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Fox Moves Forward with Private Gas Contracts Despite Opposition in Congress

by LADB Staff
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President Vicente Fox's administration continues to push forward its controversial program to extend exploration and development contracts to private companies to expand Mexico's natural-gas production in three northeastern states. At the end of January, the Fox administration awarded its fifth multiple-services contract (contratos de servicios multiples, CSM) to a private entity to conduct exploration activities the Burgos Basin, which spans the states of Coahuila, Nuevo Leon, and Tamaulipas.

The latest contract was awarded to Texas-based Lewis Energy Group LT to conduct exploration activities in the Olmos block, located primarily in Coahuila state. Lewis Energy submitted a bid of US$343 million. The award concludes the first stage of the Fox administration's CSM program, which aims to attract private capital to exploit natural-gas resources in the Burgos Basin.

The state-run oil company PEMEX awarded its first contract in October 2003 to a Brazilian-Mexican-Japanese consortium (see SourceMex 2003-10-29). Since then, PEMEX has awarded four other contracts, including the latest award for the Olmos block. The five CSMs represent commitments from private companies to produce 440 million cu feet a day, with investment of US$4.4 billion during the life of the multiple-service contracts.

The administration had also requested bids during the past two months for two other sections of the basin, the Ricos and the Coridon-Pandura blocks, but failed to attract sufficient interest from private bidders. The administration estimates that extraction of reserves in the Burgos Basin could increase the country's natural-gas production by about 1 billion cu feet per day and reverse the recent trend of reduced output. The goal cannot be achieved without increased exploration and development activities, which require capital expenditures that PEMEX cannot cover, administration sources say.

A PEMEX report published in early January said the country's production of natural gas declined by 6% during the five-year period between end of 1998 and end of 2003. Production in November 2003 was reported at 4.48 billion cu feet daily, compared with 4.79 billion cu feet daily at the end of 1998.

Congress continues to oppose program

The Fox government's push to use CSMs to capitalize natural-gas exploration and development activities has put the federal government on a collision course with the Mexican Congress, which considers the practice unconstitutional. Opponents include some senators from President Fox's center-right Partido Accion Nacional (PAN), who joined colleagues from the former governing Partido Revolucionario Institucional (PRI) and the center-left Partido de la Revolucion Democratica (PRD) in opposing a measure sponsored by the administration last year that would have created a framework to legalize the CSM scheme.
The measure, which proposed reforms to the public-works and acquisition laws (Leyes de Obras Publicas y Adquisiciones), contained language that would have given the administration a legal loophole to proceed with the CSMs. The initiative was first approved by the Chamber of Deputies at the end of 2002 and sent to the Senate for further review.

Based on the recommendation from the three committees dealing with domestic matters interior (Comision de Gobernacion), finance (Comision de Hacienda), and legislative studies (Comision de Estudios Legislativos), the full Senate eliminated or modified some provisions that would have legalized the CSMs and then unanimously approved the modified legislation at the end of 2003.

"We managed to halt President Fox's effort to introduce changes that were at first glance harmless, but which would have legalized the CSMs," said PRI Sen. Laura Alicia Galindo. "This would have been the first step in the privatization of PEMEX."

Members of the three committees said the bottom line was the danger that the CSMs could take important decision-making powers out of the hands of the federal government. "The contracts that govern petroleum-related activity have to keep operations in the hands of PEMEX at all times because through this company the government conducts activities reserved exclusively for the state," said the text of a summary put together by the committees.

Even though many PAN senators joined in opposing the legalization of CSMs through the public-works and acquisition reforms, legislators from the center-right party still support the concept of private investment to capitalize PEMEX. "We see an urgency to open up the gas sector, which will require 630 billion pesos (US$57.3 billion) in investments over the next decade, or about 64 billion pesos (US$5.8 billion) per year," said former PAN legislator Noe Navarrete, who once served on the energy committee (Comision de Energia) in the Chamber of Deputies.

The Senate decision has apparently not dissuaded the Fox administration from proceeding with its plan to use the multiple-services contracts again. PEMEX officials are hoping to reopen the bids for the Ricos and the Coridon-Pandura blocks, which were part of the first phase of the CSM plan.

There is also a proposal on the table to proceed with a second phase, which would place a higher priority on bringing Mexican companies into the process. "We are working very closely with the Camara Mexicana de la Industria de la Construccion (CMIC) to develop a proposal to give priority to Mexican companies," said Sergio Guaso, executive director of the CSM program at PEMEX.

At least 200 CMIC affiliates have expressed interest in participating in some form in the second phase of the CSM program. "This is an excellent opportunity for Mexican companies," said CMIC president Jorge Videragay.

**Multinational energy companies absent from bidding**

The government decision to reach out to more Mexican companies may be related to the lackluster interest from foreign participants, as evidenced by the lack of bids for the Ricos and the Coridon-Pandura blocks and the single bid presented for the Olmos block.
Most conspicuous for their absence in the bidding process have been the multinational energy companies. A handful of companies including US-based Exxon Mobil and ChevronTexaco, Britain's BP p.l.c., and France's Total Elf submitted inquiries about the CSM projects but in the end decided not to participate. "[Oil companies] look at the data and say there isn't enough money to be made," said George Baker, director of Houston-based consulting company Mexico Energy Intelligence.

Baker said the large energy companies are also skeptical about participating in the process because of the uncertain legal status of the multiple-services contracts. The opposition parties argue that the CSMs violate the Mexican Constitution and have threatened to bring the program before the country's highest court (Suprema Corte de Justicia de la Nacion, SCJN).

Other analysts cited the intense global competition for the services of the large multinational energy firms as reasons why they have stayed out of the bidding in the CSM program. "There are a lot of countries trying to attract exploration and development, and the deals are getting better," US-based energy analyst George Gaspar told the Mexico City-based English-language newspaper The Herald. "Mexico continues to undermine itself by attempting to control too much."

Still others see multinational companies playing a different role in Mexico's gas industry in the near term. A recent report published by the Economic Commission on Latin America and the Caribbean (ECLAC) said Mexico's inability to produce sufficient oil for its own needs leaves the country vulnerable to imports, which have been rising steadily during the past two years. Imports totaled 779.8 million cu feet daily as of December 2003, compared with only 325.6 million cu feet at the start of 2002. Imports averaged about 592.5 million cu feet daily in 2002. Mexico's recent imports have come primarily from the US through pipelines connecting northern states with Texas.

But the ECLAC report said multinational companies like Shell, Sempra, Marathon, Tractebel, and others could step in to supply a large share of Mexico's growing demand for imports. These companies are in a position to cover demand by Mexico and other countries because they recently constructed gas-processing plants in countries that include Nigeria, Oman, Venezuela, Russia, Australia, and Malaysia, said the ECLAC report. Another option is for Mexico to acquire gas from countries like Bolivia.

During a recent trip to Monterrey, Bolivian President Carlos Mesa said he asked Fox to resume discussions on a plan to export natural gas to Mexico. The plan was first proposed by former Bolivian President Gonzalo Sanchez de Lozada (1993-1997, 2002-2003) in October of last year (see SourceMex, 2003-10-29). The proposal was scrapped after the former Bolivian leader was forced to resign because of discontent regarding a controversial natural-gas export program (see NotiSur, 2003-10-24). The possibility of developing a scheme to export gas to Mexico remains open," Mesa told reporters. "In the next weeks, our economic development and hydrocarbons ministers will meet with officials from PEMEX and the Secretaria de Energia (SENER) to explore all our options." [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on January 28, reported at 10.98 pesos per US$1.00] (Sources: Reuters, 11/18/03; Dow Jones news service, 11/05/03, 11/12/03, 11/19/03; Agencia de noticias Proceso, 12/05/03; Los Angeles Times, 12/15/03; Notimex, 11/11/03, 01/01/04; Milenio Diario, 11/06/03, 11/10/03, 12/15/03, 01/15/04; The Herald, 11/06/03, 11/13/03, 11/19/03, 11/21/03, 01/16/04; Associated Press, 01/16/04; La Cronica de Hoy, 11/06/03,
11/12/03, 11/13/03, 11/21/03, 12/09/03, 01/15/04, 01/16/04, 01/22/04; El Sol de Mexico, 11/12/03, 11/19/03, 11/20/03, 12/12/03, 01/26/04; El Financiero, 01/26/04; La Jornada, 11/04/03, 11/07/03, 11/12/03, 11/13/03, 11/18/03, 11/19/03, 11/21/03, 12/09/03, 12/10/03, 01/27/04; El Universal, 11/12/03, 11/13/03, 11/19/03, 11/20/03, 11/25/03, 12/01/03, 12/09/03, 12/16/03, 01/15/04, 01/20/04, 01/27/04)

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