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Contribution: Eyes on SACE Campaign, Italy

Project: Camisea Gas Field and Pipeline Project

Total cost: US\$2.8b over the life of the project
US\$408m for initial investment in Upstream segment
US\$720m for initial investment in Downstream segment

Sponsor: Government of Peru

EPC: Upstream: Pluspetrol (Argentina), Hunt Oil (US), and SK Corporation (S Korea)
Downstream: Techint, Hunt Oil, SK Corporation, Sonatrach (Algiers), Grana y Montero SA (Peru)

Location: Block 88A and 88B, Department of Cusco; pipelines to Lima, Peru and Callao

Ownership: 40-year concession

Financing: Project finance. Public financiers to provide up to 40% of the financing. Financial advisor Citigroup is helping to arrange US\$1.6b in initial financing.

Construction dates: Upstream to come online by 2003, pipeline scheduled to be completed by December 2003

The Camisea natural gas project involves the development of a gas field located in the remote Peruvian Amazon which contains an estimated 11 trillion cubic feet of gas and 600 million barrels of condensate. The project consists of extracting natural gas from Blocks 88A and 88B and transporting it to Lima and Callao, the capital city and main seaport, through two pipelines, one for dry gas and one for liquids. The upstream segment of the project includes the development of wells and transportation infrastructure to deliver gas to a processing and distribution facility. The midstream segment includes the construction of a plant to separate liquids and gases, a liquid fractionating plant, and the installation of re-injection equipment. The downstream segment consists of transportation and distribution pipelines that will deliver the gas to Lima and Callao.

KEY POLITICAL AND DOWNSIDE RISKS

Opposition from local and international organizations concerned about the environmental and indigenous peoples impacts of the project causes delays and political risk. The new consortium's relative lack of experience, combined with technical and impact mitigation challenges, increases the project's environmental and compliance risk.

OVERVIEW

According to the Smithsonian Institute, the Camisea project is located in one of the world's most biologically diverse regions. It is also located in territory that is legally recognized and titled as indigenous sanctuary for several nomadic isolated and uncontacted tribes. In view of its sensitive location, the Camisea project has historically experienced significant cost overruns, problematic contract negotiations and delays in the bidding process. The project has long been the object of activist opposition, with internationally - recognized human rights, conservation and indigenous peoples groups actively monitoring and/or opposing the project. Camisea has been on hold since 1998, when project sponsors Shell and Mobil withdrew from the project, after having invested over \$250 million. Shell cited cost overruns and an inability to work out a vertical integration agreement with the government in its decision to pull out of the project, although some observers believe that significant environmental and social controversy also played a discernible role. Only recently, have contracts been signed with two new consortia.

HISTORY OF OPPOSITION

Since 1997, international organizations, including the International Union for the Conservation of Nature, Rainforest Action Network, and Survival International have been monitoring the Camisea project. The project's environmental sensitivity and controversy could increase the project's cost of capital, as international organizations lobby public financiers to restrict their financing of the project. Already, export credit agencies such as the U.S. Overseas Private Investment Corporation prohibit financing to projects like Camisea that are located in pristine tropical forests.

The project has been a lightning rod for controversy because of a historical incident: in the 1980s, Shell, while conducting preliminary exploration in the region, exposed the Nahua indigenous tribe to a whooping cough and influenza epidemic that killed off an estimated 50% of the population. This historical incident has heightened the political sensitivity and risk associated with this project.

TECHNICAL AND COMPLIANCE RISKS

Camisea is located in the remote jungle east of the Andes while the main markets, Lima and Callao, are located west of the Andes. The engineering and logistical challenges associated with constructing 2 trans-mountain pipelines through dense jungle are further compounded by the region's ecological sensitivity.

Peru's Petroleum Hydrocarbon Law expressly requires contractors to comply with all environmental standards and rules, and states that failure to do so may lead to contract termination.ⁱⁱ To reduce environmental risk and damage, former consortium leader Shell had committed not to build any roads into the Camisea region, electing instead to transfer its equipment and materials via helicopter and transport barges. Given the standards of environmental and protection set by the previous consortium, the new consortium faces the daunting task of having to meet and perhaps surpass those standards.

POLITICAL INSTABILITY COULD INCREASE COST OF CAPITAL

As a result of the recent election scandal, Standard & Poor's forecasts that foreign investment in Peru will be depressed, financing costs will remain high, economic reforms will stall, and the economy should slow to 3% growth next year. President Alberto Fujimori's election scandal, and his subsequent resignation and exile, has sparked fears that privatizations could be derailed as investment tapers off. Peru's risk rating has deteriorated in recent months, posing additional financing challenges to companies bidding for Camisea. Such political instability could increase the cost of capital for a project that has already been plagued by significant delays.

NEW COMPANIES' RISK MANAGEMENT QUESTIONED

When Shell withdrew from the Camisea project, the government divided Camisea into upstream and downstream segments, and re-tendered the bids. After lengthy delays, it awarded the concessions to two sole bidders, two separate consortia consisting of relatively small and inexperienced companies.

The relative small size and lack of experience of the two new consortia suggests that they may not be able to finance the investments needed for this project, nor have access to the same level of technology as the former sponsors. Several analysts have also questioned whether the new consortia will be able to manage the non-commercial project risks as effectively.

WEAK GAS MARKETS INCREASE OFFTAKE RISKS

Commercial risk for this project runs high because of the underdeveloped natural gas markets in Peru. Electroperu is currently negotiating take-or-pay contracts with electricity generating

company Endesa of Spain, but has yet to line up a firm buyer for gas output, initially estimated at 200,000 Mcf/d. Additional take-or-pay contracts with other industrial consumers are also in the works, but remain uncertain.

October Update

Citibank Says Financing Package Ready by 2002

Citibank, who holds the mandate to arrange financing for both portions of the Camisea project, said in early October that a financing package will be put in place by 2002 at the earliest, much of it from export credit agencies according to a report in Project Finance International.

Public Consultation Efforts Fail to Quell Controversy

At a 17 September 2001 public hearing for the controversial Camisea project, indigenous organizations created uproar over the release of an Environmental Impact Study for the upstream portion of the Camisea gas field. While environmental review processes can provide key opportunities for companies to mitigate risks associated with controversial projects, Pluspetrol failed to release its full environmental report, and requested that community members submit comments on a 90-page summary of the study within five days.

The short timeline and lack of full disclosure prompted outrage from indigenous leaders, who also sharply criticized Pluspetrol for limiting debate at the public hearing by requiring pre-submitted written questions and hosting the meetings far from the homes of affected communities. Machiguenga and Yine indigenous organizations are calling on the Peruvian government to extend the public comment period, and for another Public Hearing. Local authorities in the Camisea region are echoing that call and claim that Pluspetrol is failing to communicate or coordinate with them on any aspect of its operations.

Pipeline Route Causes Alarm for Conservationists

CEDIA, a Peruvian organization involved a World Bank-funded conservation program in Vilcabamba, an area that will be impacted by the project, is calling for 4.5 kilometer rerouting of the pipeline. As currently planned, the route will traverse the remote biodiverse Vilcabamba range which includes two communal reserves and a proposed national park. The range is situated to the west of the Camisea gas field in the Andes Mountain chain in south-eastern Peru, and 1.7 million hectares of this region was designated as a protected area by the Peruvian government in 1988. Fearing that the pipeline will open access into the pristine region, CEDIA has called for the pipeline to be rerouted around the proposed Communal Reserve of Vilcabamba Pavlik Nikitine.

Several international conservation groups, including Conservation International and the International Union for the Conservation of Nature, have projects in the area or have recognized the region for its biodiversity value. Three public hearings for the pipeline are scheduled in Timpia (community near the Camisea project), Cuzco, and Lima for the end of October 2001, where conservation groups will likely express their concerns over the pipeline's current route.

Camisea Pursues Aggressive Schedule, Hopes to Allay Indigenous Fears

The new Minister of Energy and Mines, Jaime Quijandria announced that the Camisea pipeline project could be in service as early as December 2003, about half a year earlier than originally planned. The consortium could begin transporting construction equipment by river into the jungle as early as November 2001, while Pluspetrol forecasts that drilling on the first well could begin as early as March 2002.

Pluspetrol hopes that by starting equipment transport rainy season, drilling equipment can be barged to the Malvinas area, where it will be taken by helicopter to the drill site. The consortium

claims that the river and air transportation will ease the concerns of indigenous groups in the jungle about more roads being built in their territory.

Electro-Peru and Endesa Obligated to Purchase Camisea Natural Gas

The ex-Energy Minister Jorge Chamot's decision to obligate Electro-Peru to purchase 70 million cubic feet of natural gas in order to secure a buyer for the Camisea consortium continues to generate controversy.

Some industry experts maintain that the take-or-pay contract is excessive. Electro-Peru signed a contract with Camisea consortium six months ago, but does not have a generating plant and is unable to use the gas. Government and Camisea consortium officials hope that Electro-Peru and the Spanish company Endesa, through its energy generating subsidiary Etevensa, will work out a temporary agreement for the use of this natural gas while details of the Camisea sale are settled. (El Comercio of Peru, June 26, 2001)

December 2001 Update

Ex-Im Bank Guarantees Loan to Pluspetrol Peru

The US Ex-Im Bank approved a guarantee for Chase Manhattan Bank on a US\$25 million, five-year loan to Pluspetrol Peru Corp SA for equipment for gas exploration activities in Camisea. Citibank continues to hold the overall project mandate for the US\$1.2bn Camisea upstream and downstream project.

In response to this financing, prominent indigenous and environmental groups from Peru and the US sent a letter to ExIm in December urging the agency to suspend the loan on the grounds that this project violates ExIm's environmental assessment policy.

Drilling Slated for April

Pluspetrol recently signed Houston-based Parker Drilling Co to drill four wells in the giant gas field. Parker's Rig 228 will leave Houston for Iquitos, Peru, in early December, while drilling commencement is slated for April.

Downstream Public Hearings Temporarily Postponed

Outcry about the date of the downstream EIA public hearings obliged the distribution company Transportadora de Gas del Perú (TGP) to temporarily postpone the first hearing on the gas pipeline held in Camisea. Local indigenous communities and their supporters had protested that TGP knew the hearing coincided with their indigenous Congress, held the hearing on October 23. The date of the hearing was changed to November 2.

Indigenous Congress Calls for More Time to Review the EIA.

In late October, participants in the Annual Congress of indigenous peoples of the Upper and Lower Urubamba (COMARU) identified numerous potentially serious project impacts on their lives and lands. COMARU represents 26 indigenous communities inhabiting the upper and lower Urubamba, the majority of whom belong to the Matsigenka (Machiguenga) people. A series of demands was formulated - communities wish to mark off no-go areas to prevent company workers invading their villages, and want the right to approve the delineation of pipeline routes.

At the Congress, representatives of the Ministry of Energy and Mines and TGP both argued that the project is in the best interest of Peru.

Following the congress, the Machiguenga Congress asked the Minister of Energy and Mines to order a new process of public consultation for both upstream and downstream EIAs. The Congress called for a 90 day period to assess the documents from the date of receipt of copies of

the full EIA. They also asked the Minister to hold workshops in local communities to inform people about the potential impacts of the project.

Gov't Approves Upstream EIA on Dec 17

On Nov 28, the Peruvian government agreed to give indigenous communities 90 days to review the upstream EIA but back dated the request to September 21st and giving communities until December 21 to submit their observations. The indigenous group COMARU as well as international support groups rejected this extension as inadequate. Even still, the Peruvian ministry of energy and mines approved the UPSTREAM EIA on December 17, 2001 ---ahead of the deadline the ministry had granted COMARU and giving Pluspetrol the green light to begin the project. This early approval of the license has angered local and national organizations given that COMARU had not been given a full copy of the EIA for Plus Petrol until November 17.

The Downstream EIA is not yet approved but it likely to occur within 90 days from the November 2 public hearings. Indigenous organizations continue to assert that the Ministry should postpone approval until March 14, 90 days after they received a full copy of the EIA.

Upstream and Downstream EIAs not Made Available to Local Communities in a Timely Manner

Although Pluspetrol and TGP representatives were present at the COMARU Congress, the two consortia COMARU reports that the companies failed to provide the organization with a full copy of the EIA documents for both Upstream and downstream projects in a timely manner and thus prevented the organization from adequate consultation process. The According to the letters of receipt from the Companies, the Pluspetrol EIA was delivered to COMARU on November 17 while the TGP EIA was given to the organization on December 14 after repeated requests from the organization.

Local organizations have asked for independent technical assistance in assessing the EIA and preparing an effective response. In response, a consortium of NGOs and technical experts formed in late December to analyze both the Upstream and Downstream EIAs and to offer their findings to COMARU at community workshops in February. They want to independent study of the project EIA to be commissioned and copies of the findings provided to them. Ironically, Pluspetrol responded to this demand by offering to pay lawyers to work with local communities. Servindi, October 26, 2001

Camisea Draws French Interest

French companies are currently looking to Peru with interest, announced Paul Bernard, head of the French Companies Movement (Medef), which visited Peru in early November. The Camisea project is attracting attention and French companies are looking to move in on blocks adjacent to Camisea to exploit potential gas reserves.

Meetings with President Toledo, government ministers and corporate leaders led Bernard to comment that the present climate is well disposed to foreign investment. He stated, "we see great business opportunities on offer in Peru."