

Message Text

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ACTION EB-08

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C O N F I D E N T I A L SECTION 1 OF 2 LA PAZ 7474

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E.O. 12065: GDS 8/31/85 (PORTER, BRUCE F.) OR-P
TAGS: EMIN, BL
SUBJECT: BOLIVIAN TIN AND PETROLEUM: CONTINUED PRODUCTION DECLINES
LIKELY

1. (CONFIDENTIAL ENTIRE TEXT.)

2. SUMMARY: A PRINCIPAL SLOGAN OF BOLIVIA'S 1952 REVOLUTION
WAS "LAND TO THE PEASANTS, THE MINES TO THE STATE." WHILE THE
EFFECT OF LAND REFORM ON THE COUNTRY'S AGRICULTURAL PRODUCTION
HAS BEEN MIXED, NATIONALIZATION OF BOLIVIA'S MAJOR MINES TWO
AND A HALF DECADES AGO INAUGURATED AN ERA OF INEFFICIENCY, BLOATED
PAYROLLS AND, FAR WORSE, A VIRTUAL ABSENCE OF INVESTMENT IN THE
SEARCH FOR AND DEVELOPMENT OF NEW DEPOSITS. AS A RESULT OF
DECADES OF NO EXPLORATION NOR DEVELOPMENT OF NEW MINES, BOLIVIAN
TIN PRODUCTION APPEARS NOW TO HAVE ENTERED A PERIOD OF DECLINE.
FURTHERMORE, SUBSIDIZED PRICES OF PETROLEUM PRODUCTS PLUS
THE SAME HISTORIC PATTERN OF LONG NEGLECTING INVESTMENT IN
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FAVOR OF FEATHERBEDDING AND PROVIDING SOCIAL BENEFITS HAS BROUGHT
BOLIVIA TO THE VERGE OF BECOMING A PETROLEUM IMPORTING NATION.
BOLIVIA'S SAGGING PRODUCTION OF OIL AND TIN COMBINE TO HAVE A
NEGATIVE IMPACT ON BOLIVIA'S ECONOMIC FUTURE. TO OFFER
A PROSPECT OF LONG-TERM SUCCESS, ANY GOB ECONOMIC REFORM PROGRAM
WILL HAVE TO ADDRESS THE STRUCTURAL PROBLEMS OF THE TIN AND
PETROLEUM INDUSTRIES, AS WELL AS THE IMMEDIATE TASK OF FINANCIAL

STABILIZATION. END SUMMARY.

3. AS IS WELL KNOWN, WITH THE EXCEPTION OF A REDOMINANTLY SUBSISTENCE AGRICULTURAL SECTOR, BOLIVIA'S VISIBLE ECONOMY IS DOMINATED BY MINING (17 PERCENT OF GDP, 70 PERCENT OF EXPORTS) AND PETROLEUM (4 PERCENT OF GDP). HOWEVER, DESPITE RAPIDLY RISING WORLD PRICES FOR BOTH COMMODITIES, THE COUNTRY'S PRODUCTION OF EACH APPEARS TO BE IN SECULAR DECLINE, A PROBLEM THAT MUST BE ADDRESSED BY ANY FUTURE ECONOMIC STABILIZATION/REFORM PROGRAM. (BOLIVIA'S STILL WEEKS-OLD NEW GOVERNMENT HAS PUBLICALLY ACKNOWLEDGED THE TIN/PETROLEUM PROBLEM BUT, NOT SURPRISINGLY, HASN'T YET HAD TIME TO EVEN PROPOSE POSSIBLE COUNTER-MEASURES.) BECAUSE OF THE OBVIOUS RELEVANCE THE CONTINUING SLIDE IN THE PRODUCTION OF THESE TWO KEY COMMODITIES HOLDS FOR BOLIVIA'S ECONOMIC FUTURE, WE HAVE PUT TOGETHER A BRIEF DISCUSSION OF THE BASIC PROBLEMS FACING BOTH SUBSECTORS.

4. PETROLEUM: BOLIVIA'S DECLINING OIL PRODUCTION (PHYSICAL OUTPUT PEAKED IN 1973 AND HAS FALLEN AN AVERAGE OF 11 PERCENT/YEAR SINCE 1976 AND DROPPED A FULL 10 PERCENT IN THE FIRST QUARTER OF 1979) IS PRIMARILY THE RESULT OF INSUFFICIENT EXPLORATION, THE CONSEQUENCE IN THRUN OF YPFB'S INCREASINGLY PRECARIOUS FINANCIAL POSITION. (WITH TOTAL DEBT CLOSE TO BOOK VALUE ASSETS, THE STATE OIL MONOPOLY IS RAPIDLY APPROACHING TECHNICAL INSOLVENCY.) AND ALTHOUGH THE REASONS FOR YPFB'S MONETARY DIFFICULTIES INCLUDE

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FEATHERBEDDING, CORRUPTION, MISMANAGEMENT AND A HISTORY OF EXCESSIVE WAGE SETTLEMENTS, THE PRINCIPAL PROBLEM IS THE ARTIFICIALLY LOW PRICE STRUCTURE FOR ITS PRODUCTS: FOR EXAMPLE, 30 CENTS/GALLON FOR GASOLINE, 6 PCENTS/GALLON FOR HOUSEHOLD KEROSENE. (IT COSTS YPFB APPROXIMETLY \$US 21 TO PRODUCE A BARREL OF PRODUCT IT SELLS FOR LESS THAN \$ 12.)

5. CLEARLY, THE OBVIOUS FIRST STEP THE GOB SHOULD TAKE IS A MAJOR (AT LEAST 100 PERCENT) INCREASE IN PETROLEUM PRODUCT PRICES. PRODUCTION WOULD STILL CONTINUE TO FALL FOR SOME TIME EVEN IF PRICES WERE RAISED AND EXPLORATION SHARPLY ACCELERATED; HOWEVER, AN EARLY PRICE HIKE AND STEPPED-UP EXPLORATION WOULD AT LEAST BE A START.
UNLESS A SWAP OF BOLIVIA'S STILL EXCESS GASOLINE FOR BRAZILIAN KEROSENE, DIESEL AND FUEL OIL CAN BE ARARANGED, THE IMPENDING NEED TO OMPORT PRODUCT WILL HAVE A SUBSTANTIAL NEGATIVE EFFECT ON THE GOB'S ALREADY CRITICAL BALANCE OF PAYMENTS SITUATION.

6 THERE ARE TWO ADDITIONAL FACTORS FURTHER CLOUDING BOLIVIA'S BLEAK OIL OUTLOOK. FIRST IS THE POSSIBILITY THAT DESPITE EVEN AN HEROIC INCREASE IN EXPLORATION, THE COUNTRY MAY SIMPLY NOT POSSESS MUCH ADDITIONAL EXPLOITABLE PETROLEUM. AS IT IS, MOST

OF BOLIVIA'S LIQUID PETROLEUM IS ACTUALLY CONDENSATE PRODUCED IN ASSOCIATION WITH NATURAL GAS. TO PRODUCE MORE NEEDED LIQUIDS FROM EXISTING WELLS REQUIRES PRODUCING MORE GAS. THE PROBLEM THEN BECOMES WHAT TO DO WITH THE GAS--FLARING IT IS WASTEFUL AND REINJECTION IS COSTLY. BUT THE THIRD ALTERNATIVE, SELLING THE "EXCESS" GAS, IS NOT PRESENTLY PROMISING. ARGENTINA, BOLIVIA'S ONLY CURRENT CUSTOMER FOR PIPED GAS (220 MCFD), IS NOT DISPOSED TO INCREASE ITS PURCHASES. AND THE SALE OF BOLIVIAN GAS TO BRAZIL (VIA A PROPOSED PIPELINE FROM SANTA CRUZ TO SAO PAULO) SEEMS STALLED UNTIL BOLIVIAN MAKES THE POLITICALLY CONTROVERSIAL DECISION EITHER TO PURSUE THE PROJECT OR DROP IT. WITHOUT A CLEAR, POSITIVE DECISION ON THE GAS SALE TO BRAZIL, BOLIVIA'S LONG-TERM PROSPECTS TO BALANCE ITS EXTERNAL ACCOUNTS AND MEET ITS DEBTS WILL REMAIN CLOUDY.

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7. TIN. DESPITE RECORD WORLD TIN PRICES, BOLIVIA'S 1979 TIN OUTPUT IS EXPECTED TO FALL SEVERAL PERCENTAGE POINTS BELOW THE 30,200 METRIC TONS PRODUCED LAST YEAR. AS WITH PETROLEUM, THE MAJOR CAUSE OF DECLINING PRODUCTION IS A LACK OF EXPLORATION THAT GOES BACK AT LEAST TO 1952, THE YEAR THE BULK OF BOLIVIAN TIN PROPERTIES WERE NATIONALIZED. STILL UTILIZING MINES ALL OF WHICH WERE DISCOVERED DECADES AGO, YIELDS FROM BOTH COMIBOL AND MANY PRIVATELY OWNED PROPERTIES HAVE STEADILY DECREASED WHILE COSTS HAVE CONTINUED TO RISE. THE HIGH COST OF PRODUCTION COULD BE ATTACKED TO A DEGREE BY A

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THOROUGHGOING REFORM OF COMIBOL (WHERE PER WORKER PRODUCTIVITY IS HALF THAT OF THE PRIVATE MINES) BUT PRODUCTION WILL CONTINUE TO DECLINE UNLESS ENTIRELY NEW DEPOSITS ARE FOUND AND EXPLOITED. BUT GIVEN THE GOB'S INABILITY TO FINANCE THE HIGH COST OF EXPLORATION, IT IS UNLIKELY ANY NEW MINES WILL BE DEVELOPED UNLESS BOLIVIAN MINING IS OPENED UP TO EXTENSIVE FOREIGN INVESTMENT. (A BASIC REFORM OF THE MINING TAX STRUCTURE COULD LEAD TO SOME ADDITIONAL INVESTMENT BY THE EXISTING PRIVATE MINERS BUT THEY SIMPLY LACK THE LARGE AMOUNTS OF CAPITAL NEED TO DEVELOP ENTIRELY NEW TIN PROPERTIES.)

8. FOLLOWING ARE FIGURES SUMMARIZING BOLIVIA'S RECENT HISTORY OF DECLINING OIL AND TIN PRODUCTION AND EXPORTS.

--BOLIVIAN TIN PRODUCTION/EXPORTS (METRIC TONS):

1975	1976	1977	1978	1979 (EST.)
31,952	30,315	30,782	30,200	28,800 (PLUS/MINUS 300)

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--OIL (LIQUIEDS) PRODUCTION (THOUSANDS OF CUBIC METERS):

1973	1974	1975	1976	1977	1978	1979 (EST.)
2,744	2,639	2,342	2,362	2,015	1,870	1,675
(PLUS/MINUS 100)						

--EXPORTS OF LIQUIDS (MILLIONS OF US DOLLARS):

1973	1974	1975	1976	1977	1978	1979 (EST.)
120	164	114	112	67	54	20

9. IN SUM, THE PROBLEMS OF BOTH YPFB AND THE MINING SECTOR CAN ONLY BE MET BY A COMBINATION OF LARGE, NEW INVESTMENTS AND BASIC STRUCTURAL REFORM OF BOTH STATE ENTITIES. UNFORTUNATELY THE GOB ITSELF HASN'T THE RESOURCES TO UNDERTAKE THE NEEDED INVESTMENT, OR IN LIGHT OF THE COUNTRY'S HISTORY AND POLITICAL CULTURE IS IT LIKELY TO OPEN THE DOORS WIDE TO MAJOR FOREIGN INVESTMENT. A MIDDLE, AND MORE LIKELY, COURSE EXISTS: A MAJOR WORLD BANK LOAN AND REFORM PROGRAM FOR COMIBOL PLUS A SWEETENING OF YPFB'S JOINT VENTURE DEALS WITH THE FOREIGN PETROLEUM COMPANIES TO REKINDLE THEIR INTEREST IN BOLIVIA. SUCH FINANCING, HOWEVER, WOULD BE AVAILABLE ONLY IN THE CONTEXT OF BASIC REFORMS OF COMIBOL AND YPFB. OUR ASSESSMENT, THEREFORE,

IS THAT WITHOUT MAJOR FISCAL AND NEW INVESTMENT REFORMS,
BOLIVIA'S PRODUCTION OF
BOTH OIL AND TIN WILL CONTINUE TO SLIP, WITH FALLING PETROLEUM
OUTPUT HAVING OBVIOUS SERIOUS REPERCUSSIONS FOR THE COUNTRY'S
INCREASINGLY TROUBLED ECONOMY. (EVEN WITH THE NEEDED REFORMS,
PETROLEUM PRODUCTION CAN BE EXPECTED TO DROP FOR AN ADDITIONAL
TWO TO THREE YEARS AND TIN PUTPUT TO DECLINE FOR PERHAPS THE
NEXT FIVE YEARS.) HOWEVER, UNLESS THE WORLD PRICE OF TIN DROPS
OR STICKS AT PRESENT LEVELS, IT IS POSSIBLE THAT IN THE NEAR
TERM LOWER PHYSICAL OUTPUT MAY BE LARGEY OFFSET BY CONTINUING
PRICE APPRECIATION. UNLIKE IN THE CASE OF OIL, THE ULTIMATE INTER-
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NAL ECONOMIC EFFECTS OF REDUCED TIN PRODUCTION WILL BE
SIGNIFICANTLY DETERMINED BY EXTERNAL FACTORS: THE WORLD-WIDE DEMAND
FOR TIN, PRODUCTIN LEVELS IN ASIA AND THE PRICE IMPACT OF ANY US
STOCKPILE SALES.

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Message Attributes

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