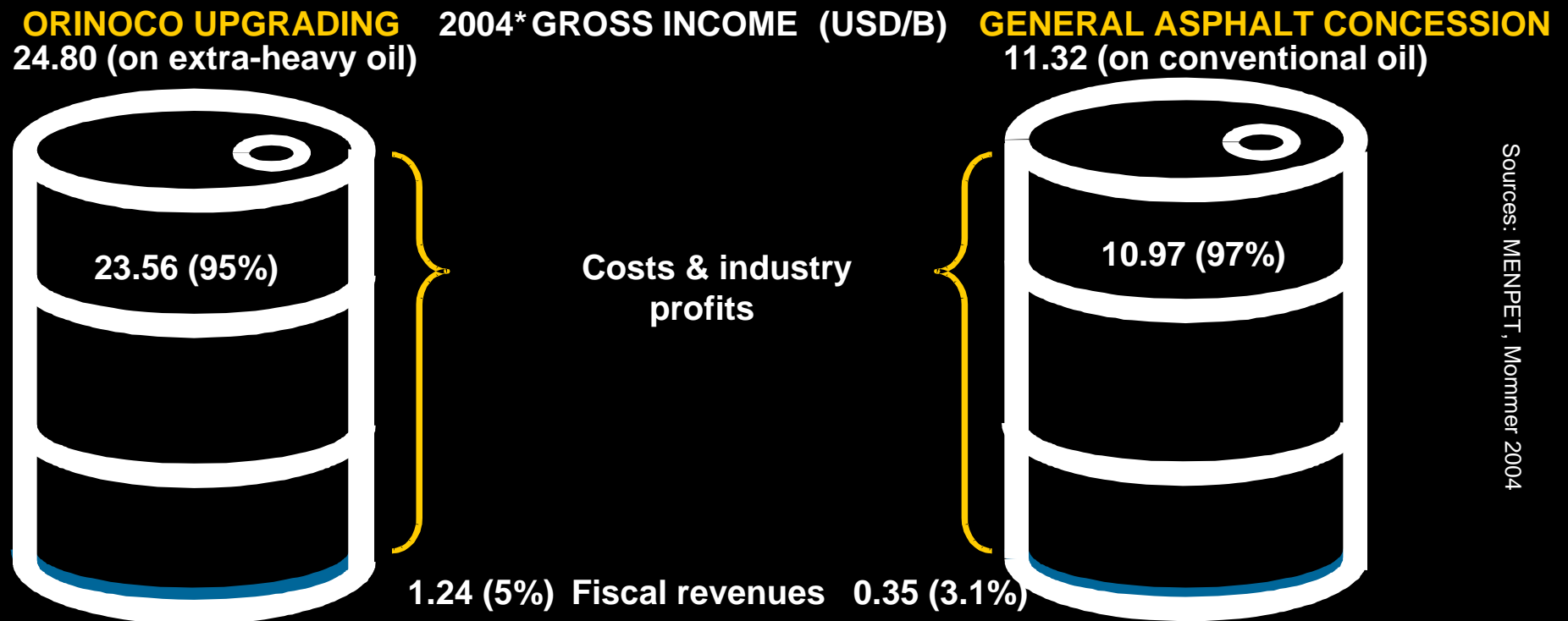

**THE FUTURE AND POTENTIAL
OF PRIVATE INVESTMENT IN VENEZUELA'S UPSTREAM
OIL, AND ITS REGIONAL AND GLOBAL IMPLICATIONS**

UPGRADING ASSOCIATIONS: WHAT WAS IN IT FOR VENEZUELA?



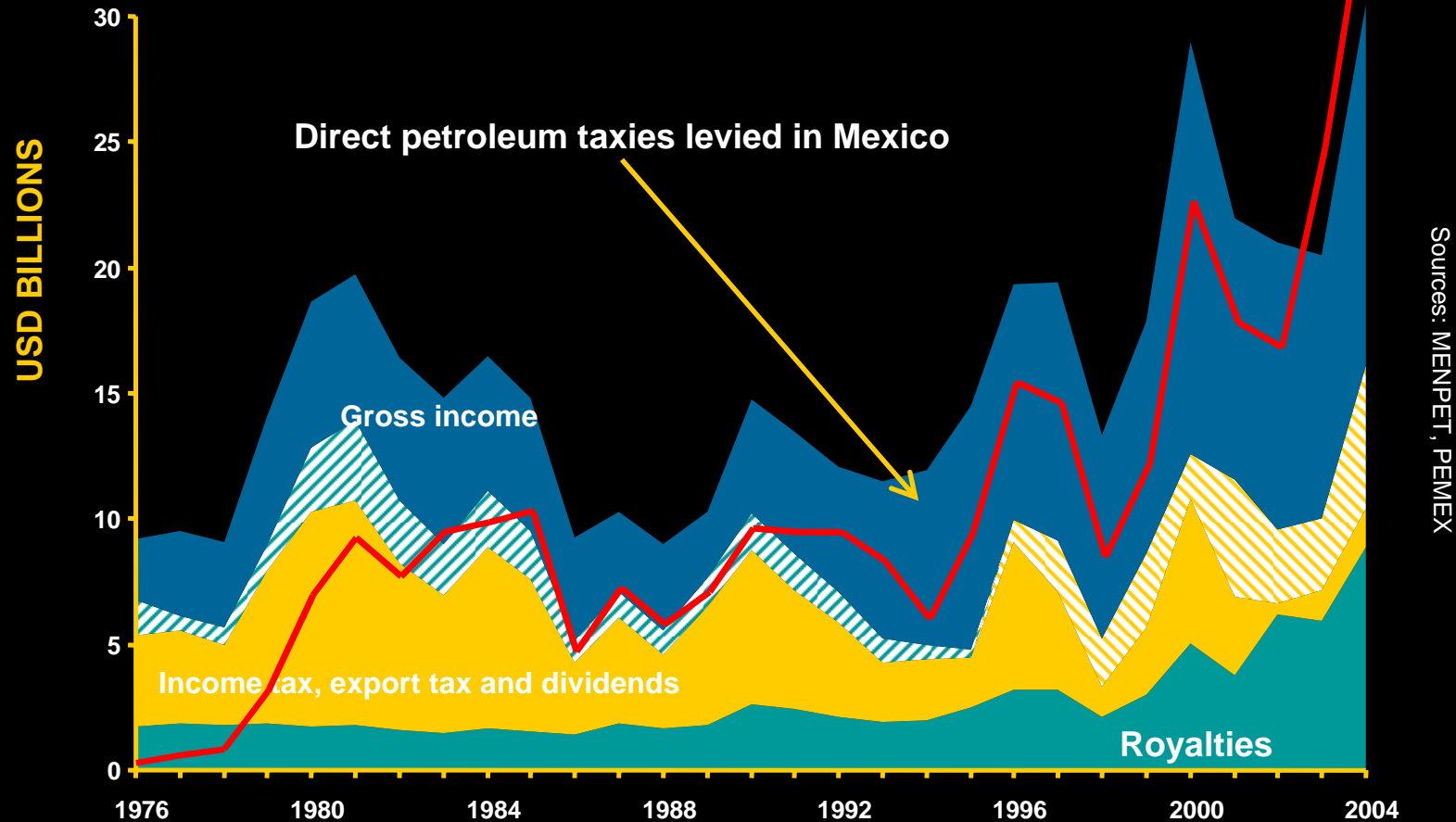
Sources: MENPET, Morner 2004

* First three quarters for Orinoco before rescission of royalty holiday; deflated 1924 figures for General Asphalt

- Until late 2004, the Orinoco upgrading projects had the least favourable fiscal terms in the history of Venezuelan oil in relative terms. They were not the worst in absolute terms, but only thanks to the existence of Orimulsion.
- It was not until the repeal of the royalty holiday that these projects left anything more for Venezuela besides the value of the investment and some jobs.

BREAKDOWN OF THE COLLAPSE IN OIL REVENUES

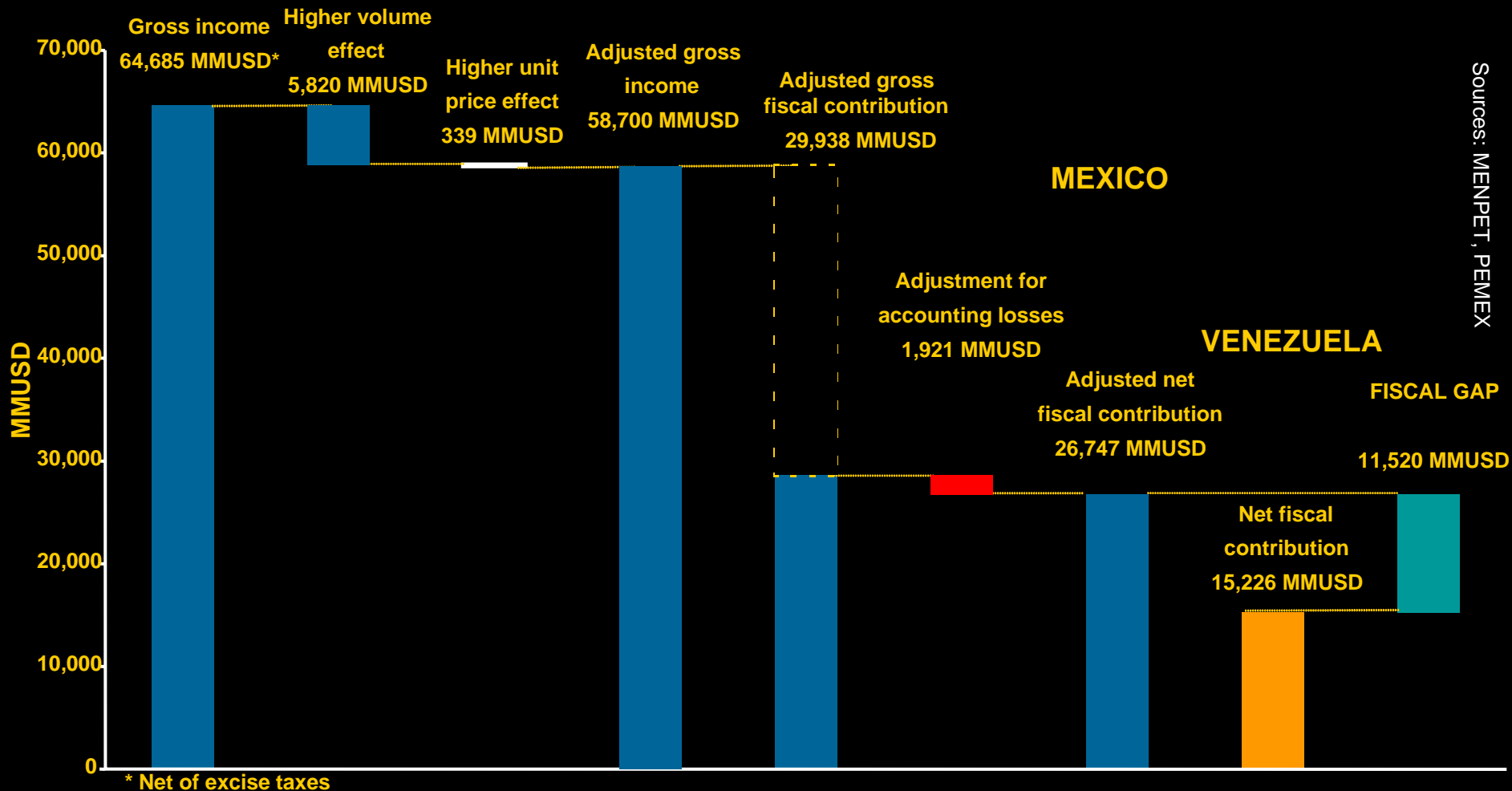
VENEZUELA. KEY FISCAL INDICATORS (1976–2004)



- Venezuelan income tax payment for 2002: 470 MMUSD (<40% of 1998 payment, even though prices 40% higher!). Mexican taxes 23 billion higher in 2003!

A CLOSER LOOK AT THE MEXICO-VENEZUELA FISCAL GAP: 2004

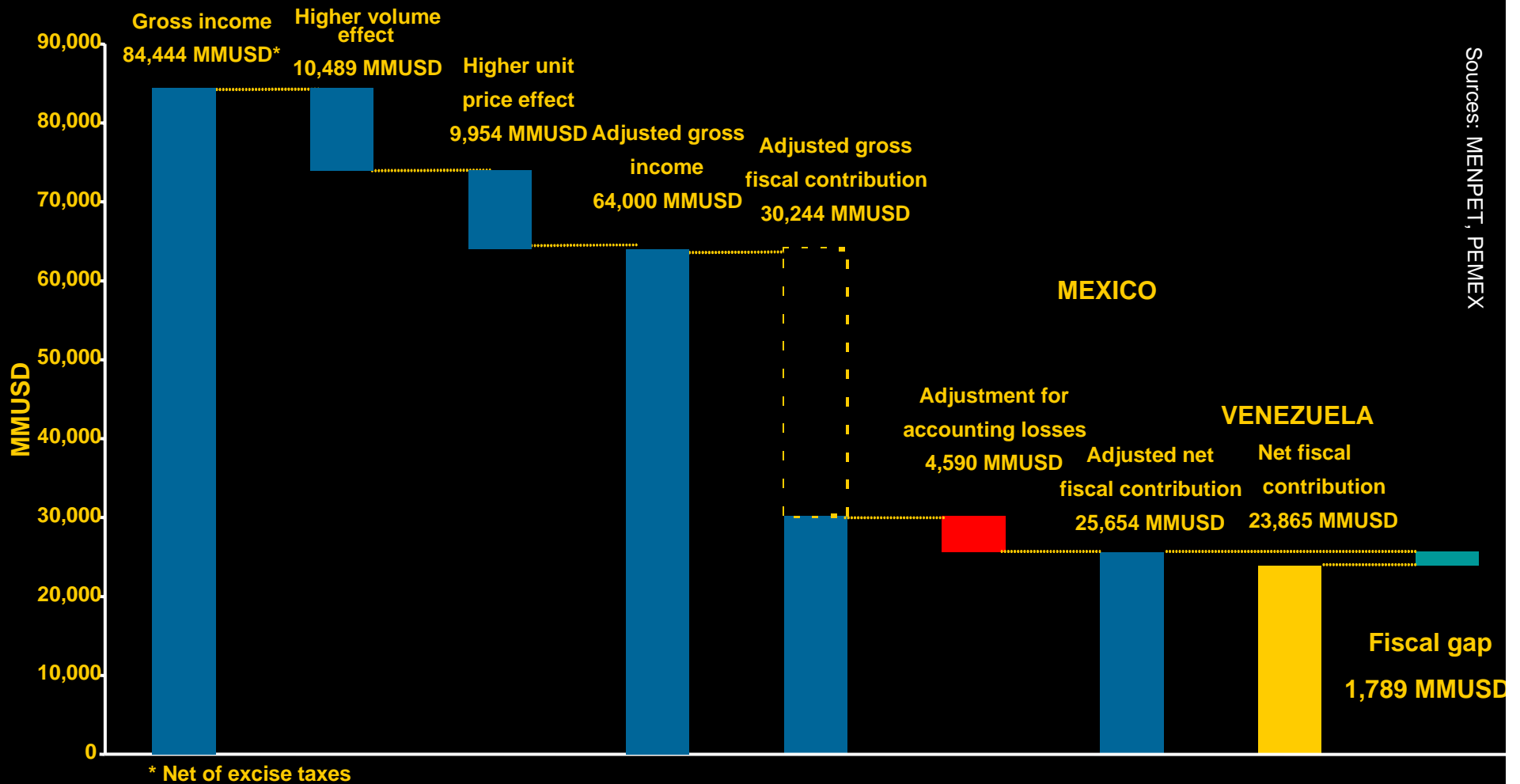
COMPARISON OF OIL FISCAL INCOME, ADJUSTED FOR OUTPUT, PRICES AND ACCOUNTING LOSSES (2004)



Sources: MENPET, PEMEX

ONE YEAR OF FULL OIL SOVEREIGNTY: RESULTS

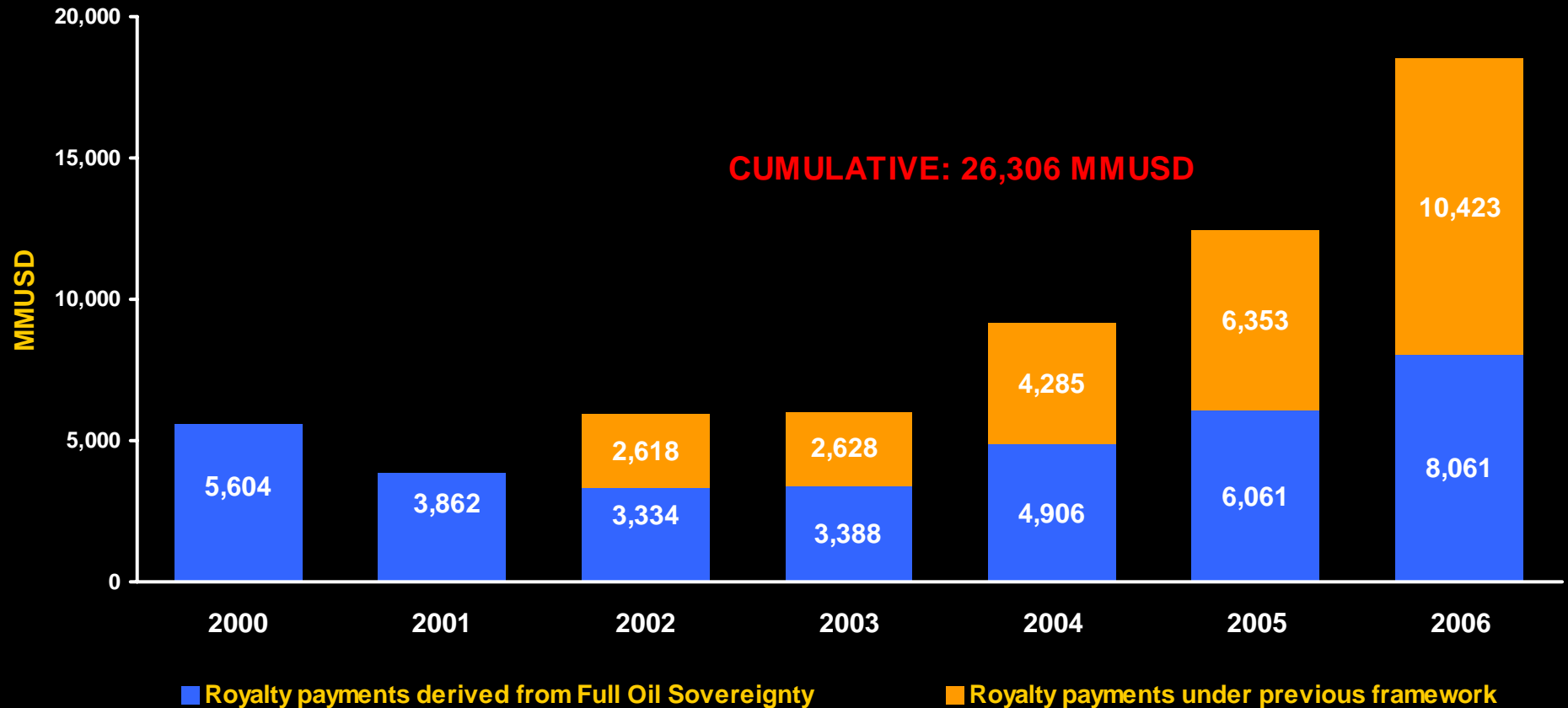
COMPARISON OF OIL FISCAL INCOME, ADJUSTED FOR OUTPUT, PRICES AND ACCOUNTING LOSSES (2005)



Sources: MENPET, PEMEX

THE STAR OF *FULL OIL SOVEREIGNTY*: ROYALTY

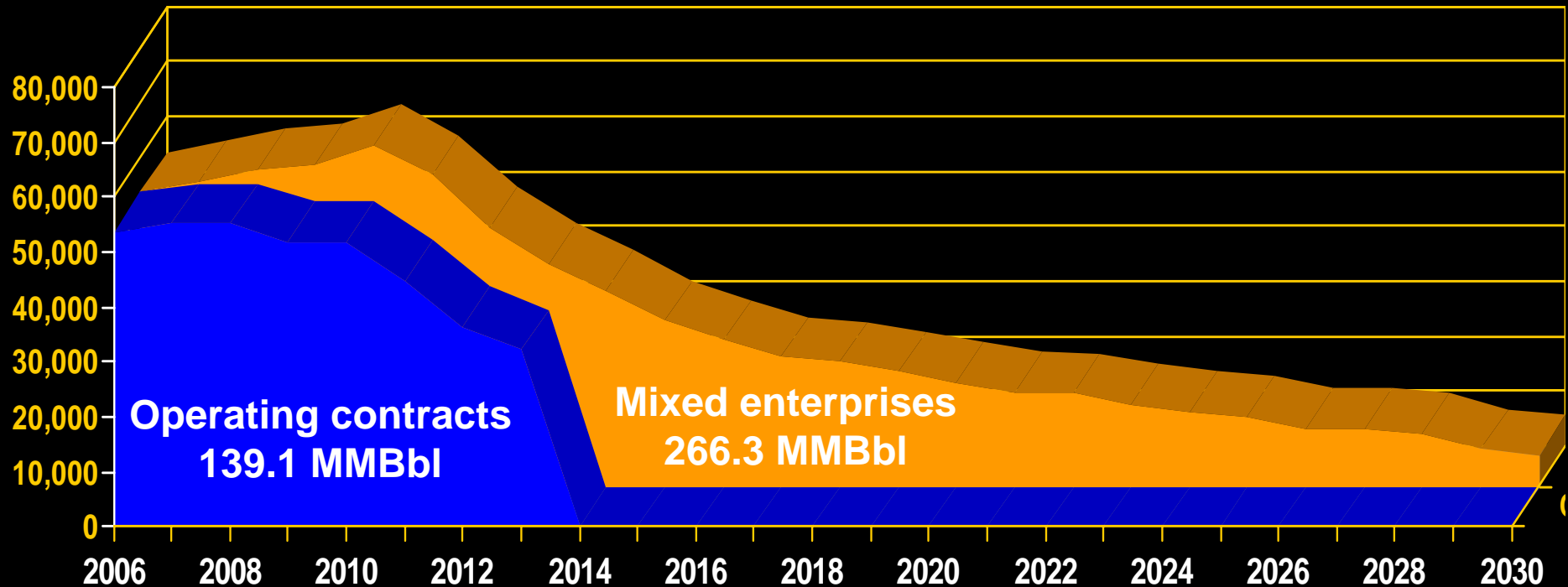
VENEZUELA. BEHAVIOUR OF ROYALTY RECEIPTS, 2000-2006



- Petroleum production highly inelastic with respect to changes in gross income levies. Gross income levies are non-contingent, take precedence over any other payment and are accountant- and fool-proof.
- Royalties do affect recovery negatively, but survive in Texas. Why should they disappear elsewhere? Profitability also has a negative effect on ultimate recovery.

FULL OIL SOVEREIGNTY: A PROSPECTIVE POLICY

COMPARISON OF OIL PRODUCTION PROFILES, 2006-2030



- Migration was not a unilateral imposition. Terms were intensely negotiated and companies were given a future beyond the expiration agreements that were, in any case, legally dubious. In this sense, a repeat of the experience of 1943.
- 30 out of 32 contractors accepted migration.

CONCLUSIONS

- **Full oil sovereignty is not incompatible with the presence of private, foreign, capital. Indeed, in the wake of the oil sabotage of 2002-3, private capital has much to offer to Venezuela.**
- **Venezuela wants to welcome foreign capital, but not at any price. Investors will have to respect Venezuela's sovereign rights over its oil resources.**
- **Investors will continue to be free to optimise their tax payments in any way they want, outside of Venezuela, that is.**
- **Gross income levies are not going to go away again, so investors better get used to them.**
- **The government expects that its recognition of the legitimate aspiration to a reasonable profit by private capital will be corresponded by the latter recognising without any reservations the legitimacy of Venezuela's aspiration for a fair and just remuneration for a depletable and non-renewable natural resource**
- **After all, the legitimate claims of investors for a return on capital also have a negative effect on ultimate recovery. So why always royalty holidays, and never profit holidays?**

CONCLUSIONS FOR COMPANIES: HOW DO WE GET MORE ACCESS?

- Tzu-kung said, 'If you had a piece of beautiful jade here, would you put it away safely in a box, or would you try to sell it for a good price?' The Master said, 'Of course I would sell it. Of course I would sell it. **All I am waiting for is the right offer.**'

Confucius, *Analects*, Book IX, 13.