

The course essay example

[Business](#), [Company](#)



Foreign Direct Investment in Venezuela's Petroleum Industry

Q.

Under the term of the new regulations announced in 2004 governing FDI in Venezuela's oil sector. What are/where the potential implications for oil production there, the long-term profitability of PDVSA, and the economic growth in Venezuela.

A.

In October 2004, Hugo Chavez the Venezuelan President announced that the royalties that the government would charge for drilling the oil along the Orinoco oil belt in the country's southeast would be increased. He hiked due the government to 16.7%. He also changed the terms on any new joint ventures with foreign oil companies. For new ventures, royalties payable to the government will be 30% and PDVSA will take a 51% stake, effectively giving PDVSA control.

The foreign companies that were a part of the strategic associations questioned the royalty hike being legal. Other companies like OSA's concerns were that the new PDVSA structure, increased royalty and tax rates would negatively affect the profitability of their operations.

Statistics show that the impact of these terms was not healthy at the start, as the real GDP growth in 2004 was 17.7% which dropped to 9.3% in 2005. But this jolt was temporary since PDVSA was a strong company. The International Oil Companies disputed the legality of the claim, but almost all of them ended up paying the taxes and the royalties at a lower negotiated

rate and by 2005 Venezuela was ranked at number eight among the largest oil producing countries, and today it is on number five. The purpose of introducing these terms was to regain PDVSA's control over the oil industry. The government take has increased by 300% and the State will receive 23% more in additional incomes. However the current statistics show a different picture, but these figures are a result of recent economic depression and oil crisis.

Although Venezuela nationalized its oil fields in Orinoco Belt, she continued to offer attractive investment opportunities. In fact, foreign oil executives resumed their business with the Chavez administration yet after the highly controversial 2004 reforms. The move of increasing the royalty was though surprising yet left very positive long run impacts on the oil production, profitability of PDVSA and on the economic growth of Venezuela.