

The Mexican Energy Reform

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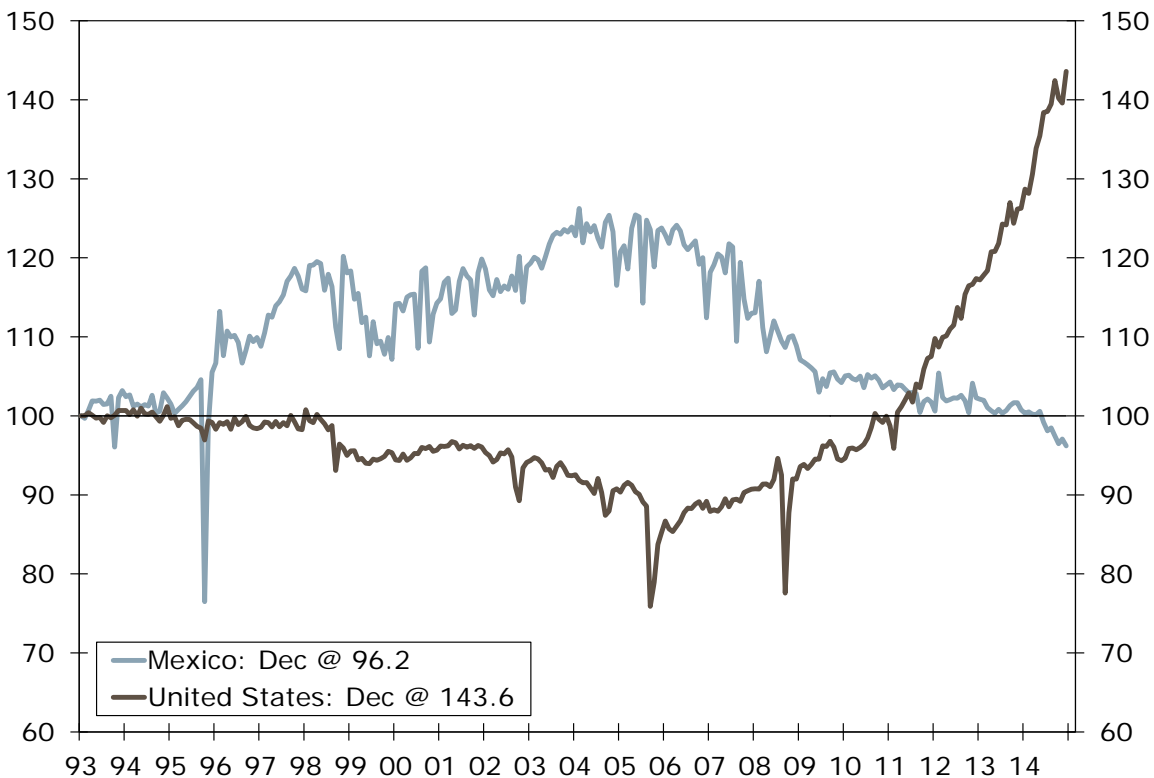
Together we'll go far



Different ways to react to price/profit incentives

Production of Petroleum and Nat. Gas

Index Jan 1993=100



Source: IHS and Wells Fargo Securities, LLC

Still waiting for the surge in growth

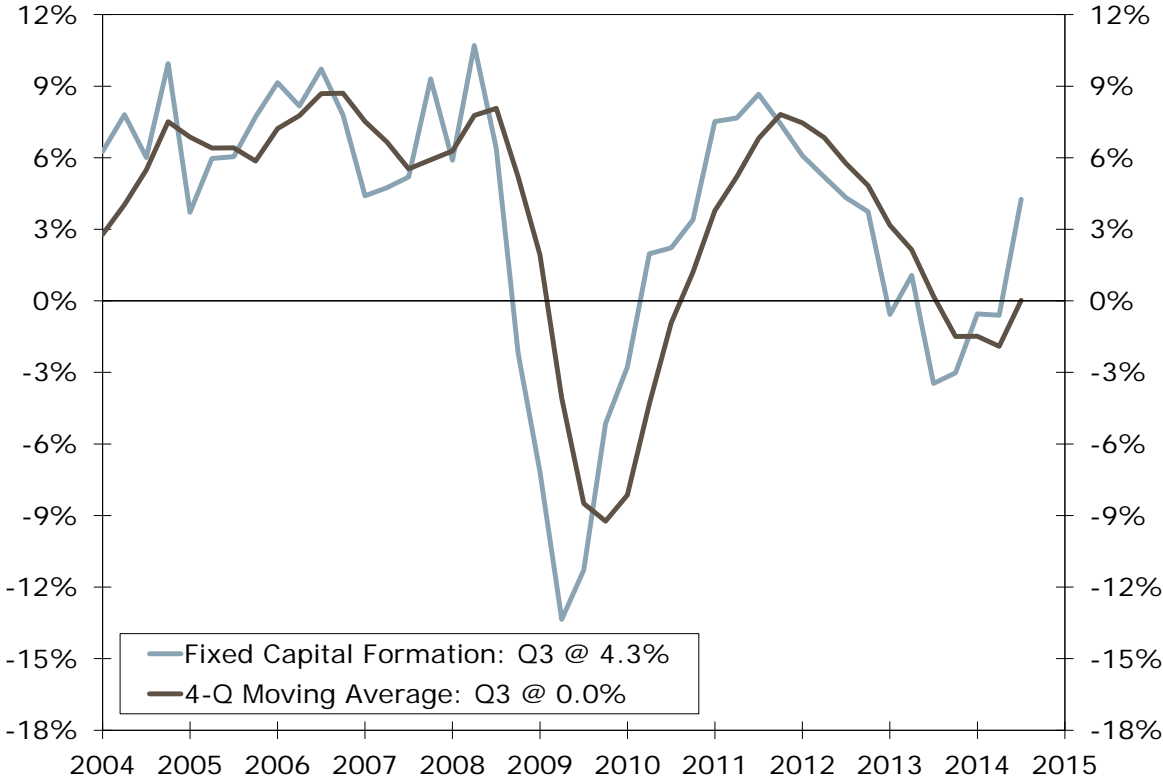


Source: U.S. Department of the Treasury and Wells Fargo Securities, LLC

Gross fixed investment is starting to grow but remains very weak

Mexican Gross Fixed Investment

Year-over-Year Percent Change

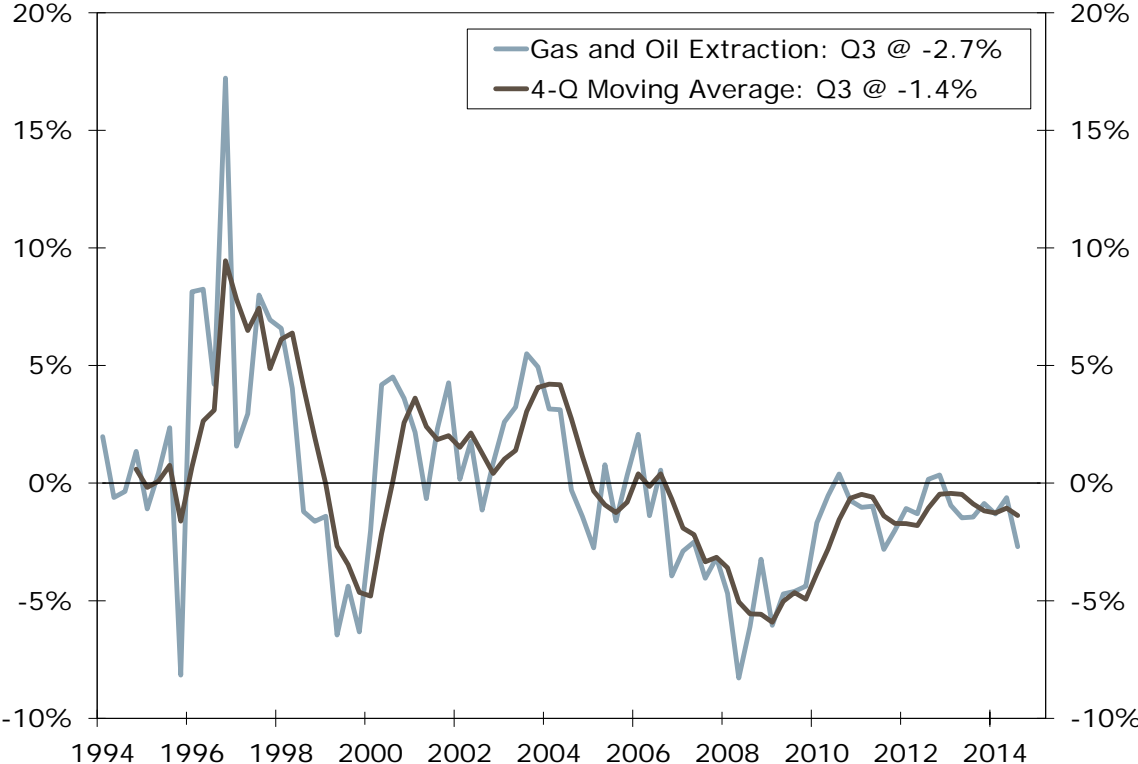


Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

Going nowhere!

Mexican Mining, Oil and Gas

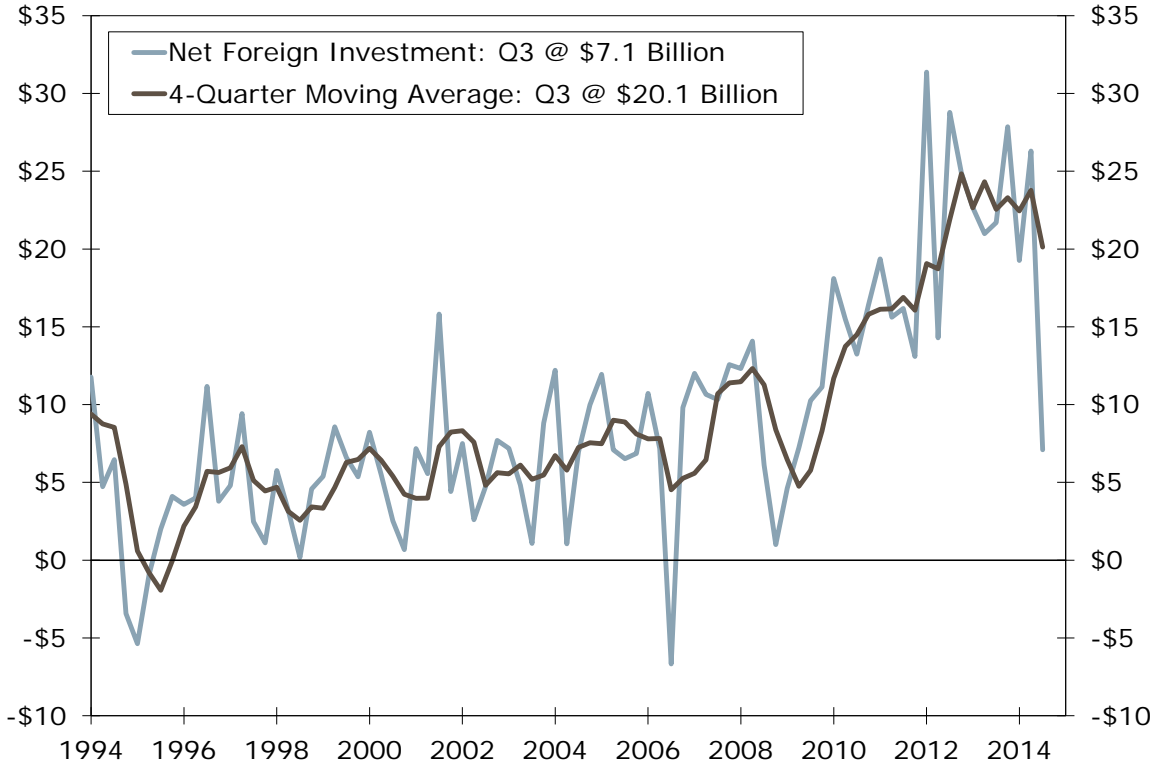
Year-over-Year Percent Change, NSA



Source: U.S. Department of Labor and Wells Fargo Securities, LLC

Worrisome fall in FDI into Mexico

Mexican Foreign Direct Investment
Billions of Dollars, NSA

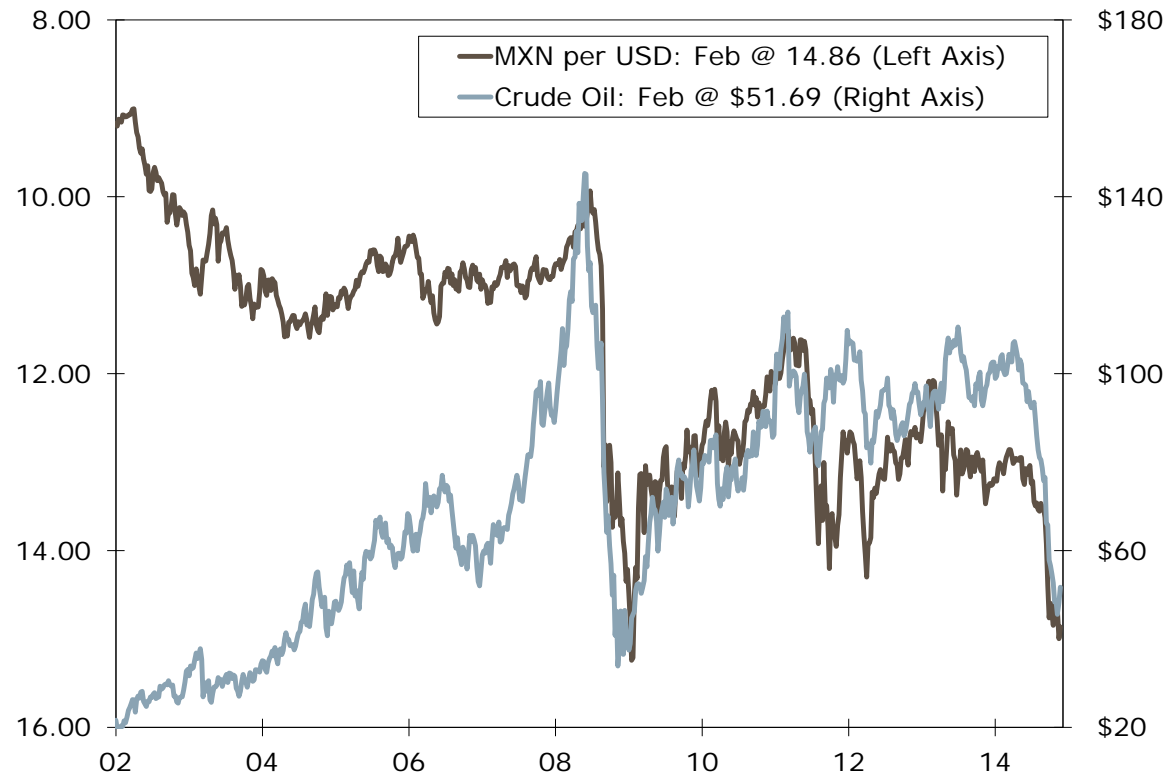


Source: U.S. Department of Labor and Wells Fargo Securities, LLC

Tell me where are you going!

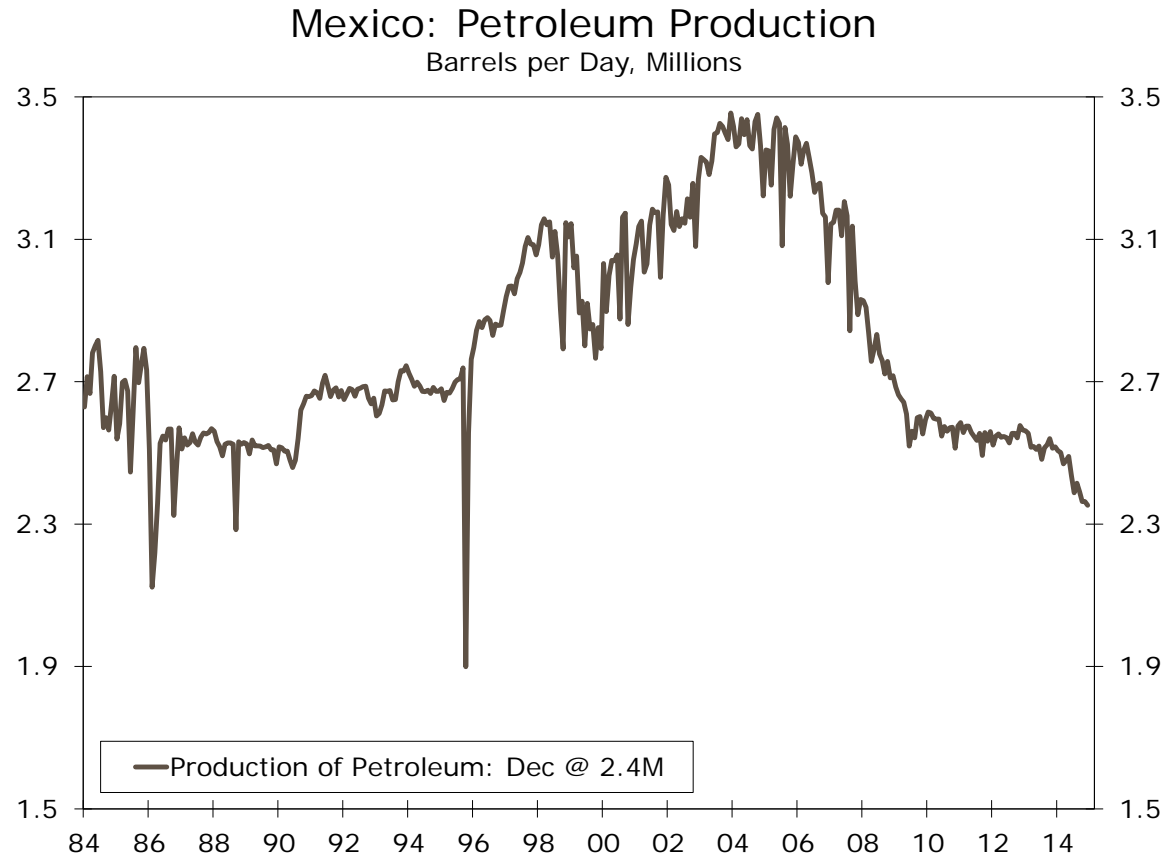
Mexican Exchange Rate and Crude Oil

MXN per USD (Inverted), USD per Barrel



Source: U.S. Department of Labor and Wells Fargo Securities, LLC

Going down!



Source: U.S. Department of Labor and Wells Fargo Securities, LLC

Opening the hydrocarbons industry to private participation- Government highly enthusiastic



December 2013- Constitutional Amendment



August 2014- Energy-related Secondary Legislation

- End of 76 year old monopoly over hydrocarbons sector
- Access to untapped deep-water reserves, offshore gas and onshore plays, plus marginal proven undeveloped reserves
- Private and foreign operators able to undertake projects t on their own or in partnership with PEMEX
- Government expects up to USD50bn in FDI through 2018, adding 1% to GDP growth, and 2% by 2025
- Government expects 500,000 direct jobs through 2018 and 2.5m more by 2025

Selected Aspects of the New Upstream Regulatory Framework

Mexican state owns subsoil, but reserves booking allowed

International Arbitration:
UNCITRAL

Local Content: To rise from 25% in 2015 to 35% in 2025

Contract Types

Royalty: if price < \$48, 7.5%
If price ≥ \$48,
 $(0.125 * \text{contractual price}) + 1.5$

Service Contract

Revenue Sharing

Production Sharing

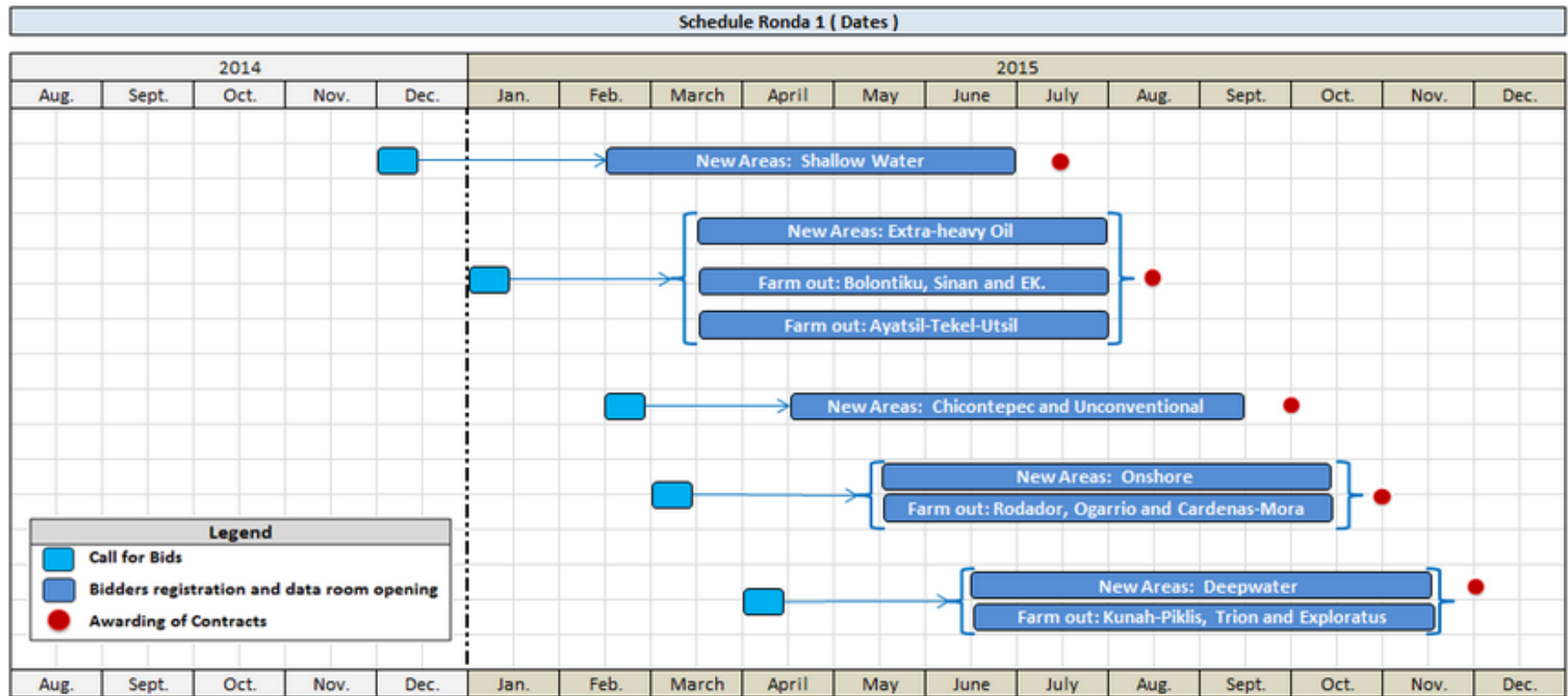
License

Payment in Cash

Payment in Kind

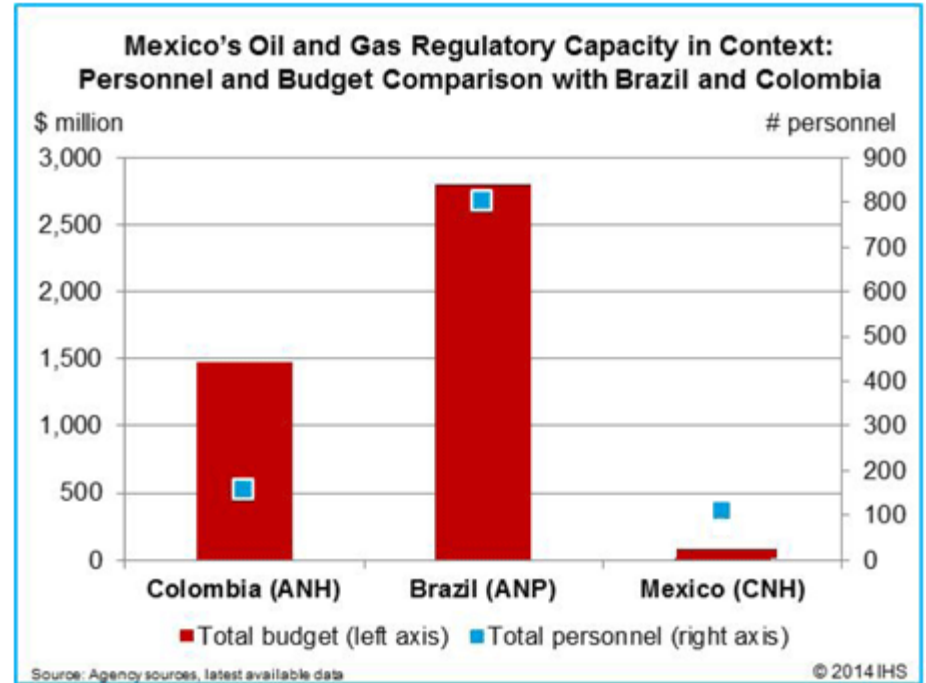
Latest on bid round plans and reform implementation

- Fourteen shallow water blocks
- Salina, Macuspana basin (Veracruz, Tabasco, Campeche)
- Production Sharing Agreements



Capacity constraints within regulatory agencies

- Government pushing for swift implementation but regulators face a steep learning curve.
- Budget and personnel constraints likely to hamper regulatory capacity.
- Potential delays in the approval of permits if authorities let regulatory agencies to operate independently,
- or omission problems arising later due to political pressure to expedite permits rapidly (169 blocks in first round).

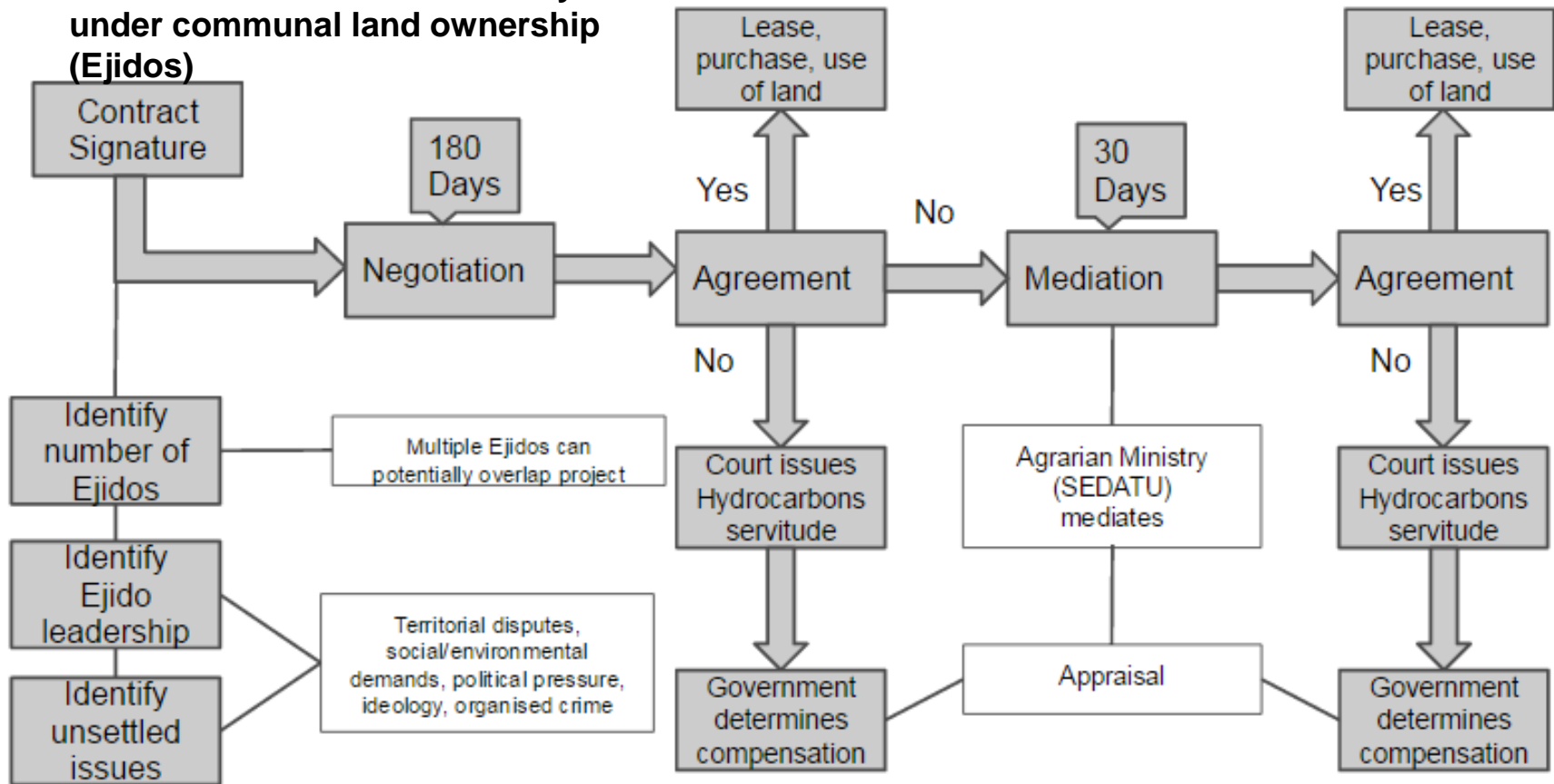


Watch For:

Energy and Finance Ministries potentially undermining role of regulatory agencies.

Onshore projects likely to face complicated negotiations over superficial rights with communal landowners.

- About 53% of Mexico's territory under communal land ownership (Ejidos)



- Between 0.5%-3% of a project's revenue towards Ejidos for non-associated natural gas projects, and 0.5%-2% for other hydrocarbon projects

Prospective Resources	
	BBOE
Burgos	2.9
Deep Waters in the GoM	26.6
Sabinas	0.4
Southeastern	20.1
Tampico-Misantla	2.5
Veracruz	1.6
Yucatan Platfom	0.5
Total	54.6

Source: SENER and Wells Fargo Securities, LLC

FMPED

Mexican Petroleum Fund for Stabilization and Development

- The purpose of this fund is to receive, administer and distribute the income derived from assignments and contracts, with exception of taxes.
- It will be a Trust within Mexico's Central Bank with a Technical Committee that will have 4 independent board members plus 3 board members from the Government

Source: SENER and Wells Fargo Securities, LLC

- Pemex will be transformed into a “State Productive Enterprise,” with budgetary, technical and operational autonomy (2-year transition)
- There will be a “Round Zero” to ensure Pemex’s exploration and production investment portfolio
- Associations in exploration and production for oil and gas, refining and petrochemicals are allowed
- Pemex will have a new corporate governance structure, in line with international best practices
- Pemex’s new Board of Directors will be composed of 5 board members representing the Federal Government (including the Energy Minister who will chair the Board), and 5 independent board members
- Pemex will have a more flexible and competitive fiscal regime, so it can retain a larger share of its profits for reinvestment

Source: SENER and Wells Fargo Securities, LLC

- **Private investment in Generation will be allowed**
- **An independent system operator (CENACE) will implement a Competitive Electricity Market**
- **Joint ventures in Transmission and Distribution between CFE and private companies**
- **CFE will be converted into an energy company with freedom to form partnerships; will have financial and operational autonomy, and freedom to establish employee wages**
- **Regulators will be strengthened**

Source: SENER and Wells Fargo Securities, LLC

- **Generation:**
 - Generators can sign long term contracts to reduce their market exposure
 - The spot market will be based on short-term optimal dispatch
 - CFE will operate its generation independently from its other activities, and will compete on a level playing field
- **Marketing:**
 - Standard Users will receive their service from CFE-Retail, which will buy energy in the spot market and under contract
 - Qualified Users will be able to buy energy directly or through a retailer
 - The threshold to be a Qualified User will decrease over time
- **Power Market:**
 - Generators and marketers will make their supply and demand offers each day
 - CENACE will establish the optimal dispatch and will calculate equilibrium prices
 - Long term contracts will cover the majority of demand; relatively small volume will be purchased on the spot market
 - Capacity markets will be implemented to ensure resource adequacy
- **Transmission and Distribution:**
 - The T&D companies will not buy or sell energy; they will only operate the wires
 - They will charge rates established by the CRE, under incentive-based regulation
 - CENACE will process payments between market participants and the T&D companies

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