Chavez Death Brings Uncertainty, Hope to Oil Patch

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HOUSTON (AP) — Venezuela's oil production is poised to reverse a dramatic decline that has seen exports fall by nearly half during Hugo Chavez's time as president.

Following Chavez's death Tuesday, Venezuela, which is a member of OPEC and sits on the world's second-largest oil reserves, faces near-term political uncertainty that could bring further turmoil to its oil industry. And even under the best circumstances it would take years to increase production and exports, analysts say. But any new government would have a powerful economic incentive to make that a top priority.

Exports fell from 3 million barrels per day in 2000 to 1.7 million barrels per day in 2011. Chavez relied heavily on the country's oil income to fund social programs, but reinvested relatively little of it to exploit new oil fields and replace depleted ones.

There has been no indication from the country's national oil company, Petroleos de Venezuela, S.A., or PDVSA, whether it will invite more foreign investment or increase its own investment in new production. But Chavez held such sway over the company's direction that his death means the direction could change dramatically.

"Without his charisma and force of character, it is not at all clear how his successors will maintain the system he created," said Daniel Yergin, author of a Pulitzer Prize winning book on global energy politics.

The discontent in Venezuela that grew with the decline of oil prices in the late 1990s helped Chavez get elected. The high oil prices that followed helped him consolidate power by allowing him to fund programs popular with Venezuelans and making allies in the region by offering cut-rate oil deals, according to Yergin.

But his refusal to reinvest in the industry, along with a strike at PDVSA in 2002 that sapped the company of some of its best talent, led to deep decay in the country's most important industry. Chavez nationalized some oil and gas assets owned by international oil companies, such as Exxon Mobil, in order to make PDVSA the majority stakeholder in all Venezuelan projects. That prompted Exxon and others to abandon work in the country, further reducing the country's access to oil and gas technology and expertise.

Citgo, the company's U.S. division, operates refineries in Texas, Louisiana and Illinois, and sells fuel through thousands of gas stations. Citgo has been used by Chavez to distribute discounted heating oil to poor American families in a high-profile program aimed at criticizing Washington's approach to the poor.

The world oil market's response to Chavez's death was muted — oil rose slightly in electronic trading in New York to $91.05 per barrel. That's 8 times the price of a barrel when Chavez took office 14 years ago.

Analysts say Venezuelan production will likely fall further in the short term because PDVSA executives may lack clear instructions from a government in transition about how to proceed. But Venezuelan oil supply has been declining for so long and oil markets are well supplied that traders are not concerned that further erosion in Venezuelan supply will disrupt markets.

That could change, however, if instability erupts as new leaders jostle for power and new elections are held, according to Sarah Ladislaw, co-director of the Energy and National Security Program at the Center for International and Strategic Studies. Dramatic unrest could lead to a sharp drop in exports and higher oil prices.

The political uncertainty is already keeping countries who had been investing in the Venezuelan oil industry, including Russia, China and India, on the sidelines.

But once a new government is established, it will likely look to fix the country's energy industry as quickly as possible to help alleviate a dismal economic situatio.

Venezuela's refineries are so weak that the country is forced to import enormous amounts of fuel from the U.S. and elsewhere even as it exports crude. Those imports are especially costly because the government heavily subsidizes gasoline. Venezuelans pay only a few cents per gallon for gasoline, and the subsidies cost the government $25 billion per year, according to Jason Bordoff, Director of the Center on Global Energy Policy at Columbia University.

An increase in oil production and exports could be a boon for the country. "The potential for Venezuelan supply is enormous," Bordoff says.

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