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By Carlos Navarro

The state-run oil company PEMEX is exploring the possibility of acquiring a partial or full share of at least one refinery in the US to increase its processing capacity and boost the domestic supply of gasoline. The move would complement the government's plan to construct the *Refinería Bicentenario in Hidalgo state*. The refinery, which would have the capacity to process 250,000 barrels per day, had originally been planned to begin operations in 2015, but PEMEX has deferred construction of the facility and has given no clear explanation for the delay.

The company has had some internal conversations about acquiring refinery capacity in the US, but the proposal became public in early March when PEMEX director Juan José Suárez Coppel mentioned the possibility in an interview with Bloomberg news service. This would be an important strategic move for PEMEX, which is looking to acquire "significant" refining assets in the US, said Suárez Coppel.

Market conditions ideal

PEMEX is likely to move quickly on these transactions because of ideal market conditions, with the possibility that more than one facility would be acquired. Suárez Coppel declined to identify potential targets, but several multinational oil companies, including Chevron Corp., Murphy Oil, and BP Plc, have placed refining facilities on the US Gulf Coast on the market. The value of these facilities has fallen sharply since 2006, making acquisition a much more financially viable option than constructing a new refinery, said the research investment bank Dahlman Rose & Co.

In 1994, PEMEX considered purchasing a refinery in Louisiana operated by US multinational company Conoco, but the asking price was considered.

The PEMEX director said the decision has more to do with meeting the potential demand in Mexico rather than budget considerations. "The driver of this transaction is strategic, so our plan is to go ahead with a deal regardless of the current oil prices," Suarez Coppel said.

The acquisition would help boost PEMEX's domestic gasoline supplies at a time when demand is projected to increase by 5% annually because of an increasing number of automobiles in Mexico. Government statistics show that gasoline purchases in Mexico reached a record of almost 803,000 bpd in 2010, an increase of 20% over the average annual purchase during the past five-year period.

The *Secretaría de Energía (SENER) estimates a new refinery would have to be constructed in Mexico every three to four years for Mexico to become self-sufficient in gasoline.*

Suárez Coppel said oil refined in US facilities could increase domestic supplies by more than 50,000 bpd. "Existing subsidies of gasoline prices in Mexico will prevent demand from slowing even during slow economic growth periods," said the PEMEX director.

The volatility of Mexico's gasoline supplies was evident during the last two months of 2010, when PEMEX implemented planned-maintenance shutdowns at refineries in Hidalgo, Veracruz, and Oaxaca states. The PEMEX subsidiary Pemex Exploración y Producción said only 1.101 million bpd were processed in December, compared with the monthly average of 1.193 million bpd.

The trend was reversed in February, when the refineries came back on line after maintenance operations were completed. As a result, imports during February reached their lowest level in 13 months.

PEMEX domestic capacity limited

At present, PEMEX's six existing refineries have capacity to process 1.54 million bpd but are not operating at full capacity because they have not been upgraded to process heavy crude. The *Refinería Bicentenario would have the capability of processing primarily Maya grades, a blend of heavy crude oils found in the Gulf of Mexico.* the Houston, Texas, suburb of Deer Park, owned jointly with Royal Dutch Shell Plc. The plant is capable of processing 340,000 bpd. Under the operating agreement with Shell, PEMEX supplies the refinery with crude oil and acquires 50% of the processed product.

The proposal to purchase refining capacity in the US is strongly supported by key members of the company's advisory board. "I am very much in agreement with the proposal to make a move based on favorable market conditions for refineries," said attorney and advisory board member José *Fortunato Álvarez* Martínez.

Fluvio Ruiz Alarcón, an energy specialist nominated to the advisory board by the center-left *Partido de la Revolución Democrática* (PRD), said PEMEX should not only look at the proposal as a means of expanding capacity but also as a way to acquire much-needed expertise from other parties. "The idea is not only to boost capacity for the Mexican market but also to link this plan to the acquisition of technological capacity," said Ruiz, who holds a master's degree in energy from Grenoble University in France.

The proposal was also endorsed by David Shields, a respected energy expert based in Mexico City, who said the acquisition of a refinery in the US "makes economic and technical sense" for PEMEX.

But Shields suggested in an interview that political considerations might derail the plan. "I don't think the president of Mexico will spend money in the US instead of Mexico a year before the Mexican elections," said Shields, publisher of the magazine *Energía a Debate.*

What about the Refinería Bicentenario?

If Calderón decides to heed his political advisors and invest in Mexico, the natural option would be to devote capital to the Refinería Bicentenario. And yet, there is no evidence that this is going to happen during the rest of the president's term in office. In fact, the administration is going the opposite direction, falling behind on its promised timetables to complete the facility. This situation has not escaped the attention of political pundits and opposition politicians, particularly officials in Hidalgo state. "[The administration] has been making plans for a refinery in Tula, Hidalgo, for two years," said syndicated columnist Sergio Sarmiento.

PEMEX has acknowledged that very little work is planned on the refinery this year but offered no explanation. The oil company's only planned construction expenditure on the facility in 2011 is a fence that will mark the boundaries of the refinery site.

The delays angered former Gov. Miguel Ángel Osorio Chong and his successor Francisco Olvera Ruiz, both members of the opposition Partido Revolucionario Institucional (PRI). Osorio noted that PEMEX had promised that construction would begin in 2010, but work on the project had not begun as of March 2011.

"Hidalgo made a great effort to meet its obligations to the project, even assuming a debt of 1.5 billion pesos (US$127 million)," Osorio Chong said in his last state address before leaving office on March 31. "We gave PEMEX all the documents and the necessary decrees to donate more than 700 hectares for the facility."

Without providing a timetable for the project, administration officials offered reassurances that the Calderón government remains committed to it. In a meeting with Osorio just two days before his departure from the state house, Energy Secretary José Antonio Meade Kuribreña and Suárez Coppel reiterated that the Refinería Bicentenario is a key element of Mexico's long-term plan to ensure an adequate supply of fuel in Mexico.

The two officials said that, even though erecting the boundary fence was the only direct construction work planned on the facility this year, PEMEX is conducting other preparatory work for the site that will ensure the environmental safety of the area. Pemex Refinación is also working on a plan with the state electric utility company *Comisión Federal de Electricidad (CFE)* to relocate high-tension lines that currently cross the site, they said.

Still, mistrust of PEMEX and the Calderón government was evident in Olvera Ruiz's inauguration speech on April 1. The new governor promised that his administration would hold the oil company to its commitment to construct the refinery. "The timetable and the process had already been defined," said Olvera Ruiz. "We will monitor this process very closely to ensure its completion, which will benefit not only Hidalgo but all of Mexico." [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on April 13, 2011, reported at 11.78 pesos per US$1.00]