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Bolivia's Natural Gas Nationalization

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The Bolivian government, led by President Evo Morales, nationalized the country's independent natural gas companies on May 1 in a most dramatic fashion. Troops were sent in to take control of at least 56 fields, and Morales showed up at the large San Alberto field in southern Bolivia operated by Petrobrás, the Brazilian national oil company, and Repsol-YPF of Spain. These two companies have the largest stakes in Bolivia, but the decree also affects other companies, including Total (of France), British Gas, and British Petroleum. The way the action was taken was surprising to the companies, but Morales had long said he would nationalize the industry.

The decree has a number of elements: the companies must turn over field operations to Bolivia's national oil company, Yacimientos Petrolíferos Fiscales Bolivianos (YPFB), which will set prices; the state tax and royalties on gas production will be raised from 50 percent to 82 percent for the largest fields, and this hits Petrobrás, Repsol, and Total; and the oil companies were given 180 days to comply with the new terms or leave the country. The dramatics were staged for domestic political effect, and Morales is quoted as saying: "We don't just make promises, we deliver on them." What Morales had promised was "nationalization without expropriation"; the nationalization half of this promise has now been kept.

There are two ways to look at the action taken by the Bolivian government. One is that the return on natural gas exports to Brazil and Argentina, Bolivia's largest markets, is relatively low at a time of rising prices elsewhere. Brazil is paying $3.26 per million British thermal unit (Btu), whereas the price for imports in Mexico, for example, is $7.65 per million Btu. There is no basic reason why the Mexican and Brazilian prices should be equal, but the disparity is quite large. It is not unusual for producing countries to renegotiate contracts when prices for its products are rising sharply, as they are for oil and gas.

The second way of analyzing the Bolivian action is that it was impulsive, looking only at the short term. Natural gas shipped by pipeline is not a global product, but a regional one. Hence, there are logical reasons for different prices in separate regions. Many observers of the hemispheric scene believe that Morales was influenced in his action by Venezuelan president Hugo Chávez, who successfully raised taxes on foreign *oil* operations, for which a global market exists. At the moment, Bolivia has two large customers for its *gas*: Brazil and to a lesser extent Argentina. This could change, especially if Bolivia produced liquefied natural gas, but other options are not now on the table.

Both approaches have validity when examined separately, but they clash when examined in their totality. Morales, by calling out the troops and overdramatizing to show that he is a president who delivers on his promises, gave a star performance before a domestic audience. The short-term increase in Bolivia's take from gas operations undoubtedly is politically appealing in a country that has been more the target of outside aggrandizement than the aggressor. By choosing Petrobrás and Repsol-YPF as his main targets, Morales demonstrated that he is *macho* enough to take on big companies from more powerful countries. The immediate internal repercussions have, in fact, been politically favorable for Morales. The expectation is that this increased domestic stature will help Morales stack the constitutional assembly with his supporters when the vote is held in a little more than a month. Here, too, Morales may be emulating Hugo Chávez; and, if so, the democratic future of Bolivia may be compromised if the constitutional assembly is stacked.

Brazil does not have much leverage in the short term to escape the consequences of higher gas prices. Brazil now imports 25.8 million cubic meters a day (mcm/d) of gas from Bolivia, which is almost as much as Brazil's domestic gas production of 27.2 mcm/d. Brazil was caught by surprise. The first reaction from Petrobrás was that Bolivia has a sovereign right to control its own natural resources, but that it must also respect the rights of Petrobrás, which had a contract in place. President Luis Ignacio Lula da Silva recalled several key aides and cabinet ministers who were traveling abroad for a cabinet meeting. A few days later, after a meeting with the presidents of Argentina, Bolivia, and Venezuela, Lula joined in a bland statement that referred to the need to maintain gas supplies. A little more than a week before the natural gas nationalization, Morales indicated that the Brazilian company EBX, which was building a steel mill in Bolivia, would be expelled; there may be no connection between the two actions, but both affected Brazilian interests. Lula had earlier leaned over backward to support Morales, and the Brazilian media consequently had harsh words about Lula's ineffectual policies.

Petrobrás's deep-water explorations in recent years have discovered what are described as large and promising finds of natural gas in the Santos Basin that could supply the needs of São Paulo state in perhaps five years, when the infrastructure is in place. Petrobrás also indicated that it will install two liquefied natural gas (LNG) plants, one in the northeast and another near Rio. Brazil may escape from its current position of hostage to Bolivian gas policy in about five years. For now, Brazil has suspended contemplated investment in Bolivia. Petrobrás investments in Bolivia now amount to about $1.5 billion, plus $2 billion for the construction of Gasoduto Bolívia-Brasil (GASBOL), the pipeline that brings Bolivian gas to Brazil.

Argentina also imports Bolivian gas because Argentine price-freezing policies have led to a near cessation of gas exploration over the past several years. The Bolivian action may spur the Argentine leadership to take the corrective action it has been unwilling to take thus far of unfreezing producer and consumer prices.

U.S. companies have investments in Bolivia, but far short of the scale of Brazil or Spain. However, the United States does have an important interest in how the Bolivian action plays out. The apparent affinity between Chávez, Castro, and Morales does not endear Morales to the Bush administration. Bolivia earlier had been declared eligible for funding by the U.S. Millennium Challenge Corporation, and this surely will be kept on hold. Morales's policy of encouraging coca production ("coca not cocaine" may be like "nationalization not expropriation") will not sit well with the United States. U.S. trade preferences to countries in the Andean group (to Colombia, Ecuador, and Peru, in addition to Bolivia) will expire at the end of this year and are unlikely to be renewed in favor of Bolivia unless there are some radical changes in Bolivian policy between now and then.

Morales's short-term political and revenue gains are unlikely to endure in the future, when Brazil has more freedom of action with respect to gas imports from Bolivia. Other investors will shun Bolivia, certainly, for now. The United States is likely to hold back nonreciprocal benefits it now provides to Bolivia, at least until there are some basic changes.

Within Bolivia itself, the greater role that the state-owned YPFB will have over the country's gas and oil production may lead to political padding of the payroll, which was the case earlier when YPFB was a state-run operation. Bolivia has a history of nationalizing hydrocarbon and other mineral operations—tin was nationalized in 1952, oil in 1937 and again in 1969. None of these actions turned out well. Indeed, the discovery of the natural gas resources took place during the 1990s, when private investment was welcomed. The nationalization gives one a sinking feeling of *déjà vu*.

If the current elation in Bolivia turns into a devastating collapse a few years hence, as may very well happen, it will be a pity. Bolivia is the poorest country in South America, and no thinking person would want further impoverishment. Bolivia has received rough treatment from its neighbors over the years, from as long ago as the War of the Pacific in the nineteenth century, when the country lost its access to the sea after its defeat by Chile. The prices paid for its natural gas by Brazil and Argentina have been low compared with world standards. Thus, there is much sympathy in Latin America for the idea that Bolivia needs some redress from its neighbors. Bolivia, however, may have squandered this goodwill by giving the highest priority to immediate internal political advantage in the way it handled the gas nationalization. Morales has injured Lula's political position, perhaps grievously, and it is hard to see why he did this.

Bolivia has been going through a struggle for political power between the older, traditional elites and the indigenous and ethnic groups that were subordinated until recently. Natural gas policy was the most important substantive theme used by Morales and his supporters to force the resignations of two previous presidents (Gonzalo Sánchez de Lozada in 2003 and Carlos Mesa in 2005). In both cases, the tactic used was street demonstrations, with growing violence. Morales was elected president in December 2005, garnering 54 percent of the vote.

There are political tensions in Bolivia related to the concentration of the country's natural gas resources in the south—in Santa Cruz, Tarija, and Chuquisaca. The GASBOL pipeline runs from Rio Grande, south of Santa Cruz, to São Paulo and Porto Alegre in Brazil. These southern Bolivian departments have a large stake in the continuation of the gas trade. The authority now being exercised in La Paz stimulates these separatist sentiments. Bolivia obviously has its share of problems. Looking out over the medium term, my judgment is that Morales has worsened them.
