PDVSA Exploration & Production Rights

BI Integrated Oils, Global Dashboard


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1. PDVSA Cash Flow Would Disappear If Production Rights Stripped

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(Bloomberg Intelligence) -- Bondholders face the risk that Petroleos de Venezuela's (PDVSA) rights to explore and exploit the country's 300 billion barrels of crude oil reserves -- which are exclusively state-controlled -- could be revoked. The Venezuelan government can transfer those rights to another entity at any time, which could leave PDVSA with virtually no cash flow and further damage its credit profile. Still, the state is unlikely to do so given the threat of litigation and vendor rejection.

If it were to revoke PDVSA's concession, Venezuela could try to make the case that such a move is justified due to the company's poor operating performance, which has resulted in a steep decline in production. (08/14/17)

Credit Considerations

Key Drivers

2. Stripping PDVSA Is an Unlikely Threat in Push for Restructuring

While the legal ability of the Venezuelan government to strip PDVSA of its exploration and production rights may not be in doubt, its practical ability to do so is questionable. It's likely that many international drilling and oilfield service companies would refuse to do business with a new entity created at the detriment of PDVSA debtholders. Many of these creditors may be significant investors in these service companies.

Consequently, it's unlikely that the Venezuelan government could credibly use the threat of stripping out PDVSA's cash flow to incite a greater willingness on the part of bondholders to consider a debt restructuring. (08/14/17)

Company Filing

"Under Venezuelan law, the hydrocarbon reserves that we develop and operate belong to Venezuela. The rights to exploration of these hydrocarbon reserves are reserved for Venezuela. We were formed to coordinate, monitor and control operations related to Venezuela’s hydrocarbon reserves."

Bond Prospectus, Petroleos de Venezuela
PDVSA 8.5% 2017 Note Prospectus, March 17, 2011

Quote located on page 10, click to view entire filing

3. PDVSA Bondholders Have a Strong Case If State Revokes Concession

In the event that Venezuela does attempt to revoke PDVSA's concession to explore and exploit its hydrocarbon reserves, the company's bondholders will likely attempt to make the state liable for their debt under fraudulent transference -- or by trying to pierce the corporate veil. The latter option is lent credence by Venezuela's constitutionally required ownership of PDVSA as well as its substantial control over the company's long-term strategy and day-to-day operations. (08/14/17)

Company Filing

"While the Venezuelan Constitution requires that Venezuela retain exclusive ownership of us, it does not require the country to continue to conduct its hydrocarbon exploration and exploitation activities through us. If the Venezuelan government elects to conduct its hydrocarbon activities other than through us, our operations will be materially and adversely affected."

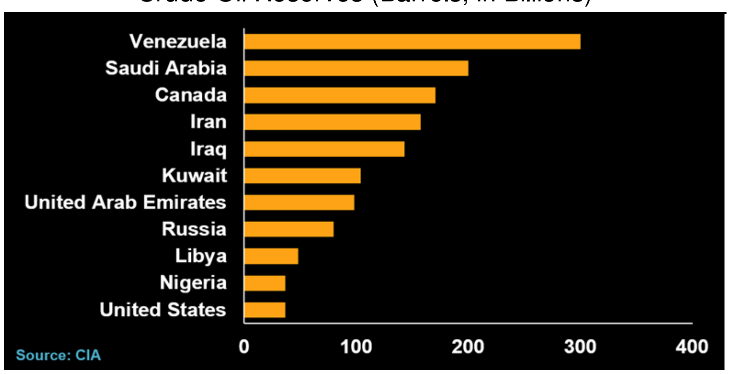
Bond Prospectus, Petroleos de Venezuela
PDVSA 8.5% 2017 Note Prospectus, March 17, 2011

Quote located on page 10, click to view entire filing

4. Just $5 a Barrel for 5% of Assets Covers Venezuela, PDVSA Bonds

Even at current low prices, Venezuela's 300 billion barrels of oil reserves would provide abundant asset coverage for the country's and PDVSA's dollar debt. Entering into new joint ventures to develop currently non-producing reserves comprising 5% of the total and generating just $5 a barrel upfront would yield $75 billion. That would be adequate to repay all $66 billion of Venezuela's sovereign bonds and PDVSA's dollar debt, leaving cash flow from currently producing assets to service bank loans and fund imports. (08/14/17)

Crude Oil Reserves (Barrels, in Billions)



5. Reserves Could Mean Modest Haircut in a PDVSA Debt Restructuring

Massive oil reserves could mean that a restructuring of PDVSA and Venezuela debt need not involve a large reduction in principal. As the current crisis is more one of short-term liquidity rather than long-term solvency, a debt restructuring may more appropriately be addressed through a distressed exchange of existing bonds for new longer-term and lower-coupon securities. This would result in substantial cash flow relief, allowing the company to fund much-needed capital spending and the state to replenish imports.

Many bondholders may be more amenable to this than to giving up principal, particularly given the significant potential long-term prospects of developing Venezuela's substantial oil reserves. (08/14/17)

News Release

" 'Less-favorable terms' could include a reduced principal amount, extended maturities, a lower coupon, a different currency of payment, or effective subordination. When such exchanges occur, we revise the rating on the obligation to 'D' (default), even if only a portion of the rated bonds is subject to the exchange offer. In addition, we revise the sovereign credit rating to 'SD' (selective default), indicating that the sovereign is proposing to pay less than what it had originally undertaken."

John Chambers - Standard & Poor's
Research Report, June 28, 2011

Quote located on page 2, click to view entire news release

6. Venezuela Likely Needs More Stable Government for Sizeable JVs

One quandary that PDVSA bondholders face is that the proceeds of asset sales are more likely to be used to fund maturing debt if President Nicolas Maduro remains in power, while a new government is more likely to give greater priority to replenishing much-needed imports of consumer goods. Yet it may require the promise of potentially greater political and economic stability that a new government could bring to entice foreign investors to participate in large-scale joint ventures in the first place.

If the recent trend of reduced engagement by international oil companies -- as signaled by local staff reductions at Chevron, Repsol and Statoil -- escalates, it will become increasingly difficult for PDVSA to enter into new joint venture projects. (08/14/17)

Chevron, Total Pull Foreign Staff in Venezuela

- Political crisis fueling violence in nation reliant on crude
- Statoil also says it's removed all remaining expatriate staff

Repsol SA pulled all foreign workers from its oil fields in Venezuela amid a deepening political crisis, while Chevron Corp. and Total SA have removed a small number of employees, said people with knowledge of the companies. Norway's Statoil ASA has withdrawn its expatriate staff.

Source: Bloomberg News, August 7, 2017

7. Near-term Venezuela Regime Change Negative for PDVSA 2017 Bonds

A near-term regime change in Venezuela could be negative for Petroleos de Venezuela (PDVSA) 8.5% notes due in November, which have rallied to almost 88 cents on the dollar on renewed confidence that the company will continue its policy of servicing foreign debt -- at least until the end of the year. While President Nicolas Maduro can accomplish this using an estimated $10 billion in foreign-exchange reserves, new leadership would quite likely begin an immediate restructuring of PDVSA debt. (08/10/17)

8. Venezuela Debt Restructuring Would Open Door to Outside Help

Credible near- and long-term strategies to address the Venezuelan economy's problems -- combined with a successful restructuring of sovereign and PDVSA debt -- should open the door for external assistance, financial as well as desperately needed humanitarian aid. While Venezuela was in a position to shun international organizations like the IMF when oil was at $100 a barrel, it can no longer do so at the average forward strip price through 2021 for Brent crude of about $54 a barrel. (08/10/17)

Economic Report

"By re-engaging, Venezuela should be able to unlock significant financial assistance from the international community to meet humanitarian needs .. several billion dollars of assistance might be unlocked more significant assistance could come once Venezuela reaches agreement on a detailed medium-term economic plan with the International Monetary Fund and the World Bank .. Venezuela might obtain tens of billions of dollars .. new loans and an officially supported debt-restructuring operation."

George Makoff - World Economic Forum
July 26, 2017

Click to view the full report

9. Just a $5 Oil Price Increase Clearly Moves the Needle for PDVSA

An increase in crude oil prices of $5 a barrel should add $3 billion to PDVSA's ability to service an estimated $3.1 billion in principal and interest payments on its dollar bonds in 2018. This assumes a 10% reduction in oil- and petroleum-products exports from 2.1 million barrels a day (MMBOED) in 2016, accounting for declining output. Further adjustments are offsets for an estimated 0.15 MMBOED of oil imports and 0.1 MMBOED of non-cash oil exports, putting estimated 2018 revenue at $28.1 billion.

The $5 a barrel increase is based off the PDVSA price basket of $46.61 a barrel and the Brent price of $51.94 on Aug. 8. (08/10/17)

Interactive Chart - Click to Change Parameters

	Cash Exports	Non-Cash Exports	Cash Imports	
Production Cut from 2016	10%	10%	10%	
2016 Oil Exports/Imports (mbld)	2,100	100	150	
Crude Oil Price ($/bbl)	46.60	46.60	51.90	
Cash Flow ($bn)	32.15	1.53	2.56	28.06
Production Cut from 2016	10%	10%	10%	
2016 Oil Exports/Imports (mbld)	2,100	100	150	
Crude Oil Price ($/bbl)	51.60	51.60	56.90	
Cash Flow ($bn)	35.60	1.70	2.80	31.10
Oil Price Increase ($/bbl)	5.00	5.00	5.00	
Cash Flow Increase ($bn)				3.04
Source: Bloomberg Intelligence				

10. Non-Oil Price Factors Dominate Near-term Venezuela Outlook

Over the longer term, a recovery in crude oil prices will likely be the single most important catalyst for a recovery in Venezuela's economy and PDVSA's credit. Near term, equally important determinants are: whether or not Venezuelans are able to effect a regime change, the speed at which the country is willing and able to draw down its international reserves and the ability to draw on external assistance to revive imports of critical goods and services.

Importantly, rising crude oil imports will partly offset the benefits of a higher price for Venezuela's oil. (08/10/17)

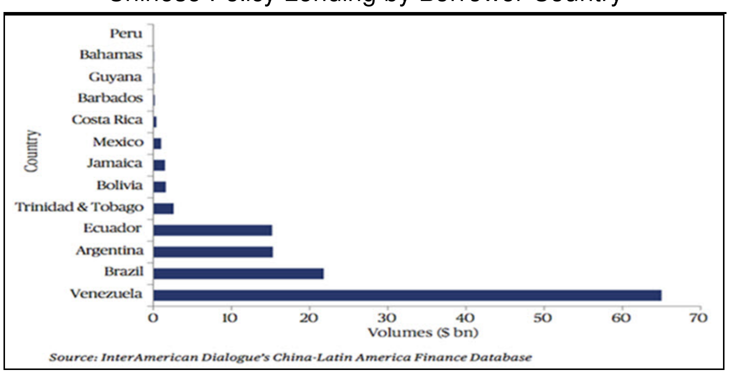
IMF Venezuela Reserve Foreign Exchange Holdings

11. PDVSA, Debt Restructuring Must Include Massive China Loans

Venezuela is by far China's largest borrower in Latin America, with total bank loans that could exceed $60 billion. Even if half of this amount is still outstanding, it would surpass the aggregate amount of PDVSA bonds. If Venezuela were to attempt to restructure its sovereign and PDVSA's corporate debt, it would need to convince bondholders that it has a credible strategy not only to address the core challenges facing its economy and PDVSA, but also its debt to China and Russia.

In the absence of a realistic and plausible plan, many investors are likely to be highly reluctant to back a restructuring that potentially involves a reduction in principal and an extension of maturities, even if the alternative is a default. (08/10/17)

Chinese Policy Lending by Borrower Country



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