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Mexico took a major step in the process of developing its deepwater supplies of crude oil and natural gas with the successful auction of 19 of the 29 blocks available to private companies to develop. The success of the auction, which took place in January, eased concerns that the energy reforms approved in 2013 and enacted in 2014 (SourceMex, Dec. 18, 2013, and Aug. 6, 2014) could be reverted if center-left candidate Andrés Manuel López Obrador wins the presidential election in July, as recent polls have suggested.

López Obrador, who will represent a coalition led by the Movimiento Regeneración Nacional (Morena) in the presidential elections scheduled for July 1, has spoken of making changes that could potentially water down the reforms, which open up Mexico's oil sector to private investors. The fiery center-left candidate has long opposed of opening the energy sector to private entities (SourceMex, March 16, 2005, Jan. 30, 2008, Oct. 16, 2013).

Specifically, López Obrador has promised that his administration would review every contract that has been awarded to determine whether they are in compliance with Article 27 of the Mexican Constitution, which stipulates that natural resources such as oil and gas are the property of all Mexicans. And he has vowed to take steps to prevent any move that would transfer Mexico's energy assets to foreign entities.

Under the energy reforms, President Enrique Peña Nieto's administration has held eight auctions since 2015 to open up energy-related projects to private companies, many of which are partnerships that include Mexican private companies. The first auction, held in July 2015, drew little interest (SourceMex, July 22, 2015), but subsequent tenders have been more successful (SourceMex, Oct. 14, 2015, Oct. 5, 2016, July 26, 2017).

Would center-left administration reverse reforms?

The Peña Nieto government is confident that all the actions taken to open up Mexico's energy sector stand on solid legal grounds. "These contracts are irreversible," Energy Secretary Pedro Joaquín Coldwell said in an interview with Reuters. The contracts have a duration of 25 to 30 years. Any company that feels its contracts have been violated can request the intervention of international arbitration authorities.

Furthermore, said Coldwell, the only entity in Mexico that has any authority whatsoever to change or rescind the contracts is the semi-autonomous Comisión Nacional de Hidrocarburos (CNH), the agency that originally handled the auctions.

"Mexico is no longer a country where a single person makes a decision," Coldwell said. "These contracts are fully protected."

Furthermore, Coldwell predicted that the auctions would continue regardless of the results of the July election. "These tenders are going to take place no matter who wins the presidency," he said.

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Immediately after the announcement of the auction results, López Obrador repeated his pledge to review all oil contracts if elected president. He also downplayed the importance of the auction, calling the process "just a show, pure demagoguery," and irrelevant to Mexico's effort to increase its oil reserves. "The contracts that were signed are, more than anything else, for financial speculation, not for production, not to extract oil, not to develop the oil industry," he said.

Analysts agree there is little that López Obrador can do to reverse the reforms, which involved changes to the Constitution that allow private companies and consortia to conduct exploration activities and exploit oil reserves. In approving the reforms, Congress ensured there was language specifying that any oil that is extracted remains the property of the Mexican state, thus making sure that Article 27 of the Mexican Constitution was preserved.

"The energy reforms are here to stay. It would be extremely complex to attain the consensus required to modify them," said analysts for consulting company KPMG, who write a regular column in the daily business newspaper El Financiero. "The law is not retroactive, meaning that the contracts that were signed would determine the relationship between the state and the operators."

López Obrador insists that any decision to make significant changes to the energy reforms would not be his alone, but would depend on the sentiment of the Mexican public. Morena has in the past called for a public referendum on the liberalization as well as the need to review signed contracts.

Analysts also noted that the strong interest in the latest auction, known as Ronda 2.4 (Round 2.4) was a sign that multinational companies were not worried about a potential victory by López Obrador.

"The auction was a great success for two reasons," financial columnist Maricarmen Cortés wrote in the daily newspaper Excelsior. "First, the government was able to auction off 19 of the 29 deepwater blocks that were made available. Secondly, this process came in the middle of the electoral season, when leading candidate Andrés Manuel López Obrador has threatened to reverse the energy reforms if he wins."

Similar comments came from Alicia Salgado, another financial columnist at Excelsior. "The resounding success of Ronda 2.4 leaves no doubt that international investors have greater confidence in the regulators of the energy sector than on the public opinion polls," she wrote.

Salgado pointed that the auction led by CNH president Juan Carlos Zepeda and his team was not only completed in a very speedy manner but also increased the chances that Mexico's oil reserves would increase over the long term.

The Instituto Mexicano del Petróleo (IMP), a research institution that is affiliated with the state-run oil company PEMEX, also pointed out that private investors were attracted by the potentially high yields available at the sites. The reserves are located at the Perdido Fold Belt, off the coast of Tamaulipas; the Cordilleras Mexicanas, in the deep waters off Veracruz state; and the Salina Basin, near the coastal areas of Tabasco state.

According to information gathered in earlier discoveries as well as established geological models, the blocks in the Perdido Fold Belt are expected to contain light crude, super-light crude, wet gas, and dry gas. The studies indicate that the Cordilleras Mexicanas region probably contains light crude, wet gas, and dry gas, while the Salina Basin is believed to hold light crude, super-light crude, heavy crude, and wet gas.

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"From a technical point of view, what the market told us is that it shares the assessment of the Mexican government that the sites have a high level of potential reserves to exploit, and that large volumes of oil and gas can be extracted from the sites," IMP president Ernesto Ríos Patrón told the daily business newspaper El Economista. "That is sufficient incentive [for these companies] to invest in the sites.

The auction secured about US$93 billion, which was more than twice as high as the previous nine tenders.

"This is an investment that will occur over the long term, not immediately," columnist Macario Schettino wrote in El Financiero. "Furthermore, this is a small amount when compared to the investment that the secretary of energy estimates the industry needs, including US$600 billion in the hydrocarbons sector and US$400 billion in electricity infrastructure."

But Schettino also pointed out that the results were positive, because the investments were committed at a time when adverse global factors are at play, including the volatile international energy market, the protectionist policies promoted by US President Donald Trump, the US tax reform, and the upcoming elections for the US Congress.

A win for Dutch-British conglomerate Royal Dutch Shell

The largest bidder was the Dutch-British conglomerate Royal Dutch Shell plc, one of 20 companies to participate in the process. Shell obtained the exploration and exploitation rights to nine of the 19 sites that received bids. It won four of the bids on its own, four others in partnership with Qatar Petroleum International, and another in a joint venture with PEMEX.

The successful bidders for the other 10 blocks were the Malaysian company PC Carigali (Petronas), which acquired rights for six sites; PEMEX, which was awarded two sites on its own and one in partnership with the US-based multinational Chevron; and a joint venture between the Italian oil company Eni and Qatar Petroleum International Limited.

Analysts said they were not surprised that Shell took such an interest in Mexico's deepwater auction, because the company already had operations in the Gulf of Mexico.

"It's only natural for Shell to pursue opportunities in Mexico," said Lysle Brinker, analyst at consultancy IHS Markit. "It's near an area where Shell is already producing."

Officials at Shell's Mexican operations said he multinational company's investment would have a positive impact on the Mexican economy by creating new employment.

"This will translate into real and effective work for Mexico—we are all winners," said Alberto de la Fuente, president of Shell México.

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