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Bid by bid, Mexico is building a private oil and gas sector

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Developing a private sector in the oil and gas industry is surely a huge undertaking—even more so in a country where private investment was banned for almost eight decades. How can a private oil and gas sector be built after all this time? Change the rules of the game, establish a clear bidding process, select some attractive assets to be auctioned off, and hope that a decent number of potential investors will show interest. This is easier said than done, but it is currently happening in Mexico. The second-largest Latin American economy is gradually laying the foundation for an oil and gas sector where private—along with some state-owned—international companies are taking central stage.

So far, five bidding rounds have taken place in Mexico, resulting in the awarding of 48 blocks in both offshore and onshore areas to international and domestic firms. This number is more significant when looked at in dollar terms. According to official press releases (PR 049, 069, 092, 125, and 139) made public by Mexico's Ministry of Energy (SENER), the ongoing investment committed to developing these blocks is around US$49 billion—a handsome number for a country that received US$26.7 billion in direct foreign investment in 2016, according to the Ministry of Economics. This amount is even larger if we take into account other activities related to the energy sector such as natural gas infrastructure, electricity, and seismic exploration.

The wave of new participants in the Mexican oil and gas industry is coming at a time when crude output in Mexico has been declining for several years—a worrying reality that is keeping Mexican authorities busy. The oil and gas biding round that occurred on June 19—known as "Round 2.1"—is just the latest effort to turn things around. Altogether, it is reported that 21 firms participated in this first tender of Round 2, which consisted of 15 shallow water blocks—10 of which were awarded to 12 firms, either individually or as consortiums.

Pemex, the country's state-owned oil and gas company, took two blocks home in association with Germany's DEA Deutsche Erdoel AG (Block 2) and Colombia's Ecopetrol (Block 8). For the bidding process in general, it is a good sign to see Pemex participating—and succeeding—after being absent from some of the past tenders. However, it is even more encouraging to see the number of players seeking to be part of the new Mexican energy ecosystem. Bid by bid, the most recent member of the International Energy Agency is recrafting an oil and gas industry where Pemex—the still-dominant player—must compete and cooperate with newcomers.

The remaining eight blocks from Round 2.1 were awarded as follows:

- Block 6: PC Carigali (Malaysia) and Ecopetrol (Colombia)
- Block 7: ENI Mexico (Italy), Capricorn Energy (the United Kingdom), and Citla Energy (Mexico)
- Block 9: Capricorn Energy (the United Kingdom) and Citla Energy (Mexico)
- Block 10: ENI Mexico (Italy)
- Block 11: Repsol Exploración (Spain) and Sierra Perote (Mexico)
- Block 12: Lukoil International Upstream Holding (Russia)
- Block 14: ENI Mexico (Italy) and Citla Energy (Mexico)
- Block 15: Total E&P (France) and Shell (the Netherlands and the United Kingdom)

It can be appreciated that Mexico is welcoming more participants into its industry as the bidding rounds progress. SENER reports that as a result of Round 2.1, four new companies will begin to operate in the country, while four others will increase their operations; this will eventually result in greater direct investment. Estimates from SENER indicate that US$8.2 billion will be poured into the development of the awarded blocks over the next 30 to 40 years.

Among firms with greater presence in Mexico, Italy's ENI deserves particular attention, since it won three blocks this time—one individually and two as part of a consortium. Regulators in Mexico must be pleased to realize that ENI, which also secured a block in Round 1.2 in 2015, continues to bet on Mexico as part of its strategy to expand internationally. The same applies to Malaysia's Petronas Carigali and France's Total, which also won contracts in past rounds.

After a humble start in Round 1.1 when only two out of 14 blocks were awarded, it seems that Mexico has made significant progress in making tenders more attractive, and the overall outcome of the bidding rounds to date can be considered positive.

All this considered, measuring the success of reforms in general—and bidding rounds in particular—should not be narrowly based upon the increasing number of international operators nor upon the number of blocks awarded. Authorities should not ignore the necessity of developing a domestic oil and gas sector, which means promoting the participation of a larger number of domestic companies by crafting specific policies to that end. And this could be within reach for Mexico. The existence of positive local externalities such as specialized labor and service firms in regions today being affected by low prices, together with the help of adequate policies and incentives, may represent fertile ground for the development of a larger number of domestic operators.

In this process of opening up the oil and gas sector to private investment, the participation of Mexican firms like Sierra Oil and Gas, Diavaz, Petrobal, and Citla Energy—which have already secured contracts—is more than welcome, but it is not enough in the long term. Given the potential of the oil and gas sector in Mexico, encouraging the development of a larger number of domestic firms should be one of the top objectives of the energy reform.

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