OPINION: The 2010 Annual Report of Petroleos de Venezuela

"A 415 page report on the 2010 activities of the Venezuelan state-owned petroleum company Petroleos de Venezuela has just been released and it provides a fascinating look into how the company is being mismanaged," says Gustavo Coronel, a former member of the Board of Directors of PDVSA.

By Gustavo Coronel

A 415 page report on the 2010 activities of the Venezuelan state-owned petroleum company Petroleos de Venezuela (PDVSA) has just been released, as part of a larger report on the activities of the Ministry of Energy and Petroleum. It provides a fascinating look into how the company is being mismanaged.

From being a world-class enterprise before Chavez arrived in power, the company has been converted into an amorphous agglomerate of a dozen companies that import and distribute food, build houses, pave roads, train athletes and has adopted as its mission “the promotion of a socialist society”. As a result, its core business of finding, producing, refining and selling hydrocarbons has become a subordinate task. The company has lost 800,000 barrels per day of production which is only partly compensated by contracts with foreign operators, its refineries are working at 70% capacity and a good portion of its oil is being delivered at subsidized prices to ideologically friendly countries.

The Name Game

In Petroleos de Venezuela almost any physical asset is given the name of a “revolutionary hero”. When the company arbitrarily decided to take over the drilling rigs belonging to U.S. company Helmerich and Payne -- so as to not pay this company a $43 million debt -- the rigs were promptly baptized with the names of Venezuelans who became “revolutionary martyrs” in a bloody coup against the democratic government, way back in 1962.

The PDVSA report itself utilizes a new terminology, full of political symbolism, replacing the traditional technical language of the oil industry. A community project now gives “supreme happiness to the people”, in the best Mao Tse Tung style. A new oil well becomes a “socialist unit of production”, in the best Stalin style. This habit could be labeled as harmless or amusing, except for the fact that it indicates the existence of a mental framework among managers that has nothing to do with running an oil company.

Bombastic Objectives but Parochial Programs

One of the main objectives of the company is “enhancing the importance of Venezuela as an energy power” but some of the “accomplishments” listed under this lofty objective sound pretty insignificant, such as “Providing (unspecified) technological upgrading to the guest house in Lagunillas [an oilfield]”. We suspect the technological upgrading refers to the acquisition of a new TV set.

Since the company now has an “Agricultural” Division (PDVSA Agricola), some of the programs accomplished during 2010 included the sowing of “2500 hectares of Cassava” and the production of “922 tons of chicken.”

The Electrical Division of the company mentioned the acquisition of 1100 Chinese trucks to bring diesel to the portable electrical generators bought in 2010 to face the national electrical crisis.

The maritime Division (PDVSA Naval) announced the “acquisition of oil 42 tankers”, none of which can be found, except in paper.

Seriously Fraudulent Claims

Although much of the contents simply fall in the category of the grotesque, there are serious fraudulent claims. One of the most important has to do with the so-called “certification” of proven reserves of oil in the Orinoco region.

Although the existence of significant resources of heavy oil in this region has been known for more than 50 years, "proven reserves", properly defined, indicates that some 10% of the oil in place can be recovered, given the heavy nature of the oil.

However, the current management has applied an arbitrary recovery factor of 20% and has “suddenly” doubled the “proven reserves” of the country, without doing the geological and engineering work required to substantiate this claim. In this report the company claims to have “certified” 215 billion barrels of “proven reserves”, by “drilling 143 stratigraphic wells” in the 55,000 square kilometers of the area. Not only is this density of drilling totally insufficient to throw much light on the spatial continuity of the producing rocks but also stratigraphic wells cannot provide any knowledge on oil reservoir behavior since, by definition, they are not subject to extensive production. This is a fraudulent claim.

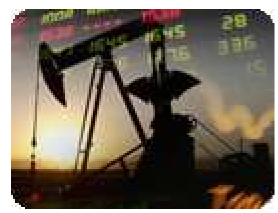
The same false claim has been made in connection with “proven reserves” of natural gas in the order of 6 trillion cubic feet in the Gulf of Venezuela, “certified” by drilling and testing three wells.

This is not possible to do with such a meager amount of data.

Equally unsubstantiated is the claim to have “certified” 84 million barrels of oil in the Orinoco region by doing “seismic “ work together with a company from Belarus. Seismic work as such cannot “certify” proven reserves.

Another claim made in the report that properly belongs in the realm of science fiction is that, by using an average of 64 active drilling rigs during the year, they drilled 3778 wells. This would amount to more than a well per week per rig -- an obvious impossibility.

Financial Hanky Panky



The report claims that the relation of financial debt to assets of the company is 17%, a low figure as compared to other oil companies. However, they fail to list among its debts the Chinese loans made to Venezuela during the last three years, now on the order of $28 billion. This would change this ratio significantly, placing it in the danger area. This debt is being paid by PDVSA since the report lists a payment of $2.5 billion made in 2010.

Another debt not listed in the books is the amount still owed to the numerous contractors expropriated by PDVSA. Helmerich and Payne is only one of the many companies that saw their assets arbitrarily taken over by the government.

Meanwhile, extreme under-investment has led to operational collapse.

The report lists 2010 petroleum related investments of $9.3 billion. This is an insufficient level of investment to maintain current level production, much less to increase it or to properly modernize refineries and other basic assets. In comparison, ExxonMobil's annual level of investments is about $30 billion, more than three times as much, with a similar level of oil production.

Corruption

The report mentions the hiring of the offshore drilling rig PetroSaudi Saturn to drill for gas in the waters of northeastern Venezuela. This transaction should be investigated, given the disastrous and irregular deal made for the rig Aban Pearl that sank some time ago and the mystery surrounding this new deal.

In short, a closer look at PDVSA's "report" clearly reveals the tragic extent of PDVSA’s deterioration.

Gustavo Coronel was author of the Cato Institute study "Corruption, Mismanagement and Abuse of Power in Hugo Chavez's Venezuela" and was the Venezuelan representative to Transparency International from 1996 to 2000. In 1994, he founded Pro Calidad de Vida, an NGO promoting anti-corruption techniques in government and civic education for children in Venezuela, Panama, Paraguay, Mexico and Nicaragua.

Coronel was President of Puerto Cabello in Venezuela from 2001 to 2002. He was Chief Operations Officer (COO) and acting CEO of the Corporacion Venezolana de Guayana (CVG), the $35 billion Venezuelan government conglomerate designed to exploit and run all of Venezuela's mineral, metal and mining operations, from 1994-1995. He was on the Board of Directors of PDVSA from 1976 to 1979.