



Brazilian oil sector reforms: The role of technical know-how and corporate *ethos* in Petrobras's dominance

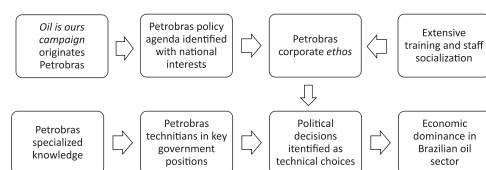
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GRAPHICAL ABSTRACT



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ABSTRACT

The literature shows that Petrobras's specialized knowledge in deep-water exploration helped it maintain its dominance of the oil sector in Brazil. This article contributes to the literature by throwing light on how this process operates: as technicians of the State enterprise monopolize the knowledge, they are called on to participate in key policy decisions for the sector, and thus exert an influence that is not counter-balanced by other experts. Also, as these technicians' *ethos* identifies Petrobras's policy agenda with national interests, their participation in oil policymaking reinforces the enterprise's dominance in the sector.

This case study contributes to energy policy studies by bringing to the discussion questions addressed here on the institutionalist approach, relating particularly to bureaucratic agents' behavior and their influence as technical specialists on processes of change. It also addresses the problem of unexpected results of institutional reforms, in view of the challenges faced by governments that seek to alter regulatory frameworks. In other words, the study of a specific case of a government agency through institutional theory seeks to answer exhortations from scholars that indicate the necessity of applying institutionalist approach in the analysis of governance structures.

1. Introduction

It is widely acknowledged that in 1997, during the Cardoso government, the legal rules that for years had governed the oil sector in Brazil were significantly modified, ending the constitutionally-guaranteed monopoly of Brazil's state oil company, Petrobras. New rules were also created to open up the sector to competition from private Brazilian and foreign companies. The new regulatory framework has been in place for almost twenty years and, despite important changes in the

sector in Brazil, Petrobras's economic dominance has remained strong.

The literature shows that Petrobras's accumulated technical knowledge was essential to maintaining its dominance in the sector in Brazil (Felipe, 2010; Alveal, 1994; Paz, 2014; Antolin and Cendrero, 2013; Paz, 2013). While not contesting this argument, this article aims to explain how this functions, by showing that this accumulated technical knowledge guaranteed not only the company's dominance in the sector, but also determined the presence of Petrobras technicians in the industry's decision-making arenas, where they had an influence not

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counter-balanced by other policymakers.² As a result, Petrobras's political agenda was established as a technical base for policymaking, allowing its economic dominance of the sector to continue. This disabled one of the key components of the 1997 liberal reform, which had ended Petrobras's economic monopoly of the oil sector.

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The text is organized as follows: introduction is followed by a section explaining the theoretical frame of reference and analytical methodology. The process is then analyzed, the implications discussed and some conclusions indicated.

2. Theoretical references and analytical process

This study employed New Institutional Theory, specially its Historical and Sociological strands, which emphasizes the importance of institutions, understood as historically-constructed, formal and informal rules that form the structure of interpersonal relationship patterns. They also condition the actions of social and political players, and public policy results. Institutions are considered not to operate deterministically, but as filters that allow certain patterns of social behavior to be selected over others. As a result, they generate certain policy results.

There are two ramifications to historical institutionalism, which differ greatly in their analytical approach. The first, and more established of the two, rests on how institutions share power unequally among players. It emphasizes that institutional structures continue until exogenous shocks engender critical situations with consequent changes in existing paths. This first ramification is characterized by disruptive and non-incremental changes (Hall and Taylor, 1996; Immergut, 1998; Pierson, 2004), which are very enlightening when longer periods are considered, because this approach highlights not only those critical situations that lead to path changes, but also path-dependence mechanisms. This situation occurs when the chosen institutional path ends up determining subsequent choices; the process is then difficult to reverse completely because the longer it is in place, the greater the returns the model introduces.

The second strand of historical institutionalism, which has developed significantly, emphasizes endogenous and incremental changes and presents a typology based on the ways in which gradual changes – involving displacement, layering, conversion and drift – affect

institutions. Change by displacement occurs when older institutional rules are replaced by newer ones; layering involves the introduction of new institutional rules without removing the old ones; conversion means changing the action of existing rules by way of strategic redirection; and drift occurs when old rules that have become obsolete are ignored because of changes in the environment surrounding the institution (Thelen, 1999, 2003). In this line of theory, institutional changes are connected with ambiguity in the rules and how these allow different types of player to influence the rules' use, and thus to redirect institutions to satisfy their interests with regard to power distribution (Mahoney and Thelen, 2010).

The sociological approach, on the other hand, is also very important to understanding the role played by Petrobras in the institutional change process. Since social actions are not determined by individual choices resting on ahistorically given preferences, the analytical approach of sociological institutionalism centers on how historically-constructed institutions mold individual behavior patterns and practices that are reiterated in organizations without requiring repeated collective mobilization or authoritarian intervention. In addition to preventing certain types of behavior, such patterns of regularity either define opportunities and facilitate ways of interaction or structure rules that constitute, at one and the same time, the players' identities and interests. In other words, by constituting guides for practical action and positions assumed without question, institutions can be the model of how to do things, and last as long as these patterns are repeated and change is unimaginable. The result is that normative and cognitive variables overlap: "moral become factual" (Clemens and Cook, 1999). In the present study, what we will see is the conception that the interests of Petrobras coincide with the interests of the country, which becomes a guide for the formulation of public policy of the sector.

In this regard, the specific contribution of the article is the analysis of the maintenance of Petrobras' dominance in the oil sector in Brazil through the lens of the institutional theory. In this sense, it is interesting to remember that Francis Fukuyama, in an article that motivated important analytical inflections in the area, stated that studies on public governance should consider the state is not monolithic and therefore it is necessary to think of governance not in terms of country, but rather in terms of different government agencies within each country (Fukuyama, 2013).

In addition, in the 30-year celebratory edition of Governance magazine, in reviewing the field of Structure of Govern, Guy Peters and Jon Pierre point out the need to apply the theoretical advances of the institutional literature to the issues of State Reform (Peters and Pierre, 2017):

One rather obvious example of the divergence between theoretical development and empirical analysis is in the relative lack of use of institutional theory by public administration. Despite the significant developments in this field, and the public bureaucracy being a major institution in the public sector, and operating in a field composed of other institutions, very little has been done to use this large body of theory to address the structure and performance of the bureaucracy.

Thus, this article applies the approach of historical and sociological institutional theory to understand the governance structure of a specific state agency, which would be an empirical contribution to the advancement of energy policy and governance literature.

The within-case study allows detailed and holistic evaluation to delineate the way causal mechanisms operate in specific contexts, as it enables rare events explanation and assist in the discovery of unobvious variables (George and Bennett, 2005). As well, they are attuned to research objectives that formulate hypotheses, in which internal validity is tested, and where understanding of the causal mechanism is needed in order to deepen the proposal's scope (Gerring, 2007). Finally, the within-case study differs from the cross-case because it is more rigorous, which allows in-depth causal mechanisms to be investigated, while overcoming other methods limitations, in order to provide a

² Since finishing our empirical research in 2014, Petrobras suffered several inter-related impacts. First, corruption scandals involving the company directors, that were political appointees, the state-owned company suppliers, and political campaigns financing. Second, Petrobras suffered a financial crisis, derived from: a) the impacts of the corruption scandal on the company share price; b) the dramatic international oil price drop; and c) the artificially low fuel price maintenance due to governmental intervention. Third, this financial crisis affected Petrobras scheduled investments, hence impacting the whole oil sector suppliers network, and in a cascade effect, deepened the country recession cycle. Finally, with the new government after President Dilma Rousseff impeachment, Petrobras gets a new political direction, along with changes on the 2010 oil regulation. Regarding this last point, Petrobras no longer is the only Pre-Salt fields operator, and the company is no longer obliged to participate in every Pre-Salt exploration (previously, the minimum compulsory share was 30%). All these elements are pivotal to understand the sector future development in Brazil, and should be the object of new research. Despite their reach and importance, they do not alter the focus of our study and the argument we have supported here, which refers to a recurrent behavior pattern, which characterizes the bureaucracy of the state-owned company. However, these developments have to be monitored in order to evaluate eventual impacts on the company *ethos*.

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