If Latin America is to catch up with the world’s leaders in energy transition, it needs investment. And that means Latin America needs regulation that works. As IPD’s John Padilla stated at the Madrid Energy Conference, strong regulatory frameworks are key to attracting long-term investment. Three quarters of total energy sector investment originates from the private sector. Stability and predictability are key.

Panelists at the Madrid conference agreed, Latin America generally displays a willingness to embrace affordable renewables-based solutions. The people themselves support that kind of switch. Juan Verde, former U.S. Deputy Assistant Secretary of Commerce for Europe, cited data from a Power Environmental Energy Research Institute study that shows 77% of Latin Americans are acutely aware of the risks posed by the climate emergency. And they are voting
According to a recent HaaS market study in the region, 95% of consumers would choose a green product over a similar non-green product. They also note that regulatory bodies could take a more active leadership role in facilitating access to investment. Thiago Barral Ferreira, CEO of Empresa de Perquisa Energetica (EPE), a research and planning entity with Brazil’s Ministry of Mines and Energy remarked, “Regulation should open the space for innovation that is not competitive today.”

But in Latin America, regulation and politics go hand-in-hand. There are few truly independent regulatory bodies, and that dynamic can create instability. Francisco Xavier Salazar Diez de Sollano, who previously served as Chairman of Mexico’s Energy Regulatory Commission (CRE) cited the story of that country, “[Mexico] used to think we had the best regulation in the region. [The regulatory body] was enshrined at the constitutional level. You can have a perfect system, but if the political will changes, a lower credit rating can be more powerful than a legal challenge.” Jose Vicente Zapata, a partner at the Colombian office of law firm Holland & Knight, noted that the key reason for heightened regulatory risk in Latin America is political pressure. Politicians are aware that a discourse encouraging sustainability sells in Latin America. But renewable energy potential is often oversold because fundamental issues with connectivity have yet to be addressed. As Diez Sollano explained, “The problem in Mexico was the overselling of the energy reform: voters were told prices would be cheaper. But that is not the same as prices being competitive. Because, in reality, energy prices are relative to the rest of the world.” When promises are not kept, the hum of latent political pressure grows louder. And political pressure brings regulatory uncertainty.

This problem pervades the implementation of environmental rules, where courts often decide which requirements apply, and when. Zapata described how the lack of clarity over the rules of the game and the power of the courts often makes low-paid public officials susceptible to corruption. Large energy contracts may try to circumvent these problems by including international arbitration as a venue for resolving disputes. But international laws are constantly
evolving. Thus, the option fails to bring stability. Low regulatory risk requires trust that the rules will be followed as written. Zapata also explained that, in Latin America, there is a generalized perception that the rules are merely a suggestion. Regulatory risk also emerges when there are inconsistencies between similar projects.

But there are bright spots. Argentina’s electricity sector has made advancements toward autonomy that works. The sector constitutes the third largest power market in Latin America, and has survived over ten economic crises. The secret, according to Andres Chambouleyron, Chairman of the National Electricity Regulator of Argentina, is that the nation’s energy sector is structured like a mini state within the country. The market operator, CAMMESA, tracks all the operations in real time. It wields executive power. The regulator, ENRE, wields credible judicial power, including the ability to set limits and impose fines. Finally, the Secretary of Energy wields effective legislative power. Argentina still has plenty of work to do. The sector is still underperforming, and tariffs are a huge fight. But, as Chambouleyron emphasized, the institutions must continue to be shielded from polarization. As Diez de Sollano asserted, “[Mexico’s] energy policy can only be solved by allowing the regulator leadership autonomy and greater stability.”

It takes policies that foster efficiency, encourage innovation, invest in digitalization, and drive environmental and financial education to attract investment in decarbonization initiatives. It takes political will to make those policies.

How can governments demonstrate and encourage that will? This is where national oil companies (NOCs) come into play. Regulation aside, governments can influence energy policy by investing in renewable energies through their NOCs. These companies are generally integrated firms that operate across the value chain. Rafael Santamaria, a former commercial lead for Colombian NOC Ecopetrol, spoke at the Madrid conference about the company’s role in Colombia. He explained that, as a national oil company, Ecopetrol does not make policy, but is a tool the government can use to influence the local market. For example, Ecopetrol is Colombia’s largest employer.
The Colombian government plans to reduce carbon emissions by 30% by 2033. Ecopetrol has mirrored this approach by integrating renewable technologies and actively seeking to improve its operating efficiency. In Argentina, state energy firm YPF has embraced the challenge of the energy transition and created a strategy that relies upon the UN Sustainable Development Goals and Global Compact. Specifically, the company is developing actions to reduce the total intensity of carbon emissions associated with operations, including technological developments focused on carbon capture, but also enhancing efficiency across the value chain to improve water management and the company’s overall sustainability.

Throughout Latin America, governments have responded to broad positive environmental support, and have yielded to the political incentives associated with investing in renewable energy to improve the public perception of NOCs. Colombia’s Ecopetrol just won an environmental award. Fiscal incentives also bring NOCs on board. Beyond political motivation, these kinds of incentives motivate Ecopetrol to increase its share of renewable investments.

Not all NOC investments in renewables end well. Joe Amador, Managing Director for the investment banking firm, Tudor, Pickering, Holt & Co. pointed out that some NOCs have dipped their toe in renewables, only to realize that they need a different skill set from their core business.

Regulation, politics, and NOCs are a tightly bound trifecta that will impact Latin America’s upward mobility in the renewables sector for the foreseeable future. The region’s highly fragmented, shifting political landscape will drive near-term policy evolution, as this year’s elections mark the beginnings of a new political supercycle. These new leaders will have to negotiate to advance their policy agenda, and that will create tensions amid discontent with institutions and political parties. Looking at the landscape, Verde quoted former U.S. President Obama, saying, “When you are in power, you don’t do what you want, you do what the opposition allows you to do.”

The Madrid Energy Conference is an annual event hosted by IPD and the Institute of the Americas. Click here to sign up for notifications, information, and an invitation to the 2020 conference.