Saudi Arabia. The scheduled import bans and price caps on Russian oil on behalf of the European Union and G7 nations created a demand shock that made crude oil prices skyrocket: in March, the price of a barrel reached USD 115, a record price since 2013.

The price boom did not last long, and by December 2022, when the sanctions were implemented, the price of a barrel of crude oil had fallen to USD 70, exactly where it was before the start of the Russo-Ukrainian war. In light of the falling prices, in October 2022, the Organization of the Petroleum Exporting Countries (OPEC)[2] announced that it would cut oil production, and despite immediate negative response on behalf of the United States, OPEC+ members continued to produce two million barrels per day less than before the October announcement.

The interest of Western countries, most of which are net importers of crude oil, is to keep oil prices relatively low, while at the same time weakening Russia's economy with a combination of price caps and sanctions. Given the conflict of interests with OPEC, and especially Saudi Arabia, it has become a key issue for the West to re-evaluate possible sources of oil import. Shale oil from the United States can partially cover Europe's needs, but it is far from being sufficient.

In this landscape of economic and political factors, Latin America's vast reserves of natural oil have come into focus. Venezuela holds approximately 300 billion barrels of oil reserves, the world's largest, however, its production (as of 2021) was only 600,000 barrels per day, placing the country at 25th place on the list. The dramatic collapse of the Venezuelan economy, triggered by the fall of oil prices after 2013, and aggravated by the mismanagement of the state oil company by a leftist authoritarian regime, made Venezuela unable to take advantage of its natural resources. US sanctions against the country further worsened the situation, and Chinese and Russian involvement made the production of Venezuelan oil a geopolitical issue. Other Latin American nations have less in reserves, but the fast pace of their extraction puts them above Venezuela's position: in 2021, Brazil was the world's 8th biggest crude oil producer, while Mexico held the 13th, Colombia the 21st, Argentina the 28th, and Ecuador the 29th position on the list. Finally, a tiny South American country,

1 Russia is also a major exporter of natural gas, but this analysis only covers the production of oil. From a perspective of world market effects, Latin American gas reserves would be much more difficult to use as substitutes of Russian export than oil, given the almost total lack of natural gas liquefaction (LNG) plants in the region. One such plant exists in Mexico and one in Peru, while Argentina, the region's major potential gas exporter, can build its own LNG terminal by 2029 at the earliest.

2 OPEC is an international organization of which Russia is not a member, although it participates in the initiative called OPEC+, which provides a forum for talks between OPEC members and other major oil producer countries.

Guyana is widely believed to be the new "oil frontier": the recent discovery of large offshore oil fields has made Guyana the country possessing the third largest oil reserves in Latin America[3], just behind Brazil.

The objective of this analysis is to present a broad overview of the diverse realities of oil production in Latin American countries, and to assess how the Russo-Ukrainian war has changed or can change these realities. In Venezuela, there are already signs of a rapprochement with the United States, as US oil giant Chevron has resumed its activities in the South American country. Other oil producer countries in the region are eager to take advantage of the new export opportunities. However, there are environmental and social concerns related to oil production: Colombia, the third largest producer in Latin America, has already announced that it will stop offering new licenses of exploration in order to stop deforestation and environmental damage in the Amazon rainforest.

After a general overview of data on oil reserves, oil production, ownership, and export, the first part of the analysis presents Venezuela, as the most important case in point. Then, in the second part, other significant Latin American oil producers are analysed briefly. Finally, a short assessment of the environmental, social, and political concerns is carried out related to the oil production in Latin America, the changes observed in 2022, and the possible pathways in 2023 and beyond.

Oil reserves and production in Latin America: an overview

Petroleum was known to exist in Latin America already during colonial times, but the industrial extraction of the material only started in the last decade of the nineteenth century. Financed mostly by British and US private capital, oil fields were explored in several countries. In the early twentieth century, it became clear that Venezuela, Argentina, Brazil, and Mexico are among the world's most important sources of oil. In Venezuela, the massive extraction in the Maracaibo Basin in the country's west, and later in the Orinoco Belt in the country's east, transformed the country into a petrostate whose economy has long depended entirely on the extraction and export of crude oil.

Beyond the two extremely oil-rich regions in Venezuela, major reserves can be found in the territory of Mexico (in Tabasco and Veracruz states), Colombia (in the central areas of the country), Ecuador (in the coastal area and the Yasuni region in the Amazon rainforest), and Argentina (in Patagonia). Furthermore, large offshore oil reserves exist under the territorial waters of Brazil and Guyana, and new technologies of exploration and extraction have enabled these two countries to become major producers of oil.

3 Guyana is an English-speaking country, and for cultural and linguistic reasons, it is usually not considered part of Latin America. Yet, its geographical location on the South American continent, bordering Venezuela and Brazil, makes its inclusion in the present analysis arguably necessary. For the same reason, nearby Trinidad and Tobago and Suriname are also mentioned later.

Map 1.
Oil and gas reserves in South America

Source: Wikimedia Commons, last accessed on 12 December, 2022. Oil fields are shown in green, gas fields in red. The map does not yet show the recently discovered underwater oil fields near Guyana.

As the economic importance of oil grew, several Latin American governments nationalized oil reserves and extraction: most notably, Argentina, Brazil, and Mexico founded their fully state-owned oil companies and prohibited the access of foreign

capital. Venezuelan oil extraction remained in the hands of foreign companies until 1976, when President Carlos Andrés Pérez nationalized the oil industry and founded Petróleos de Venezuela S.A. (PDVSA).

Shaped by resource nationalism, most Latin American governments had a strategic approach to oil reserves, which they regarded as key sources of income for state-led development projects. The state is the only (Venezuela, Mexico) or the majority (Argentina, Brazil, Colombia) shareholder of the respective national oil companies. Despite corruption scandals (of Brazil's Petrobras), indebtedness (of Mexico's Pemex), or general dysfunctionality (of Venezuela's PDVSA), citizen support for maintaining oil reserves in national ownership is high.

Critics of exclusive or majority government ownership maintain that it often leads to rentierism, corruption, and a lack of investment in new technologies. Defenders of a national control of resources nonetheless argue that state control is needed because global private corporations focus on maximalising and repatriating profit rather than on the development of the country where they operate. During Latin America's "Pink tide"[4], statist-nationalist arguments seemed to prevail over market-based liberalism, especially because the market price of crude oil was high. Following 2013, however, the price of oil fell due to China's declining demand and the increasing supply of shale oil production in the US.

Table 1.
Proven oil reserves and oil production in Latin America,
top 10 countries as of 2021

Country	Proven oil reserves (millions of barrels)	Ranking (global)	Country	Actual oil production (barrel per day)	Ranking (global)
Venezuela	303,806	1	Brazil	2,905,121	8
Brazil	12,714	15	Mexico	1,734,495	13
Guyana	~11,000[5]	17	Colombia	736,351	21
Ecuador	8,273	18	Venezuela	594,808	25
Mexico	5,786	22	Argentina	507,337	28
Argentina	2,482	34	Ecuador	472,873	29
Colombia	2,036	37	Guyana	110,200	40
Peru	858	42	Trinidad and Tobago	59,847	51
Trinidad and Tobago	242	54	Peru	38,391	52
Bolivia	240	55	Cuba	33,912	58

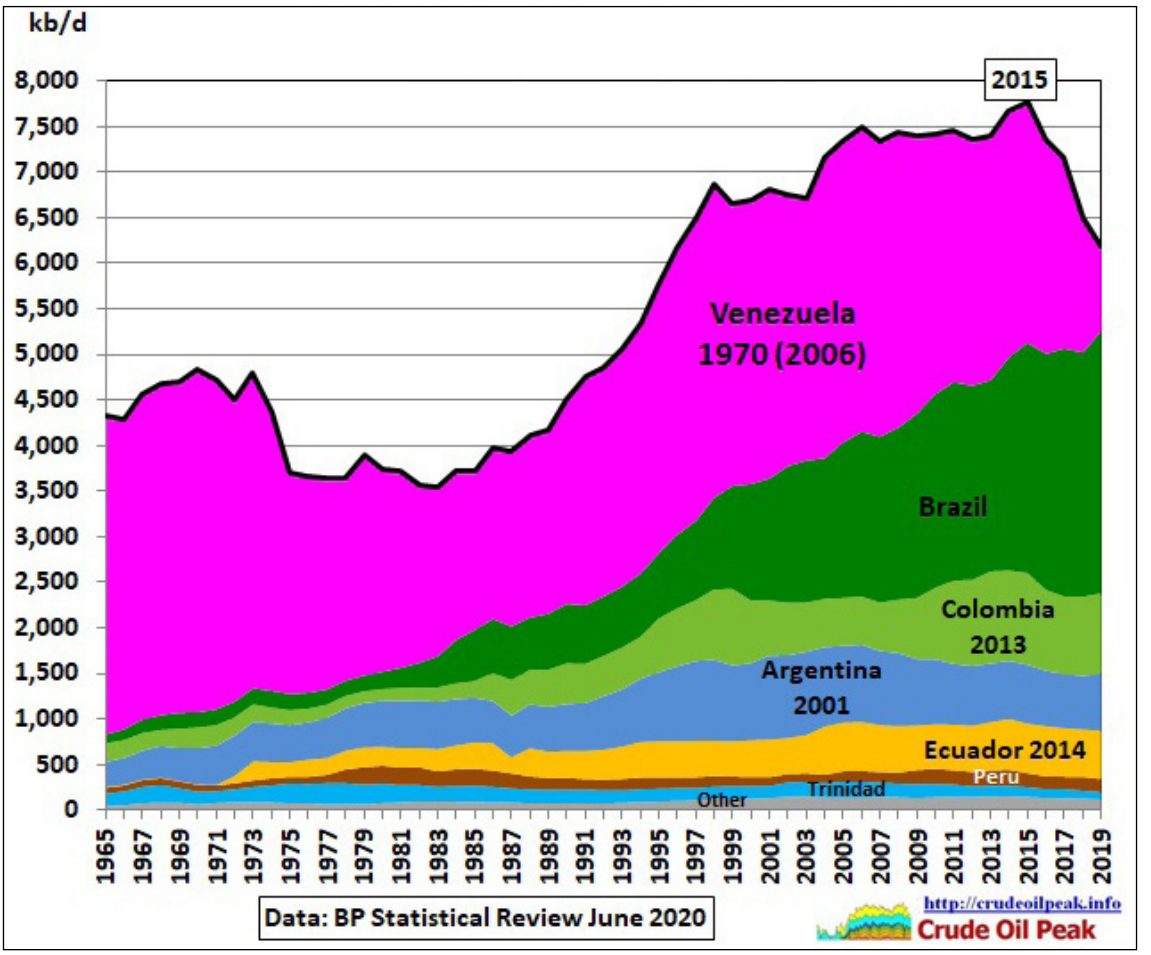
Source: U. S. Energy Information Administration database, last accessed on 12 December, 2022.

4 The "Pink tide" was a historical period approximately between 2002 and 2015, when left-wing or centre-left governments ruled most Latin American countries.

5 Source: OilNow.gy, last accessed on 12 December, 2022.

Despite owning the world's largest reserves, oil production fell sharply in Venezuela after 2013, the year that also saw President Hugo Chávez's sudden death and the election of his successor Nicolás Maduro. As PDVSA became increasingly vulnerable to politically motivated management decisions, and its profit fell due to low international market prices, the operation and maintenance of the oil wells became increasingly difficult. Also, heavy crude oil mined in the Orinoco Belt would have needed chemical agents to dilute its consistency, but this was hindered by the trade sanctions implemented by the United States (prompted by the democratic backsliding of Venezuela). Finally, in 2019 the US stopped buying Venezuelan oil, leading to a spectacular collapse of PDVSA's production. Chinese loans of a total of approximately USD 50 billion helped the company (and the country) out of the crisis, loans that had Venezuela's oil reserves as collateral.

Graph 1.
Oil production in South and Central America, 1965-2019, thousands of barrels per day



Source: Crude Oil Peak, last accessed on 12 December, 2022. Mexico is not included.

Brazil, Colombia, Mexico, Argentina, and Ecuador remained stable suppliers of the world market. The main destinations of their exports were varied: as of 2020, Latin American oil was an important element of the import structure in China and India,

but the United States as well as several European countries have also been relying on these trade relations. Brazil was the fifth largest oil supplier for China, while in the case of the United States, Mexico was its second and Colombia its fifth largest source of oil import. For Spain, Mexico was the second, and Brazil the fifth biggest supplier. Mexico was the largest source of oil imports to Taiwan.

Table 2.
Top 5 Latin American oil exporters, their top 5 export destinations, and the value of their exports (billion or million USD) in 2020

Export from: / Export to:	Brazil		Mexico		Colombia		Venezuela		Argentina	
Nr. 1.	China	11.4B	USA	8.16B	USA	2.67B	India	2B	USA	275M
Nr. 2.	USA	1.37B	Tai-wan	3.85B	China	2.19B	Spain	240M	Netherlands	152M
Nr. 3.	India	1.22B	India	1.9B	Panama	1.05B	Malaysia	195M	China	96.9M
Nr. 4.	Spain	1.03B	Spain	1.89B	India	421M	Italy	154M	Chile	85.7M
Nr. 5.	Portugal	924M	South Korea	1.89B	Saint Lucia	264M	Greece	14.4M	France	40.6M
Total value of oil exports		19.8B		17.8B		7.46B		2.62B		689M

Source: The Observatory of Economic Complexity (OEC), last accessed on 12 December, 2022.

A recurring problem of the Latin American oil industry is the scarcity of refineries. Oil producer countries of the region have several small or mid-sized refineries with a joint capacity somewhat lower than their oil production. An exception is the Paraguaná refinery complex in Venezuela, which is the second largest refinery in the world, yet its actual production is lagging behind its capacities. Due to the insufficient capacity of the refineries, crude oil with no added value is often exported instead of gasoline while gasoline must be imported from somewhere else. This has decreased the rentability of the hydrocarbon trade of Latin American countries and, especially in recent years, led to paradoxical situations of gasoline shortages in major oil producer countries.

Venezuelan oil and the Russo-Ukrainian war

By early 2022, the Venezuelan economy reached rock bottom, following years of bad governance, hyperinflation, and the US sanctions that were enacted between 2017 and 2019, starting with a ban on the state oil company PDVSA's access to US financial

markets, and ending with a total embargo of Venezuelan oil import.[6] US companies had been buying approximately half of Venezuela's oil export even during the presidency of Hugo Chávez, who regularly insulted the US and even called George W. Bush the Devil. After Nicolás Maduro took power in 2013, US–Venezuela relations remained tense, but the oil export continued undisturbed. Despite Chávez's plans to sell Citgo, PDVSA's subsidiary in the US, Maduro maintained the ownership of the company but tried to bring it under closer political control. As the Trump administration enacted its sanctions, Citgo could no longer carry out payments to PDVSA, and it also had to stop exporting US-manufactured diluents to Venezuela, a material that is crucial for transporting the heavy Orinoco crude oil via pipelines. Juan Guaidó, Venezuela's US-recognized interim president[7] appointed an ad hoc Board of Directors in June 2019. The company, with a revenue of USD 24 billion as of 2021, is still under the political control of the Venezuelan opposition.

Cut off from its main export market and the revenues from its main subsidiary, PDVSA became increasingly dependent on Russian investment and loans. Already before the 2017-2019 period of the implementation of cumulative sanctions, when the falling oil prices left Venezuela and its state oil company close to bankruptcy, PDVSA received two major loans from Russia's Rosneft: USD 6.5 billion in 2014 and USD 1.5 billion in 2016. The former transaction was accompanied by Rosneft becoming a minority shareholder of five joint ventures[8] with PDVSA, while the latter deal was collateralized with 49.9% of Citgo's assets. The Citgo deal was soon placed under moratorium by the US Treasury Department due to national security concerns (should the moratorium end, Rosneft could effectively take over half of Citgo's assets due to the unrepaid Venezuelan debt). Rosneft was exporting Venezuelan oil until 2020, effectively breaking US sanctions, but finally Rosneft's shareholders, including British Petroleum (BP) and the state of Qatar, pushed the company to get rid of its five joint ventures with PDVSA. Rosneft finally sold its Venezuelan assets in March 2020 to a company called Roszarubezhneft, owned exclusively by the Russian state.

Coincidentally, this was the time when the outbreak of the Covid-19 pandemic and subsequent lockdowns pushed oil prices to the lowest point recorded in the twenty-first century: USD 17.5 per barrel, as opposed to the USD 100 average price of the early 2010s. Embargoed and left without income, the Venezuelan government resorted to emergency measures, all of which contributed to its dependency upon China, Russia, and to a lesser extent, Iran. For example, a Chinese government-owned defence company reportedly acquired around 25 million barrels of oil from PDVSA as debt offset, while other intermediary companies illegally rebranded smaller amounts of Venezuelan oil as Malaysian. Despite a general collapse of the official export, power shortages, and a lack of investment, Venezuela's oil production remained at the same level in 2021 where it had been in 2020 – that is, a very low level compared to the country's reserves, but still placing Venezuela at 25th place on the global list of oil producers.

6 An overview of the sanctions against Venezuela can be read (in Hungarian) in the analysis of the Institute for Foreign Affairs and Trade, written by Dorottya Városi (E-2021/04).

7 An overview of the events leading to Juan Guaidó's recognition by the US as Venezuela's president can be read (in Hungarian) in the analysis of the Institute for Foreign Affairs and Trade, edited by Sándor Gyula Nagy (4:1 2019/06).

8 The five companies, the largest of which is Petromonagas, together account for approximately 20% of Venezuela's crude oil production.

Map 2.
Oil production sites operated by Venezuelan-Russian joint venture companies, as of mid-2022

Source: Reuters, last accessed on 16 December, 2022.

The desperate situation of the Venezuelan regime changed fundamentally after Russia's invasion of Ukraine. Already on 7 March, 2022, President Nicolás Maduro received a US government delegation in Caracas. According to official communication, they discussed the release of nine US citizens, former executives of Citgo, who had been held in Venezuelan prisons since late 2017 (their release finally happened in early October). Yet the timing of the visit (President Biden signed the executive order banning the import of Russian oil to the US the following day, on 8 March) makes it reasonable to assume that a roadmap was discussed for lifting the sanctions and resuming Venezuelan oil export. Indeed, the US government announced in May that oil firm Chevron would receive a special permit to negotiate with PDVSA. In June, the US allowed Spain's Repsol and Italy's Eni oil companies to ship oil out of Venezuela without being subject to sanctions, although they could only do so as long as it covered the debt that the Venezuelan government had previously accumulated towards these companies (Chevron received a similar license in late November). Later in June, a second US government delegation travelled to Venezuela – again, the official purpose of their visit was to negotiate the fate of the detained Citgo employees – and they met with members of the Maduro administration, but also with Juan Guaidó. The interim president recognized by the US saw his position considerably weaken in the previous months also within the Venezuelan opposition, and by the time that negotiations between the Maduro and the Guaidó teams

officially resumed in November in Mexico City after one year of suspension, it became clear that Maduro had gained the upper hand. In late December, the Venezuelan opposition declared that Guaidó was no longer considered their leader. Parallelly, the informal dollarization of the economy ended with the hyperinflation of the previous years, while the perspective of increasing the oil export and hopes for the end of the scarcity of imported goods made supporters of the regime claim that "*Venezuela se arregló*" (Venezuela has been fixed). This is of course far from being true, as the relative stability comes after a period in which the country's GDP contracted by 75% as compared to the Chávez years. Still, the Venezuelan opposition, which could not seize the opportunity in 2019-2020 to topple the ruling regime, cannot realistically set any further goals than to manage a humanitarian aid fund together with the Maduro administration, as agreed in Mexico, and to ask for free and fair campaign conditions and an international observing mechanism for the next elections set to be held in 2024.

While Russia's Roszarubezhneft is still an important player in the Venezuelan oil industry, the financial sanctions against Russia have disabled the payments it used to make through the international banking system and obliged the company to pay in roubles. Another Russian joint venture, GPB Global Resources, owned by former Gazprom officials, had to sell 40% of its stakes to PDVSA, which became a majority shareholder through the deal and replaced the whole board of the company. Despite official statements from the Russian government, e.g. by Deputy Prime Minister Alexander Novak, who visited Caracas on 15 December, about enhanced cooperation in the future, it is highly likely that Russian influence over Venezuela's oil production will decrease in the near future. On the diplomatic level, the Maduro regime maintains a friendly approach to Russia through official visits and talks, but as soon as oil export to the US resumes, the Russian connection will be losing its relevance for Venezuela.

China's influence might continue to be important, but unless an open trade war breaks out between Washington and Beijing, Venezuela is likely to align with a strategy already followed by many Latin American countries, such as Brazil, which regard the two powers as dual hegemons over the region and will trade with both of them. A political momentum of like-minded leftist governments in Latin America, most importantly in neighbouring Colombia, can further help ease Venezuela's isolation. Other powers, such as European nations or India, might benefit from Venezuela's resuming oil export, but it is unlikely that the European Union and/or its member states can become strategic partners of a Maduro regime that has started to emerge from its decade-long agony without substantially changing its authoritarian traits and human rights abuses.

(The second part of the analysis offers an analytical overview of the other key oil producer countries in Latin America, including Brazil, Mexico, Colombia, Ecuador, Peru, Argentina, Guyana, and Suriname.)

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