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The weak and uncertain global oil market finally forced the federal government in Mexico to take direct action to support the financially fragile state-run oil company PEMEX. In mid-April, the Finance Ministry (Secretaría de Hacienda y Crédito Público, SHCP) announced a plan to inject about US$4.2 billion to PEMEX to help improve the oil company’s liquidity and help to make this year’s pension payments. Miguel Messmacher, deputy finance secretary in charge of the revenues division, said the move represents an effort to avoid the need for PEMEX to tap credit markets.

A steady drop in global oil prices over the last two years led the Mexican government to use the derivatives market to raise funds for the oil stabilization fund, which helped the Mexican treasury cope with a sharp drop in global oil prices and at the same time provide a cushion for PEMEX (SourceMex, Nov. 19, 2014). This activity in the derivatives market, in effect, provided the Mexican economy—which continues to rely heavily on oil-export revenues—with a guaranteed price of US $49 per barrel on 212 million barrels of oil for 2016.

The move includes the direct injection of about 26.5 billion pesos (US$1.5 billion) in capital as well as a credit facility for a further 47 billion pesos (US$2.6 billion) to pay down pension costs this year. Additionally, the plan allows PEMEX to deduct more of its exploration and production costs. The move would reduce PEMEX’s tax liabilities by about US$2.9 billion in 2016.

The SHCP said the government obtained the funds for the capital injection via budget cuts announced at the beginning of this year (SourceMex, Feb. 10, 2016).

PEMEX officials said the state-run oil company would use some of the extra cash to pay back billions of dollars owed for last year to dozens of suppliers and contractors, many of which are small- and medium-sized firms fully dependent on business with the Mexican oil giant.

“This is good, because it is comprehensive and it deals with the main issues,” said Alexis Milo, an economist at Deutsche Bank in Mexico City. “The reaction of markets will be positive because this is the beginning of the structural changes that markets were expecting.”

Uncertain future for oil prices

PEMEX’s budget problems are associated with two trends. The first is the slump in the global oil market, which has affected the export price of Mexican crude oil. At the end of 2013, the Congress considered an average oil-export price of US$81 to US$85 per barrel when setting the budget for 2014 (SourceMex, Oct. 23, 2013). The value of Mexican exports eroded gradually over the next several months because of an oversupply on the global market, leading analysts to project the oil price for 2015 at an average US$53 per barrel in 2015 (SourceMex, Feb. 4, 2015). In projecting the budget for 2016, the Congress and the executive branch considered a price of US$50 per barrel (SourceMex, Sept. 16, 2015).
Given recent trends, administration sources are anticipating an oil-export price of US$35 per barrel in 2017. According to deputy finance secretary Fernando Aportela, the administration plans to continue to use the derivatives market to help ensure an adequate level of revenues for 2017. The hedge is based on PEMEX's trademark Maya heavy crude and the benchmark Brent crude, which traded at US$45.30 per barrel on May 3.

A survey of market analysts conducted by the Reuters newswire suggests that prices could remain volatile through the third quarter, although no big swings are anticipated. The analysts forecast Brent crude to average US$42.30 per barrel for 2016, but the US Energy Information Administration (EIA) has projected the price at US$34 per barrel this year and US$40 in 2017.

For PEMEX, declining production and reserves over the past 11 years has been another reason for the state-run oil company’s misfortunes (SourceMex, Oct. 26, 2005, March 7, 2007, and Sept. 24, 2008). The energy reforms proposed under ex-President Felipe Calderón (2006-2012) and enacted during the administration of President Enrique Peña Nieto are an attempt to attract private investors into Mexico’s oil sector to find new sources of reserves, particularly in the deep waters of the Gulf of Mexico (SourceMex, Feb. 22, 2012, Dec. 18, 2013, and Aug. 6, 2014).

“[PEMEX] is fighting to maintain its current levels of production, which are below the average of 2.548 million barrels per day that prevailed at the start of Enrique Peña Nieto’s government in 2012,” columnist Fausto Alzati Araiza wrote in a piece published in the daily newspaper Excélsior at the end of April. “The oil company has cut about 100 billion pesos (US$5.6 billion) from its budget this year, on top of the 62 billion pesos (US$3.5 billion) that were cut in 2015. The largest portion of the cut will be absorbed by the exploration and production subsidiary, which will reduce the extraction levels to about 2.13 million barrels per day in 2016.”

Alzati Araiza noted that PEMEX had lost its role as a monopoly following the energy reform implemented last year, adding, “However, we have yet to see the first barrels of crude produced by private companies. This will take years to become a reality.”

Injection called insufficient
Some analysts believe the SHCP injection of capital and tax measures will be insufficient to solve the dilemma facing PEMEX.

“Whoever thinks [that this rescue] is going to rehabilitate the Mexican oil company is mistaken. This is just a breath of oxygen that could give it room to maneuver the rest of the year,” Eduardo Torreblanca wrote on the Noticias MVS online site.

Some financial experts had expected the SHCP to inject a much larger amount of money into PEMEX, given that the state-run oil company owes about US$6.9 billion in overdue payments to suppliers and the firm’s total unfunded pension-liabilities amount to US$86 billion.

“This is not a long-term solution, but rather a bandage to ease PEMEX’s short-term cash problem,” energy consultant Antonio Juárez told The Wall Street Journal.

Juárez, a former official with the energy ministry (Secretaría de Energía, SENER), said the SHCP might have to take a similar action later in the year if oil global prices remain depressed.
Other analysts offered similar assessments of the situation, particularly regarding the state-run oil company’s huge labor force. “PEMEX employs 150,000 workers and supports almost 100,000 retirees,” columnist Macario Schettino wrote in the daily business newspaper El Financiero.

According to Schettino, Mexico employs more workers than anyone else in the oil sector, and many are not even involved in actual oil production or processing of oil products. PEMEX not only extracts oil from the ground, but also refines and processes the product into petrochemicals and other byproducts, such as fertilizers. On top of that, PEMEX manages medical services for its employees, as well as maritime, air and ground operations, marketing and sales campaigns, and other activities.”

“Some of these activities make sense for the oil company while others should be assumed by a third party,” Schettino wrote.

Schettino suggested that the government should consider hiring private companies to take care of even some activities that are oil related. “We lose money in refining, and not a small amount, about 100 billion pesos (US$5.6 billion) per year,” he said.

“At last, someone remembers that PEMEX is our country’s leading company and the main source of support for the federal expenditures budget (presupuesto de egresos),” columnist Carlos Fernández-Vega wrote in the daily newspaper La Jornada. “[This concern] resulted in the approval of more than 73 billion pesos (US$4 billion) for a financial rescue to give the state-run oil company liquidity, and the majority of the funds will be destined to pay debts and pensions.”

Fernández-Vega added, “This is good news, no doubt. However, the best solution would be to reduce the burdensome fiscal charge that PEMEX has had to endure since the modernization of our country, beginning with the administration of ex-President Miguel de la Madrid (1982-1988).”

According to Fernández-Vega, the fiscal charges that PEMEX has had to pay to the Mexican treasury have amounted to 155% of its total earnings. “No other company, public or private, has had to endure this fiscal situation,” he said.

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