Marcos y Asociados

20+Year Experts

# Energy Monthly News

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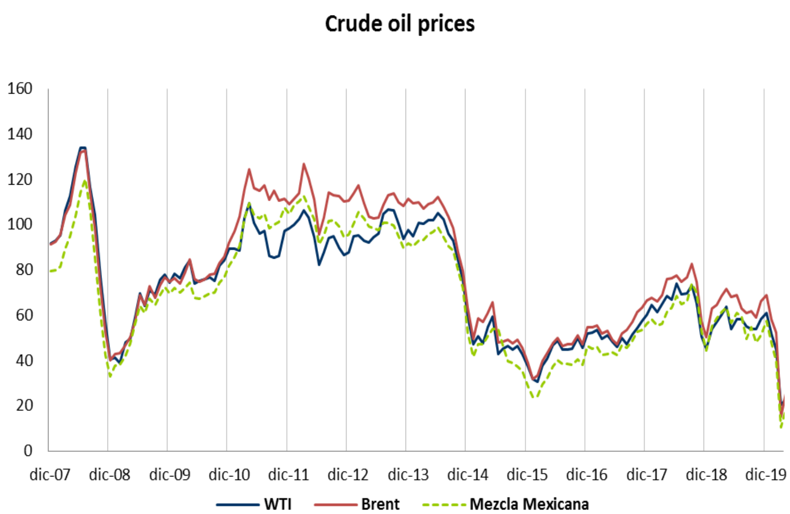


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|---|---|
| Crude oil Price* US/BD | WTI 38.72<br>BRENT 41.05<br>MME 33.67 |
| NG price* US/MMBTU | Henry Hub 1.54 |
| Mx crude production MMbd | 1.64 *(May-20)* |
| Mx NG production MMpcd | 4,449 *(May-20)* |
| US crude production MMbd | 12.71 *(March-20)* |

| | |
|---|---|
| FX Rate** | 22.79 |

** 25/06/2020 **26/06/2020*
*Source: EIA. El Reforma, Pemex, Banxico, and CNH*

## Oil & Gas

### Pemex proposal would sharply cut drilling rigs from private service firms – *Reuters*

Pemex has proposed slashing the number of privately owned drilling rigs used this year as stated in the proposal dated May 20, “Movement of Rigs, Quarterly Operational Program.” The document details 76 separate rig suspensions this year, with 14 planned for the company’s most productive field – Ku Maloob Zaap – responsible for about half of Pemex’s current oil output. The cost-cutting measures detailed in the plan mirror cutbacks made by other global producers in the wake of collapsing demand and crashing prices this year.

Labeled “preliminary” the proposal details a reduction in offshore drilling rigs from 42 currently to 20 in December, while onshore rigs would go down from 43 to 29. Proposed reductions next year are steeper, with offshore rigs falling to 14 and onshore rigs down to just one by the end of 2021. The proposal does not appear to affect plans for some 20 priority Pemex development projects unveiled last year.

The private firms named in the document include London-based Seadrill, as well as prominent Mexican service providers Grupo R, and Perforadora Mexico, the oilfield service company of major miner and rail company Grupo Mexico. None of these firms immediately replied to requests for comment.

Rig suspensions at Ku Maloob Zaap would effectively scrap drilling new wells and repairing existing wells for the rest of this year, which would likely reduce output and cost some 5,000 lost jobs spread across several contractors, according to a source with knowledge of the proposal who requested anonymity to speak candidly. The drilling rig suspensions detailed in the Pemex planning document do not amount to outright contract cancellations.

The proposal calls for two of Seadrill's offshore rigs, West Courageous and West Intrepid, to be suspended from Ku Maloob Zaap for the remainder of this year. Three of the firm's other rigs are listed as suspended during the second half of 2021. Two of Grupo R's offshore rigs, Cantarell I and Cantarell II, are listed as suspended next year from August-December, and March-December, respectively. Meanwhile, four of Perforadora Mexico's six rigs would be affected by the proposed suspensions later this year or next year, with each rig idled for at least 10 months.

**Mexican daily oil output declines steeply in May – *CNH***

Mexico on average produced 1.64Mbd (million barrels per day) of oil in May, indicating compliance with the country's commitment in the OPEC+ agreement to reduce output by 100,000bd in May and June. From January-May, production averaged 1.71Mbd of oil.

Six months after AMLO and Pemex began touting a 2020 output approaching 2Mbd, Mexico is further away from that goal that it was at the start of the year. In May, Pemex produced almost 1.59Mbd of oil and the production from private contracts reached 124,200bd. The data give credence to the idea that Pemex has bigger operational problems. Among them, the company appears unable to expand to new camps to lift its output.

**CNH approves two exploratory wells in Veracruz to Pemex – *CNH***

CNH has approved Pemex to drill two wells in Veracruz:

- Kusum-1EXP will be in the Cuenca de Veracruz, part of the 740km² assignment AE-0125-Llave. It will cost USD $42.7 million and is part of PEP's development plan for the assignment approved by CNH in December 2019. It is a high temperature and high pressure well, 175°C and 15,646psi. Depths and drilling conditions will extend the time horizon and make it a relatively costly terrestrial exploratory well. PEP is scheduled to begin drilling on June 29 and to finish December 31, with final termination expected on February 14, 2021. Drilling will cost USD $35.5 million and termination USD $7.2 million. PEP estimates Kusum contains around 1.39Bboe, with a recovery rate of 31%.

- Tum-1EXP, an exploratory well in the assignment AE-0124-Llave. The well is also classified as high-temperature and high-pressure. PEP estimates Tum could yield 1.06Bboe, with a 20% recovery rate. Total costs will be USD $44.6 million, including USD $34.8 million on drilling and USD $9.8 million on termination. That is above the range prescribed for such a well, according to a recent set of CNH guidelines for commercially-viable well drilling. PEP explained the cost hikes on the basis of higher engineering costs and the weaker peso to the dollar.

**API seeks US intervention in Mexico discrimination against US fuel companies – *S&P Global***

The American Petroleum Institute has asked the US government to urge Mexico to uphold its commitments to the United States-Mexico-Canada Agreement and to stop discrimination against US companies in Mexico's fuel market. In the June 11 letter, API CEO Michael Sommers complained that US companies are facing new regulatory actions which undermine the framework that allows the continued trade flows and capital investments in energy between Mexico, the US and Canada and encourage the US "to use diplomatic channels to engage with the president of Mexico" to solve this issue. These regulations are either inconstantly applied or are inconsistent with past practice and include difficulties in getting permitting approval for new or rebranded fuel retail stations; arbitrary shutdowns at pumps for minor or non-existent infractions; new storage capacity requirements, and delays or rejections for gasoline and diesel import permits, Sommers said.

Mexico's Energy Regulatory Commission has "opaquely" removed asymmetric regulation applicable to Pemex which allows the state oil and gas firm "to unfairly and opaquely undercut the pricing of foreign competitors, giving the company a significant advantage in downstream pricing," Sommers said. The government actions likely contravene Mexico's commitments to national treatment investment protection in the investment chapters of both NAFTA and USMCA, Sommers said. They also likely contravene Mexico ́s commitment to non-discriminatory treatment in the state-owned enterprises and designated monopolies chapter of USCMA, with regards to state-owned Pemex, he said. The letter was sent to US Secretary of State Michael Pompeo; Commerce Secretary Wilbur Ross; Energy Secretary Dan Brouillette and US trade Representative Robert Lighthizer,

Neither API nor Pemex responded to requests for comment. The complaints by API members are in line with those by companies in other segments of the energy sector, like electricity generators and developers of pipeline infrastructure, which have voiced similar complaints regarding permits and regulations.

**CNH approves to Shell the modification to exploration plan – *CNH***

CNH approved permission to move forward with the exploratory plan by optioning a "maximum alternative scenario" that allows the company to expand upon its base scenario by drilling two more exploratory wells. One of them would begin in 4Q20. The 1,900 km² assignment, CNH-R02-L04-AP-PG06/2018, lies off the coast of Tamaulipas state, some 155 km from the city of Tampico. Shell won the assignment in the Round 2.4 auction held in 2018.

The plan implies that Shell will decide on its maximum scenario soon. Technical advisors explained that the wells “are not conditioned”: if Shell opts to pursue the maximum alternative scenario – a decision on which it would have to act by October – it will be two wells.

While Shell had expected to make total investments of USD $78 million over the next three years, based largely on two exploratory wells drilled in 2021, the alternative maximum scenario has it spending over USD $311 million, largely as a result of what would be four exploratory wells. While Shell’s plan is only an alternative, it continues to signal the firm’s appetite to explore Mexico’s oil-rich deep and ultra-deep offshore reserves. In 1H20, Shell launched the most aggressive ultra-deepwater campaign seen so far in Mexico. It began by spudding the Chibu-1 well, at a cost of more than USD $93 million and Max-1, at a cost approaching USD $91 million. Chevron is a partner in both ventures. In early June, Shell spokesperson Cynthia Babski confirmed that the Max-1EXP well had been wrapped up, not commenting further.

**CNH approves the modification to exploration to Pantera – *CNH***

CNH approved a modification plan that would allow special purpose operator Pantera to drill two to five delimiter wells – provided security concerns don’t stand in the way. The eight operational fields in the assignment include: Écatl, Fíton, Fósil, Granaditas, Ita, Pípila, Rusco and Ternero. The 440 km² area lies in the Burgos basin, a mature field in Tamaulipas state about 86 km south of Reynosa. Over the years, Pemex has drilled some 60 wells in the area, which is covered by both 2D and 3D seismic studies.

Pantera's base scenario includes a focus on evaluation of the Pípila and Rusco camps, with an eye toward drilling two shallow delimiter wells, Pípila-106DEL and Rusco-106DEL, and subsequent geophysical analysis of the two wells. An incremental scenario would see Pantera drilling three additional wells, Fósil-106DEL, Écatl-106DEL and Granaditas-106DEL, followed by well studies.

Pantera expects to find condensed gas, with a recovery rate of 83%. Costs of pursuing the incremental plan with its five delimiter wells would rise to USD $27.7 million over the next three years, as opposed to the two-well base plan costs of USD $10 million through 2022. The potential cost increase, almost USD $16 million, would come from drilling the extra wells in 4Q20. Under the modified plan, Pantera will drill Pípila-106DEL between September and October and Rusco-106DEL from October-December. If it pursues the incremental plan, it will drill the three additional wells in October and November.

### Renaissance oil founder frustrated by Mexico's ban on fracking – *Reuters*

The Mexican government's ban on the hydraulic fracturing of dense petroleum deposits known as fracking, as well as its decision to suspend oil auctions, has drained investor interest, the founder of Renaissance Oil told Reuters.

Ian Telfer, the former chairman of Goldcorp who in 2014 founded Canadian-based Renaissance Oil, noted that earlier this week the company announced it would begin to diversify away from Mexico's energy sector and had already begun seeking out new projects in the African nation of Botswana. "Put us down as very disappointed, very sad and disappointed that we've been forced to diversify by the changes and the policies in Mexico," said Telfer, a major Renaissance shareholder who said the company was initially formed with an exclusive focus on Mexican projects.

In 2017, Telfer sought aggressive expansion in Mexico including potential joint venture partnerships with Pemex after Renaissance won four oil contracts at auction two years earlier, as well as inking a separate tie-up with Russian producer Lukoil covering the onshore Amatitlan block in eastern Veracruz state. Moreover, AMLO's shift to a model that only offers oilfield service contracts to would-be Pemex partners has been another knock on the attractiveness of investments in Mexico's oil patch, said Telfer. "The government seems to prefer service contracts rather than equity interests, and for foreign investment, it only really works if we have equity interests," he said.

### Hokchi terminates Grupo R jack-up rig deal early – *Offshore Energy*

Hokchi Energy, a subsidiary of Argentina's Pan American Energy, has terminated the charter of Grupo R's jack-up rig Cantarell III earlier than originally planned.

Having arrived from Singapore earlier this year, the newbuild offshore drilling rig started drilling operations at the Hokchi field off the coast of the State of Tabasco in April 2020. However, the drilling contractor Grupo R said that, "due to changes in global oil and gas market conditions, on June 1, 2020, Hokchi Energy decided to notify GRP of Early Termination for Convenience." Grupo R said that the rig had been used to "repair" the Hokchi-4DEL (producer) and Hokchi-5DEL (injector) wells, prior to the contract termination notice." The Cantarell III jack-up rig was built at the Keppel Fels shipyard in Singapore. It is of KFels B-Class design with the capacity to drill in a water depth of up to 400 feet (122 meters) and up to 30,000 feet (9144 meters) of drilling depth. It has the capacity to accommodate up to 150 people.

**Pemex well falls short on priority fields promise – *El Economista***
CNH has revealed that Pemex falls short on 20 "priority" fields by 75%. In 1Q20, Pemex produced 21.8Mboed of the intended 89Mboed from 17 of the 20 fields that were put into production during 2019.

The company has only drilled five of the 15 wells that it set out to do between January and March of this year, while investing only 44% of the intended $11.82 billion pesos (USD $530 million) budget. Results are disappointing for the administration, which is a fierce defender and supporter of Pemex and has made the "rescue of sovereignty" its energy priority. Regarding drilling, Pemex is 8% ahead with just five of the 62 exploratory wells approved by 2020, in addition to 13 development wells in these fields.

## Power/Renewable Energy

**Iberdrola scraps $1.2 billion power project – *Bloomberg***
Spain's Iberdrola is canceling a project in Mexico to build a $1.2 billion combined-cycle plant because it can't secure a supply of natural gas, according to Mexican officials.

The mayor of Tuxpan, Juan Antonio Aguilar, said in an interview that representatives of Iberdrola told him that it's scrapping the project in his city because in nine months it hasn't been able to reach a supply agreement with the state utility, known as CFE. Hours later on Wednesday, Cuitlahuac Garcia, the governor of Veracruz, tweeted that the Energy Ministry told him the project will be left in the hands of the CFE. Tuxpan is located in Veracruz state. This would be the first major investment cancellation in the electricity sector since the administration of President AMLO announced new measures to limit private renewable energy production and prioritize the state utility. It wasn't clear whether the lack of a deal with the utility had to do with the government's position on private generation, or if it was related to AMLOS's recent public criticism of the company.

Iberdrola declined to comment on the matter and the public utility, known as CFE, as well as the Energy Ministry, didn't immediately respond to a request for comment. Iberdrola could restart the project if it strikes a deal over natural gas supply with the public utility, or with Transcanada Corp., in the next 15 days, Aguilar said. The company has already spent USD $40 million on permits and other expenses for the plant. In a June 12 press conference, AMLO said that Iberdrola is a monopoly in the power sector. He did not provide a breakdown, but CFE says it produces 54% of the nation's power.

The Tuxpan project was due to start construction next month and would have created about 2,000 jobs, he said. Reforma newspaper reported on the matter earlier. Garcia, the governor of Veracruz, said that the CFE would auction the construction of the plant, opening the door to local investors.

**Transmission Fee Hike Escalates Public-Private Battle – *El Financiero***
Mexico's CFE has hiked for transmission up to 800%. The rise in costs applies to 'legacy contracts', which are private energy projects finalized before the 2014 Energy Reform. The measure applies to fossil fuel-based energy generation, as well as renewable energy making use of cogeneration and wind. The hike comes two weeks after CRE's approval of a CFE request to increase transmission costs.

Even though CFE has not specified the start date, transmission costs are to change to the following: For high tension, the fees increase from MX$0.049 to MX$0.27857, an increase of 469%. Medium tension fees increase from MX$0.049 to MX$0.2586, which represents a 428% increase. Finally, low tension fees were hiked over 800%, from MX$0.09799 to MX$0.8928.

**Judge suspends SENER policy – *El Universal***
Federal judge indefinitely suspended SENER's policy that aimed to gain deeper control of Mexico's National Electric System. As soon as the policy was made public on May 15, the entity Defensa Collectiva (Collective Defense) requested an "amparo" (protection), which has now been made definitive until SENER challenges the decision. It is the second amparo won against SENER's measure; the first one was awarded in the beginning of June to GreenPeace.

The decision was made by judge Rodrigo de la Peza, who presides over the first Court specialized in economic matters and telecommunications. The definite suspension follows temporary suspensions and is considered a second step in a legal dispute that experts say could be resolved in months. De la Peza mentioned that establishing barriers for players seeking to generate clean energy did not go in line with existing provisions regarding free economic competition. SENER's policy was issued after CENACE's controversial measure to halt new renewable power plant tests needed to connect the projects to Mexico's grid. Intermittent renewable energy would further complicate power transmission, CENACE argued. SENER's policy expanded on the powers CENACE had at its disposal, aiming to increase tests and other entry barriers for new renewable energy projects. One of these barriers is related to location, which is how SENER hopes to achieve what it considers a healthier balance of renewable energy nationwide. The measure furthermore took stronger control of the National Electric System and aimed to favor CFE over private energy generators.