



Mexico's Oil Reform:

Managing expectations

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Preview of coming attractions

- The speaker's three hats
- Quiz about Houston
- History lesson: Who owns the subsurface minerals?
- Visual picture: Mexico's oil potential and aspirations
- Conundrums
- Star-gazing
- Q&A

A tricorne (3 pointed hat)



[Charles III of Spain](#), c. 1786–88

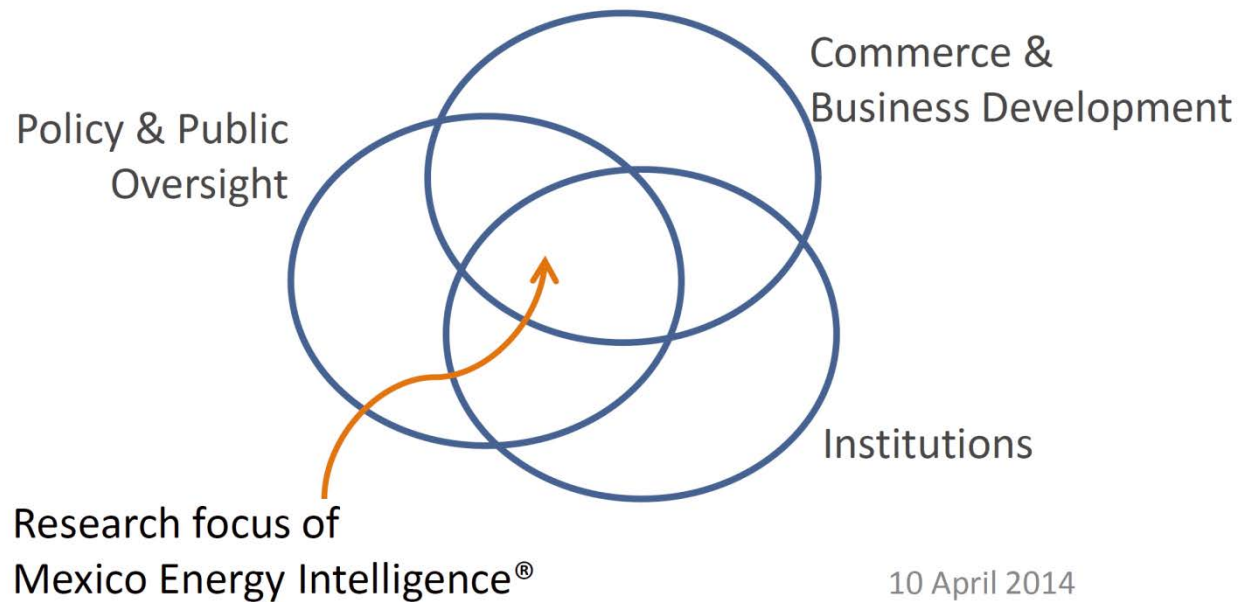
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Fig. 1

MEI Research Focus: RISK INSIGHT

The interface between social science, public policy and business development



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Posted in: [Featured Interview](#) | Feb 23, 2014 11:35 pm, by [George Baker](#) [No comments](#)

On January 7, 2014, Arturo Henríquez Autrey, the president of Pemex Procurement International, Inc., gave a presentation in Houston. Afterwards, he spoke with MEI and agreed to an interview. Within 10 days of his presentation, Mr. Henríquez was named Corporate Director of Procurement in Pemex, with the result that his...

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PAPER TRAIL IN MEXICO'S ENERGY SECTOR

Posted in: [Featured](#) | Feb 22, 2014 12:38 am, by [George Baker](#) [No comments](#)

In this report, we give focus to a very Mexican characteristic in the law and regulations, which is to blur the critical path of decision-making in a fog of language about how one government agency advises another and a third making decisions based on the guidelines of someone else, etc.....

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BAKER TO PRESENT MARCH 12 AT AIPN'S US CHAPTER LUNCHEON

Posted in: [Featured](#), [Mexican energy](#), [Mexico energy reform](#) | Feb 18, 2014 12:01 am, by [George Baker](#) [No comments](#)

George Baker will be presenting at AIPN's US Chapter Luncheon on March 12. The topic of his presentation is: MANAGING EXPECTATIONS REGARDING MEXICAN ENERGY REFORM. There are heightened expectations in Houston regarding the outlook for a real energy reform in Mexico, one that would finally create new commercial opportunities for...

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TWO REPORTS ON PEMEX'S 2013-14 MEGA-TENDER FOR ONSHORE WELLS

Posted in: [Market Notes](#), [Mexican economy](#), [Mexico Energy Intelligence](#), [Pemex](#) | Feb 18, 2014 9:28 pm, by [George Baker](#) [No comments](#)

On August 29, 2013, Pemex issued an international RFP (Request for Proposal) No. 18575088-542-13 which called for proposals for some 1,300 wells in ten blocks (or packages). In December, two of the five blocks in Chicontepec were withdrawn, leaving the maximum number of wells at slightly less than 800. The...

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NAVIGATION PATH FOR PEMEX DOCUMENTATION

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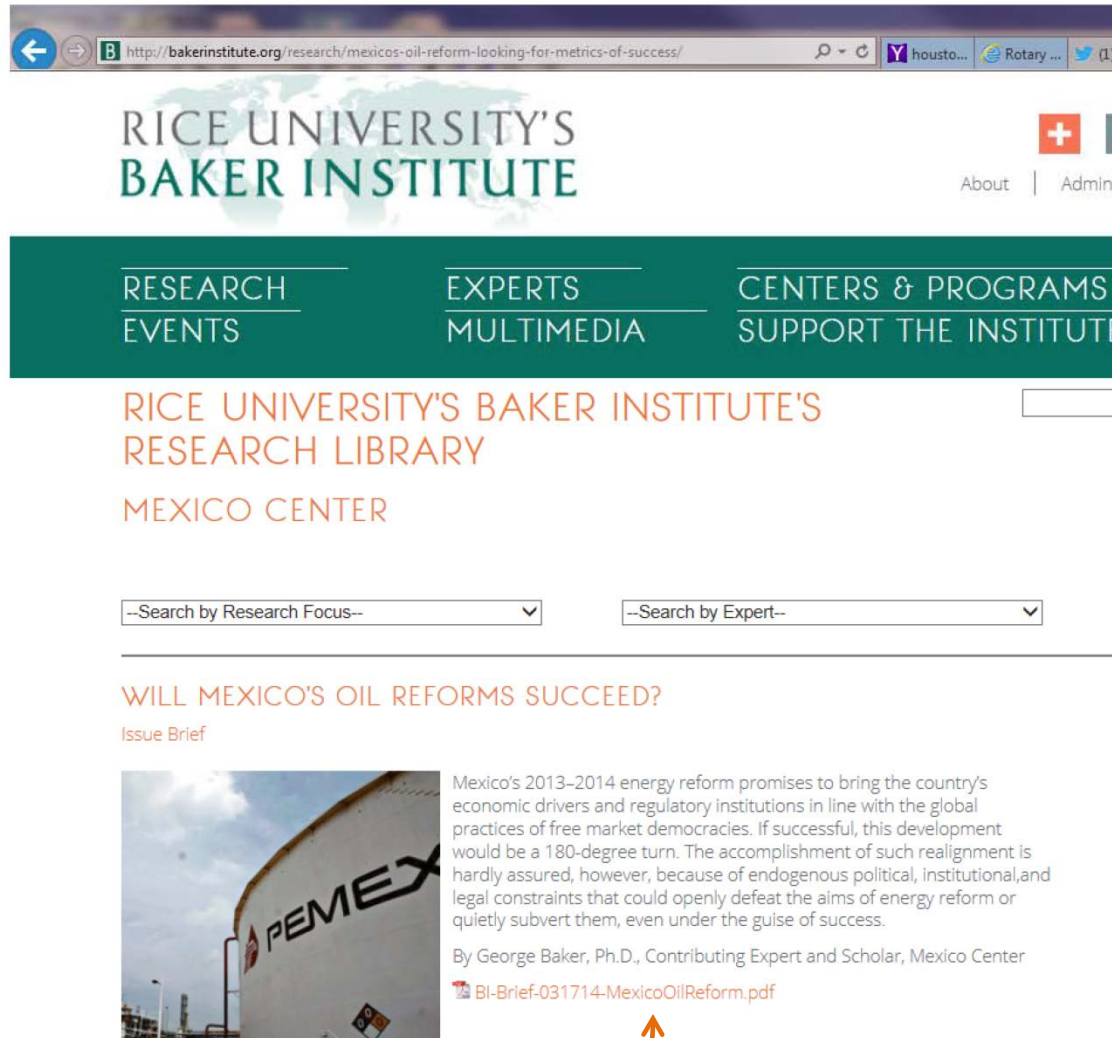
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Mexico Center: Issue Brief

Will Mexico's Oil Reforms Succeed?



The screenshot shows a web browser window with the URL <http://bakerinstitute.org/research/mexicos-oil-reform-looking-for-metrics-of-success/>. The page header features the Rice University Baker Institute logo and navigation links for 'About' and 'Adminis'. A dark green navigation bar contains links for 'RESEARCH', 'EVENTS', 'EXPERTS', 'MULTIMEDIA', 'CENTERS & PROGRAMS', and 'SUPPORT THE INSTITUTE'. Below this, the text 'RICE UNIVERSITY'S BAKER INSTITUTE'S RESEARCH LIBRARY' and 'MEXICO CENTER' is displayed. Two search dropdown menus are visible: '--Search by Research Focus--' and '--Search by Expert--'. The main content area is titled 'WILL MEXICO'S OIL REFORMS SUCCEED?' and is categorized as an 'Issue Brief'. It includes a photograph of a PEMEX storage tank and a paragraph of text discussing Mexico's 2013-2014 energy reform. The author is identified as George Baker, Ph.D., Contributing Expert and Scholar, Mexico Center. A PDF link is provided: [BI-Brief-031714-MexicoOilReform.pdf](#).

Download here 

Quiz about Houston

Solve for X

$$X = \left(\left(\overset{\textit{Direct effects}}{\left(\frac{\text{Space}}{A_x} + \frac{\text{Oil}}{B_x} + \frac{\text{Medicine}}{C_x} \right)} \right) + \left(\overset{\textit{Indirect effects}}{\left(\frac{\text{Arts}}{D_x} + \frac{\text{Higher Ed}}{E_x} \right)} \right) \right)$$

Answer to Quiz about Houston

- It is the exponential demand by the oil industry for increased signal processing of geoscientific data that drives technological innovation in the oil industry, with direct spill-over effects in space and medicine.
- Indirect benefits are investments in higher education (the Baker Institute, for example) and in the visual and performing arts.

For discussion of this observation about Houston, read my article

« **Houston - Carrefour de l'or noir** » (*Sciences Humaines*, Mis à jour le 15/06/2011)

http://www.scienceshumaines.com/houston-carrefour-de-l-or-noir_fr_24612.html

History lesson

A quick survey of five (5) centuries about just one question:
Who owns the subsurface mineral rights?



Who owns the subsurface minerals?

Isabella I of Castile



Answer: The Crown
(1492-1894)



Who owns the subsurface minerals?

Porfirio Díaz of Mexico



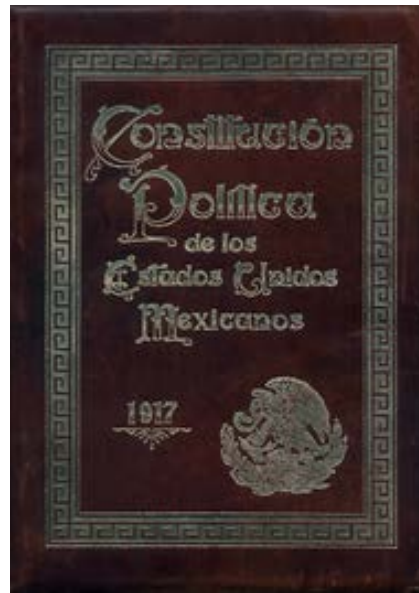
The immediate result of the change in law was a major oil boom in Mexico, in the upstream, midstream and downstream. Two prominent oilmen in Mexico were Edward Doheny (US) and Weetman Pearson (UK).

Answer: The Surface Owner
(1894-1917)



Who owns the subsurface minerals?

Constitution of 1917



Article 27. All natural resources in national territory are property of the nation, and private exploitation may only be carried out through concessions.

Answer: The State
(Since 1917)



Who owns the subsurface minerals?

Sir Weetman Pearson of England



In 1889, he founded the first EPC company in Mexico, winning major contracts. In 1909, he founded EL AGUILA (Mexican Eagle) oil company.

Answer: The State
(Controversy: 1917-1938)

But you don't mean to apply Article 27 **retroactively**, do you?

"We bought the land, with mineral rights, under the then-current law."

Who owns the subsurface minerals?

Lázaro Cárdenas of Mexico



*Answer: The State
(Controversy resolved by
expropriation in 1938)*

Unable to definitively resolve the controversy over the retroactivity of Article 27—and exploiting the pretext of a labor dispute—the oil industry was nationalized.

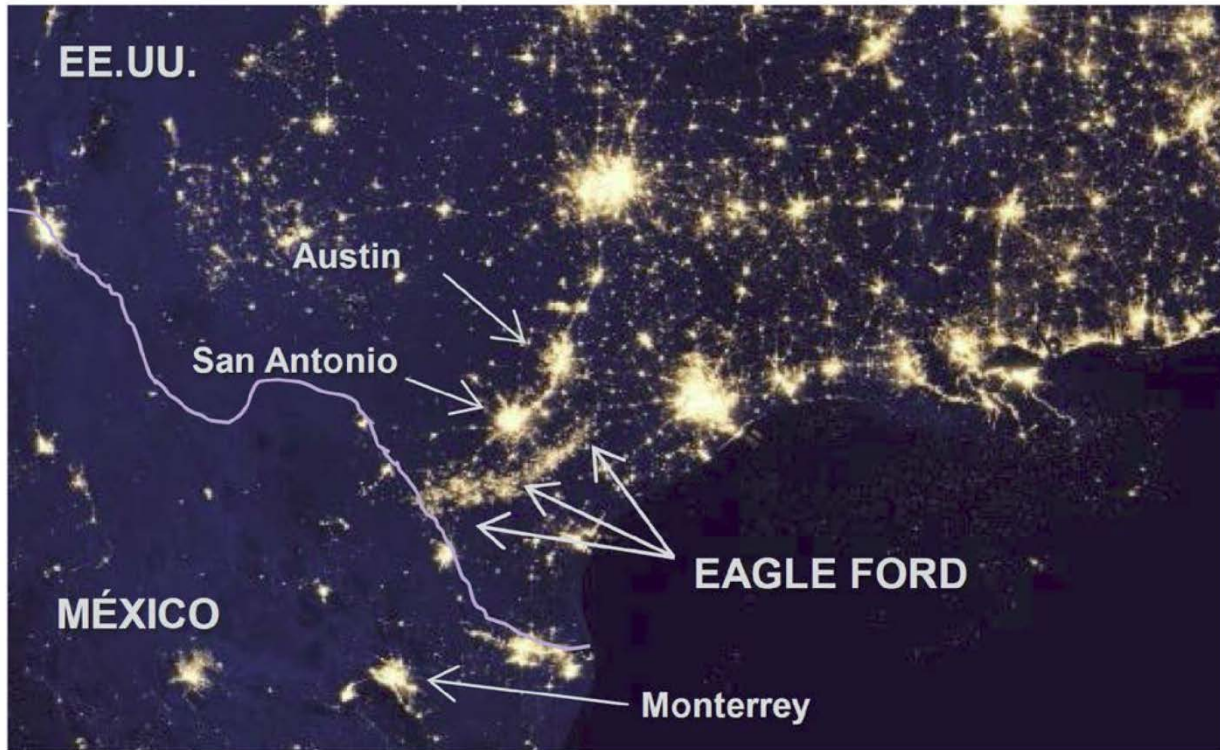
Oil company assets in Mexico were seized and the companies were expelled.



Visuals

Mexico and the Shale Revolution

Eagle Ford formation, Texas

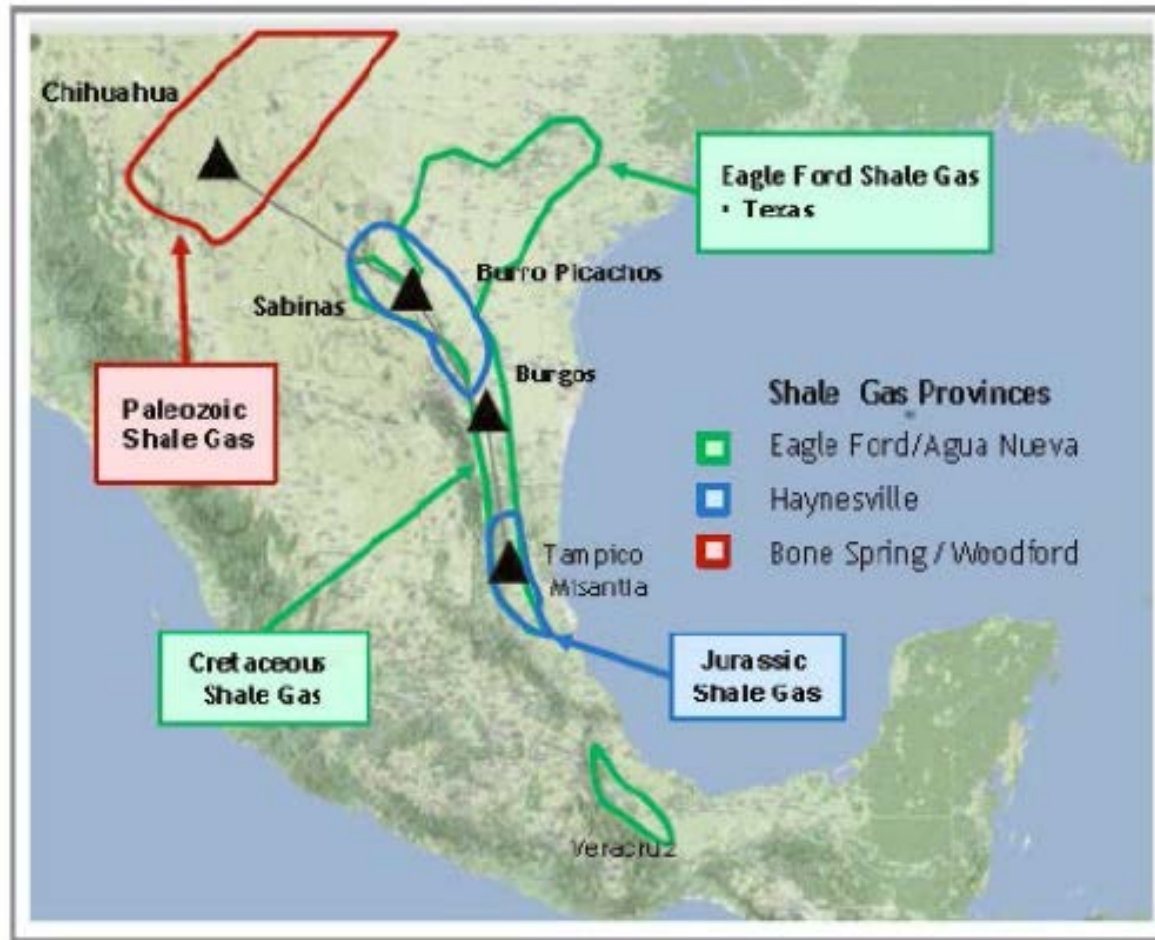


In 2012, only 3 wells of shale oil/gas were drilled in Mexico. By contrast, in the USA that number grew to 9,100.

Mexico's shale gas potential is large

Estimates of 150-450 Tcf

Enough to supply current U.S. gas demand for 17-50 years

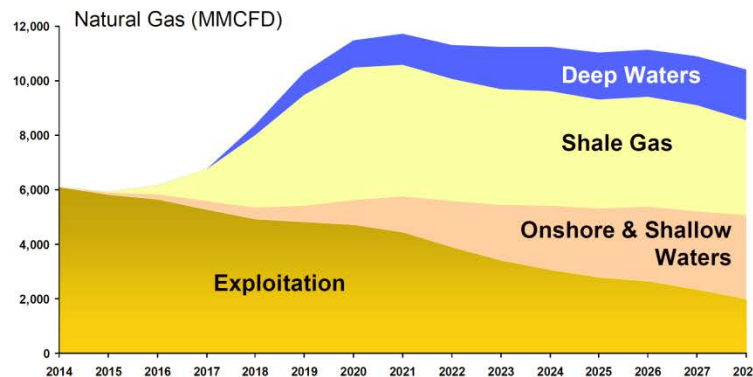
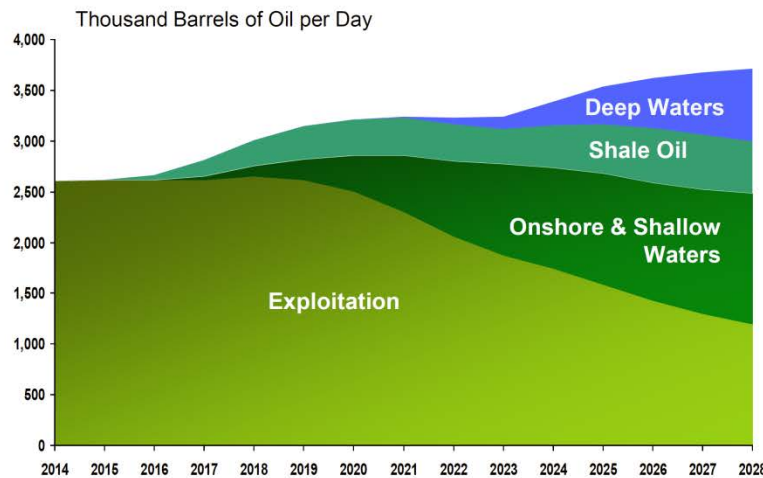


Big expectations from upstream redesign (aka, reform)



Comisión Nacional
de Hidrocarburos

Natural Oil & Gas Production Post-Reform (2014 – 2028)



◆ During the next years oil production will come mainly from South-eastern Basins, while supply in the middle and long terms is estimated to come from the Deep Gulf of Mexico and unconventional plays.

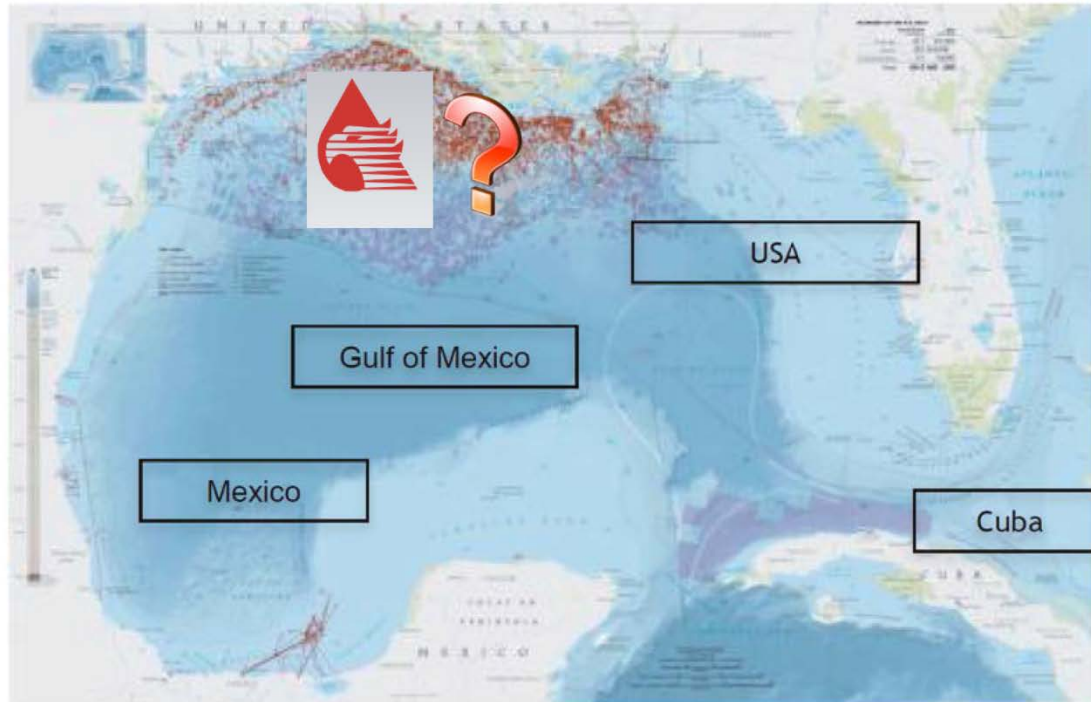
◆ **The implementation of the Energy reform to assign blocks to Mexican and international companies, together with a favorable fiscal regime will promote the supply of shale gas in the near future.**

Source: CNH 2014-02-05 Shale Potential in Mexico Portfolios 2013 – Upper Scenario, Includes the development of discovered non-associated deep water fields

CNH February 5, 2014 Shale Gas Potential in Mexico

Pemex 2.0

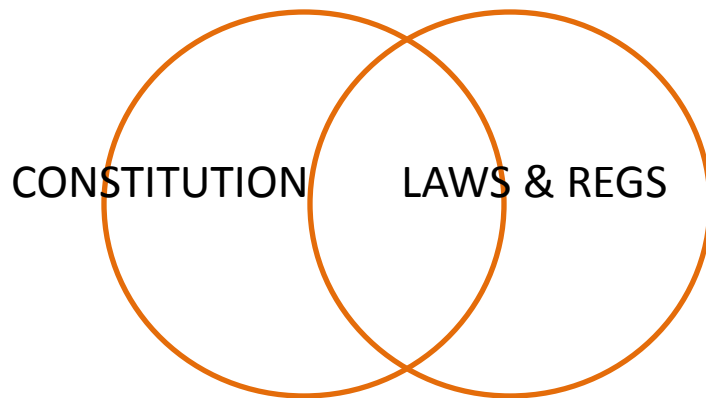
Deepwater and ultra deepwater drills in the Gulf of Mexico



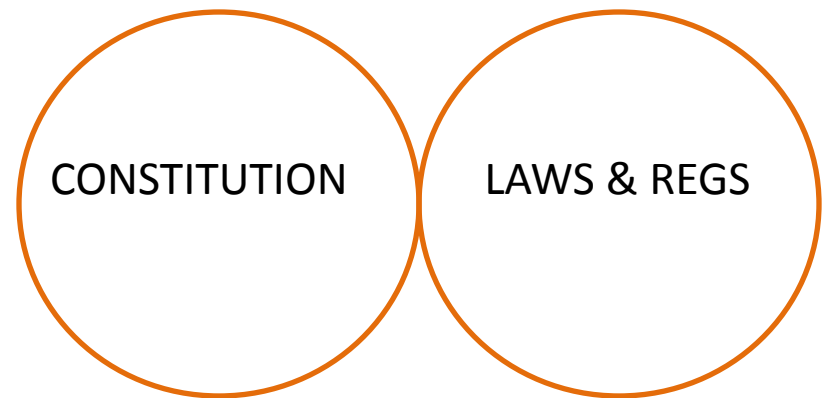
While there were only 6 wells drilled in deepwaters and ultra deepwaters in Mexico during 2012, in the USA that number was 137.

What's going on in Mexican Energy?

1958-2013



2013-2014+



*The right
course
correction*

Goal: Return to the Executive and Legislative Branches the authority to adapt energy policy and law to evolving technologies, business models and market conditions.

Examples: Shale Revolution and Deepwater

Conundrums



Possible glitches

Paraphrasing Winston Churchill's remark about the U.S. Government:

**THE MEXICAN GOVERNMENT
WILL ALWAYS DO THE RIGHT
THING IN ENERGY POLICY—
AFTER HAVING EXPLORED ALL
OTHER POSSIBILITIES.**

Doing the right thing by Pemex

- Create a Pemex 2.0 as a mercantile, stock-issuing company
 - Majority state-owned
 - Unrestricted minority shares in the NYSE
 - Mandate to qualify as an operator outside of Mexico
 - Free managers from status as public servants
 - Introduce global hiring of managers/executives
 - Establish English as the corporate language
- Benefits
 - The business model has been tested in court, lawsuits, arbitration and in public opinion.
 - Introduce dynamic of global competitiveness
 - Instantaneous feedback from minority shareholders

Other than doing the right thing

- **Restrict public discussion prior to the promulgation of 28 laws**
- **Create a new legal figure of “State Enterprise”**
 - New laws for Pemex and CFE
 - Mandate to seek joint ventures and farm-outs
- **Do not update Mexico’s National Petroleum Narrative**
- **Create unnecessary risks**
 - The business model has *not* been tested in court, lawsuits, arbitration or in public opinion in Mexico or Houston.
 - Can the “State Enterprise” exercise sovereign immunity?
 - Will it be required to follow NAFTA procurement rules?
 - Will its employees be public servants subject to the LFRSP?

Doing the right thing by investors

- **Give priority to the license model without Pemex participation**
- **Unequivocal right to post reserves volumetrically**
- **Fiscal terms competitive with those in U.S.**
- **Benefits**
 - Participation in a public tender by an American oil company will have positive ripple effects in other sectors of the Mexican economy
 - Evidence that the government has done the right thing.

Star-gazing



What's going to happen?

- **Pemex to be grandfathered in “Round Zero”** (by Sept. 17, 2014)
 - All profitable production assets
 - Shallow water
 - Onshore
 - Prospective areas (undiscovered or undeveloped)
 - Perdido (ultra-deepwater)
 - Shale formations (20%)
 - If permitted, Pemex to seek JVs and farm-outs *immediately*
- **Everyone else**
 - **Join with Pemex** in a JV or farm-out
 - **Wait until 2Q+ 2015** for a “Round One” with contractual options
 - License agreement
 - Production-sharing agreement
 - Profit-sharing agreement

As for everything else,
Stay tuned!

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Questions or comments?





For your attention,
muchas gracias

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