Mexico: An Ally in the Balance

by Richard R. Loomis and Susan Salter

In Bolivia, new president Evo Morales is cast from the Hugo Chávez mold. In Brazil, leftist Luis da Silva seems to be making concessions toward the center. In Argentina, Nestor Kirchner evokes memories, for better or worse, of Juan Peron. Of course, the most vocal of the leftists in Latin America is Hugo Chávez. And in Mexico, one of the three presidential candidates, Andres Manuel Lopez Obrador, is as far to the left as the country's lame-duck leader, Vincente Fox, is to the right. With our reliance on these countries for our energy supply, this could represent serious problems for the U.S. economy.

What's happening in Latin America? No less than a wide-ranging ideological shift toward liberalism, nationalism, populism, socialism and in some ways radicalism as candidates and elected leaders follow in the controversial footsteps of Venezuelan strongman Hugo Chávez. While this is not exactly breaking news, it does come at a time when the United States can least afford to deal with emerging hostility. "While we turned our backs to focus on the Middle East," noted a *New Republic* editorial, "Latin America went and painted itself red."

Illustrating that point is Morales, who was sworn in as Bolivia's president in January. He is, according to *USA Today*'s David Lynch, "the sixth Latin American leader in seven years to take office after campaigning against the market-oriented policies that the United States has urged on its neighbors for two decades." Indeed, even as countries like Brazil, Argentina and Chile have emerged from dictatorship to become economic power players, continuing poverty in these and other nations has led to a political backlash that could lead to instability – socially, economically and, of course, in the area of energy trade.

Daniel Griswold of *American Spectator* finds Latin American governments "pursuing two basic economic models that face in opposite directions. One model embraces free enterprise, macroeconomic stability and growing engagement with the global economy, including free trade with the United States." Griswold places Mexico, Chile and El Salvador in this category. At the other end of the spectrum are Bolivia, Cuba and Venezuela, which look "with suspicion, if not outright hostility, on private enterprise, foreign investment, and trade liberalization."

Who's Left in Latin America

Numerous Latin American nations have recently held presidential elections or will go to the polls later this year. Apart from swing player Mexico, the new generation of *el presidentes* ranges from "pinks" to "reds," as Chris Hawley of the *Arizona Republic* notes: "The so-called pink tide of new leaders ranges from moderates to radicals. But they are all wary of the United States and less likely to back President Bush on trade policy, the anti-drug fight and world affairs."

So what has pushed so many of these countries into the pink/red column, and did it happen by accident?

In the pink

- Evo Morales, Bolivia. This former cocoa farmer was elected Jan. 22. He seeks to nationalize the oil and gas industry and recast the cocoa trade away from its most notorious use: as a basis for cocaine.
- Michelle Bachelet, Chile. This moderate socialist was elected in January and takes office this month. She was jailed under the Augusto Pinochet dictatorship.
- Tabare Vazquez, Uruguay. Named president last March, he is the country's first left-wing leader.
- Luiz Inacio Lula da Silva, Brazil. Took office in January 2003 and is up for re-election this October.
- Nestor Kirchner, Argentina. This well-liked head of state is credited with helping Argentina emerge from a financial crisis.
- Ollanta Humala, Peru. A frontrunning candidate for April 9 elections, Humala is a nationalist and leader of a 2000 coup attempt.

Simply red

- Hugo Chávez, Venezuela. This political firebrand needs no introduction, except to note that his anti-American influence is becoming quite apparent throughout the continent.
- Fidel Castro, Cuba. See Chávez.

In the case of most of these countries, the swing to the left has little impact on the United States except to make it more difficult to lead the nations toward the policies of free trade. However, in the case of Venezuela, this places the U.S. energy supply at risk. Venezuela could choose to sell its crude oil to China or India at a discount. As U.S. influence in the region wanes, the countries of Latin America may allow Venezuela's leadership to influence matters of policy. This could make it very difficult for the United States to implement policies of free trade among the Latin American states.

The Swing Player

While Mexico is – for now, at least – in Griswold's category of a capitalistic government, much may change come election day, July 2. For quite a while, Mexico was the shining example of a capitalist country in Latin America. However, with the peso losing its value and the economy faltering, the country's image has been tarnished. As the promise of capitalism has failed to become fully realized in Latin America, the rhetoric of the Venezuelan president has carried the day for many liberal candidates. In addition, the constant influx of illegal immigrants into the United States continues to cause stress with its neighbor to the south. What's more, recent coverage of the drug-trafficking problems coming across the border has not helped the situation.

Mexico is important to the United States in the same way that Venezuela is important: as a significant import partner providing much-needed resources for the country.

This year's presidential election has produced three candidates:

- Andres Manuel Lopez Obrador, the former Mexico City mayor, is standing for the Revolutionary Democratic Party (PRD).
- Former Energy Minister Felipe Calderon is with Fox's conservative National Action Party (PAN).
- Roberto Madrazo represents Mexico's once dominant Institutional Revolutionary Party (PRI).

At the end of 2005, the once clear frontrunner, Obrador, was in a virtual dead heat with Calderon. A poll by the Mexican daily *La Reforma* gave him 29 percent of the vote to Calderon's 28 percent and Madrazo's 21 percent.

Differing Energy Platforms

Each of the candidates has recognized that energy is the key issue of the campaign. Obrador and Calderon have both expressed their views of how Mexico's energy future should be shaped, and one can assume that Madrazo will carry a similar platform to Calderon.

Obrador has made a call for continued government control of Mexico's energy sector. His campaign promise is to keep the country's oil and gas assets as national resources and not allow foreign investment.

In his platform he is sure that Mexico's state oil monopoly, Pemex, can go without private money. Obrador's view is that by operating more efficiently and cutting the tax burden, Pemex can continue without the support of private investment. As a model he points to the recently passed tax cut, approved last fall by Mexico's Congress, which is expected to save the company about $2 billion as early as 2006. One part of the plan is to reintegrate Pemex's E&P, refining, gas and chemical subsidiaries into a single entity.

This policy would in effect shut down any opportunity for foreign investment. It is also rumored that Obrador is receiving funding from Hugo Chávez. The president of Venezuela is very interested in a left-leaning Mexico.

Calderon has expressed the need to modernize Pemex but has made it clear he has no intentions of privatizing the company. However, he would leave the door open for alliances with strategic partners. He has also expressed an opinion that Pemex's petrochemical, refining and the upstream gas sectors could be opened. This is promising for those wishing to enter the Mexican energy industry. Calderon also backs a plan by Pemex management to issue about $19 billion in shares, which would represent up to 20 percent of the company's capital.

Should Calderon or Madrazo take the lead, it is likely that Mexico will stay out of the red/pink column, and we may see a shift in policy allowing for foreign investment of some kind.

Oil Supplies at Stake

Should Mexico join the ranks of the red or the pink under the direction of Andres Manuel Lopez Obrador, the United States would be then be relying on several countries that do not share the U.S. worldview for its supply of oil.

War of Words

Would you buy your low-cost heating oil from Adolf Hitler? If U.S. Defense Secretary Donald Rumsfeld is to be believed, we already are. The latest round of U.S.-Venezuelan sniping began when Washington ushered out Venezuelan diplomat Jenny Figuerado after Chávez had expelled a U.S. naval attaché for alleged espionage. Rumsfeld then compared Hugo Chávez to the Führer; in response, Chávez threatened to curtail his nation's oil imports to the United States. Before you could say "cold war," however, cooler heads had begun to prevail, as Venezuelan ambassador Bernardo Alvarez told reporters in early February that his country "will continue to be a reliable source of oil for the world, including the United States."

All this comes at a time when the wind-chilled eastern section of the nation continues to take Chávez up on his offer of low-cost heating oil through a program implemented through Citgo, the U.S. subsidiary of PDVSA. Early this winter, Massachusetts and New York were the first to participate in the program, followed by Maine, Rhode Island, Vermont, Delaware and Connecticut, with New Jersey reportedly exploring the option.

Allusions to Hitler aside, perhaps the more realistic Chávez comparison is to Argentina's legendary power player, Eva Peron. "Like Chávez, Peron was trying to highlight the defects of the U.S.-style capitalism while casting herself as a goodhearted Latin American leader," Michael Schifter, an analyst with the Inter-American Dialog, told Associated Press reporter Michael Melia.
As the continent's most vocal Bush-basher, Chávez has furthermore taken steps to align himself with other critics of U.S. policy, most notably through a January photo-op with anti-war activist Cindy Sheehan.

Conversely, should Mexico follow a path that ultimately leads to private investment in its oil and gas industry, the upside could be a more stable oil supply from a trusted economic partner.

"Enough already with the imperialist aggression. Down with the U.S. empire! It must be said, in the entire world: Down with the empire!"

– Hugo Chávez, Jan. 30, 2006

Mexico is the fifth-largest oil producer in the world, and the $40 billion in annual oil income accounts for one-third of the nation's annual revenue. Most of the country's petroleum sales are to the United States. Pemex predicts Mexico's output will actually grow this year to 3.42 million barrels per day from 3.33 MMb/d last year. This comes with rumors of production dropping at the Cantarell field and other assets of Pemex not performing well enough to make up the difference. Currently 6 out of every 10 barrels of oil come from the Cantarell field.

What are the implications of the decline of Cantarell? Prof. Emma Brossard, an author and former adviser to PDVSA and its affiliates, explains: "Mexico in recent years has been the second largest source, after Canada, of U.S. oil imports. Mexican imports have a short haul up the Gulf of Mexico to our Gulf ports. Thus, the decline of one of the world's greatest oil fields, Cantarell, is bad news for both Mexico and the United States. Bad news for Mexico because Cantarell's production of 2 million b/d represents about 60 percent of Mexican production. With a possible decline of half of Cantarell's production by the end of 2007, and a half again (i.e., to 500,000 b/d) by the end of 2008, Mexican current exports of 1.8 million b/d might be eliminated! Most of Mexico's exports go to the United States – and, to repeat, it is the second largest source of our oil imports."

Without clear leadership to move the other Latin American countries back toward the center or perhaps right of center, a clear risk presents itself: If these countries follow the path of Venezuela too closely, the United States risks losing the ability to swing policy in its favor with neighbors to the south. If Mexico follows the example of Venezuela, the energy resources to continue to supply the U.S. "oil addiction" may be in jeopardy. Clearly, the investment needed in Mexico is huge, and because Pemex is burdened with taxes and inefficiency in its organization that effectively take all available cash, the likelihood of the oil monopoly being able to increase production on its own is slight.

Over the years, the idea of privatization in Mexico has hung like a sword of Damocles over the U.S. oil industry, but with so many hurdles the probability of this happening has always been very low. However, the political climate might be right for some changes in the Mexican laws that would allow the United States to help its neighbor improve its producing capacity.

A Citgo Sell-off?

This is especially important in the light of Hugo Chávez's repeated threats to sell off Citgo and divert his oil to India and China. Would he do it out of economic need? Not likely. Out of political spite? More probably.

Though ambassadors are quick to refute the notion of Citgo's departure from U.S. shores, the real possibility remains. The loss of about 1 MMb/d is equivalent to the shut-in oil precipitated by Hurricane Katrina – an event that caused widespread accusations of price gouging from the industry.

If Chávez follows through on his threat to stop exporting oil to the United States, the resulting import instability could send pump prices into the $3 to $5 range, unacceptable in most Americans' eyes. However, the right atmosphere in Mexico could open the door to more opportunity. Mexico could potentially become the counter-balance to Chávez's plans for the Bolivarian revolution. A strong Mexico would once again show the people of Latin America that market economies work and that moving toward managed or even communistic economies will only further delay the promise of the American dream to their countries. Ironically, a change in the investment policies for the oil industry in Mexico provide an answer to the global issue of Venezuela, the local problems of immigration and a very real supply of oil to help with the U.S. addiction. ◆

Where does it all lead?

Since Hugo Chávez has complete control of "all powers," he takes the liberty of giving away Venezuelan resources to the people or countries where he is seeking to import his Bolivarian revolution, thereby buying influence, without consulting with the National Assembly. So the question remains: Will the Bolivarismo of President Chávez be the highest level of the subdevelopment, not only of Venezuela, but of all Latin America?

The Chávez Connection

Many of the Latin American countries that have left-moving governments had felt the clear leadership of the Venezuelan government. While not the only factor in moving these administrations into place, it is clear the Venezuelan government is following a strategy to encourage this movement.

On Jan. 16, 2005, the Center of Economic Investigations (CIECA) published the public spending brief for the Chávez regime for the year 2005.

According to Gustavo Coronel, former PDVSA board member and president of the Caracas-based Pro-Quality of Life Alliance (Agrupacion Pro Calidad de Vida), this spending – which likely doesn't include the "secret," or informal, spending that escapes transparency and accountability – adds up to $2.3 billion. "While the amount is public, the regime does explain the duration of the spending," Coronel wrote in a Petroleumworld.com article. "At the same time the regime announces that the fiscal revenues for 2005 are around $6.5 billion, including about $1 billion of extraordinary revenues, which is public debt and irregular use of the reserves from the Venezuelan Central Bank (BCV). This revenue, derived from new debt and other abuses, covers 16 percent from the public revenue for 2005. The income from oil revenue covers about 43 percent from the total, while taxes including the abusive and despised bank debit taxes cover 30 percent. The remaining amount, about 11 percent, comes from non-specified funds."

Below, some of the spending already done or "compromised" in Latin America by Hugo Chávez.

Argentina
Chávez connection: $3.9 million toward paying the Argentinean external debt, including $100 million for the Campanas refinery, and $4 million barrels of oil in exchange for agricultural machinery.

Bolivia
Chávez connection: $60 million for social programs and a diesel oil subsidy of 5,000 barrels.

Brazil
Chávez connection: $4.6 million for the Pernambuco refinery, 20 airplanes, 28 Tucanos oil tankers for PDVSA, a polypropylene plant, and a "Vila Isabel Samba School" in which the pictures of Simon Bolívar, Chávez and Ché Guevara will be displayed as the three heroes of the Bolivarian revolution.

Cuba
Chávez connection: $4.4 billion, including 95,000 barrels of oil per day, adding $2.1 billion, $20 million for electricity programs for Havana, $480 million for expenses of "installation and capitalization" of the Banco Industrial de Venezuela (BIV) in Cuba, $50 million for housing, $58 million for the "ancient" refinery Cienfuegos and another $8 million for PDVSA-BIV program development.

Peru
Chávez connection: Vote buying? Enrique Naime of the competing Venezuelan Copei Party recently denounced Chávez for offering Venezuelan nationality to Peruvians in exchange for Humala votes (and, by extension, for Chávez votes in Venezuela's December elections). For his part, Humala said the Chávez endorsement had not had a negative impact on his campaign. Nevertheless, in Caracas, Venezuela, posters of Ollanta Humala, the "Chavist" candidate for the Peruvian presidency, plaster the walls of the barrios.

Uruguay
Chávez connection: $ 1.1 billion for the La Teja refinery, PLUNA airline, food, oil, hospital and electricity, plus financing for labor unions.

Venezuela
Hugo Chávez is not only anti-American, but he is even more so than his dictatorial mentor, Fidel Castro. Chávez has Castro's ambition for power and the Venezuelan oil to pursue his plans, including destroying the Venezuelan institutions and PDVSA. And his reach appears to be going beyond Latin America: On Feb. 17, Congressman Dan Burton (R-IN), chairman of the House International Relations Subcommittee on the Western Hemisphere, released a statement expressing his concern that Chávez and other Latin American leaders were "reaching out to known Islamic terrorist organizations, such as Hamas, and cozying-up to renowned terrorist-sponsoring nations like Iran and North Korea."

And lest we forget a neighbor to the north …

United States of America
Chávez connection: $16 million, including $1 million of expenses for the Venezuela Information Office (VIO), plus the well-publicized millions in oil subsidies to lower-income consumers in the eastern United States ◆

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