

Dominican Republic Macro View

The Petrocaribe Connection

- In this Macro View we focus on the amount of financing that the Dominican Republic is getting through Petrocaribe. This could help us gauge how important the Venezuela election is for the Dominican Republic.
- According to our estimations, the Dominican Republic has been purchasing between 13 and 15 million oil barrels per year from Venezuela. In addition, it has been able to get financing through Petrocaribe for around 40-50% of this oil bill.
- If financing from Petrocaribe were to change—namely decrease—we would expect the Dominican Republic to be more active in global markets. In a world in which oil prices hover around US\$90/bbl, the Dominican Republic could lose cheap financing for around US\$500 million in new loans. In a US\$100/bbl world, this amount could reach US\$700 million.
- We would expect Petrocaribe to temporarily displace the IMF as the main topic in Dominican Republic. Since we do not expect much news about the IMF in the following days, we think that Petrocaribe should be the focus in the country—at least on the eve and aftermath of the Venezuela election.

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The Petrocaribe Connection

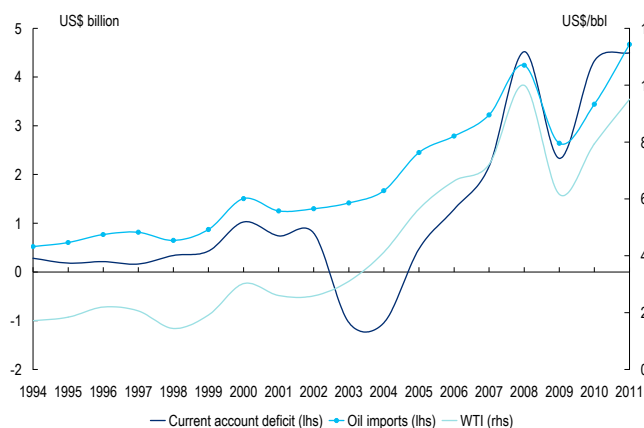
Do not forget about Petrocaribe this Sunday

The elections in Venezuela may have implications on Petrocaribe and, consequently, on the Dominican Republic. As we get closer to the October 7 presidential election in Venezuela, we sense that the investor community is beginning to question what may change in Petrocaribe under different political scenarios. Several countries in the Caribbean and Central America have benefitted from Petrocaribe, not only because they have been able to purchase oil with cheap financing at below-market-rates, but also because this financing provides relief to the capital account. In this piece we refrain from going through all the polls and scenario probabilities of the upcoming election in Venezuela. We prefer to focus on the amount of financing that the Dominican Republic is currently getting from Petrocaribe. This could help us gauge how important the Venezuela election is for the Dominican Republic.

Oil prices are a major driver of the current account in the Dominican Republic.

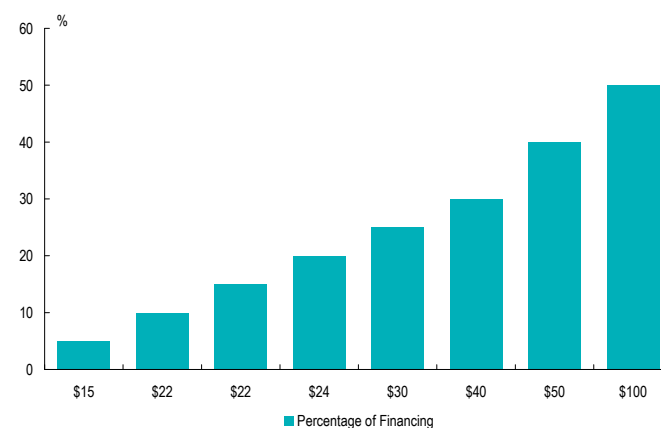
As a net commodity and oil importer, the Dominican Republic has witnessed significant swings in its balance of payments whenever oil prices increase or fall abruptly. Figure 1 shows how closely related are the current account and oil imports in the country. With the exception of the 2003-04 crisis, the swings in the current account are closely related to those of oil prices. In our view, the actual and expected shifts in the current account are a major input for the government to decide how much money it has to raise overseas. In the following years, we would expect mining exports to also become a major input in this decision; but for the time being, oil should continue explaining most of the volatility in the current account.

Figure 1. Dominican Republic: Oil and the current account



Source: BCRD, Haver and Citi Research

Figure 2. Petrocaribe: Higher oil prices translate into higher financing



Source: Petrocaribe, PDVSA and Citi Research

Petrocaribe financing becomes more important when oil prices increase. For example, if oil prices are above US\$40/bbl but below US\$50/bbl, Petrocaribe finances 30% of the oil bill that the Dominican Republic (or any other member country) purchases from Venezuela (see Figure 2). If prices hit US\$50/bbl, the percentage goes to 40%, and it jumps to 50% when oil prices are US\$100/bbl or higher (see Figure 2). Loans through Petrocaribe usually have a grace period of 1-2 years. According to the Ministry of Finance (Hacienda),¹ the average interest rate that the Dominican Republic is paying for these loans has been 1-1.1% during the past 3 years.

¹ According to the Quarterly Report to Congress published by Hacienda.

Some numbers to remember on October 7

We estimate the financing that the Dominican Republic is getting from Petrocaribe. In the Dominican Republic, Hacienda publishes the amount outstanding of Petrocaribe debt, but does not fully disclose all the transactions associated with Petrocaribe (new funding and amortizations). The debt outstanding with Petrocaribe stood at US\$2.8 billion as of June 2012, up from the US\$2.4 billion outstanding as of December 2011. To estimate the yearly gross financing that the country gets from Petrocaribe, we assume that all imports coming from Venezuela are oil related. We also use the PDVSA Crude Oil Basket price to estimate the number of barrels that are imported from Venezuela. Finally, we use the financing rules from Figure 2 to get the estimated amount financed through Petrocaribe.

Figure 3. Dominican Republic: Estimations on Petrocaribe financing

	2009	2010	2011
Total imports from Venezuela (US\$ million)	877	1,046	1,328
PDVSA Crude Oil Basket price (year average, US\$/bbl)	56.5	71.6	100.8
Estimated number of oil barrels imported from Venezuela (million bbl)	15.5	14.6	13.2
Estimated amount financed through Petrocaribe (US\$ million)	351	418	664
Debt outstanding with Petrocaribe (US\$ million)	1,476	1,852	2,439

Source: IMF (Direction of Trade Statistics), Bloomberg, Hacienda, and Citi Research

If financing from Petrocaribe were to change—namely decrease—we would expect the Dominican Republic to be more active in global markets. According to our estimations, the Dominican Republic has been purchasing between 13 and 15 million oil barrels per year from Venezuela. In addition, it has been able to get financing through Petrocaribe for around 40-50% of this oil bill. This means that in a world in which oil prices hover around US\$90/bbl, the Dominican Republic could lose cheap financing for around US\$500 million in new loans. In a US\$100/bbl world, this amount could reach US\$700 million. Of course, there could be some multilateral funding lending a hand, so that not everything has to be financed through market issuance. But even that multilateral financing would not be as cheap as that from Petrocaribe.

We would expect Petrocaribe to temporarily displace the IMF as the main topic in Dominican Republic. Since September, fiscal accounts and the potential agreement with the IMF had been on the spotlight in the Dominican Republic. Since we do not expect much news about the IMF in the following days, we think that Petrocaribe should be the focus in the country—at least on the eve and aftermath of the Venezuela election.

Appendix A-1

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