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Mexico's energy-sector reforms unlikely to hinder US natural gas export opportunities

By Jodi Shafto

Facing demand growth against production decline, Mexico is set to remain a major importer of natural gas, keeping opportunities wide open for U.S. exporting despite reformation of Mexico's own oil and natural gas industries.

Mexico began attempts to open its energy sector to private participation in the early 1990s, after closing outside participation to the oil and natural gas industries officially in the 1960s, when all hydrocarbon industries were incorporated into the state-owned PEMEX.

After several failed attempts at reform, the natural gas industry remained closed and reached a critical stage in 2011-2012, when insufficient supply from the southeast and a lack of infrastructure in the northeast and western Mexico resulted in a strained natural gas supply to feed the growing demand of the industrial sector that was experiencing an economic boom, Jose Maria Lujambio, an attorney with Cacheaux, Cavazos & Newton LLP said during a joint presentation with Platts/Bentek energy analyst Javier Diaz at the LDC Gas Forum Southeast in Atlanta on April 11.

New strides have been made to free Mexico's floundering energy sector from PEMEX control, but the bulk of the changes will impact the oil sector. Initial private investment is directed largely to offshore oil production, leaving the natural gas sector to continue to struggle amid growing demand and a shrinking supply.

Mexico's power sector is driving demand growth, increasing by 7% per year to 47% of Mexico's total natural gas consumption in 2015, Diaz said. Power consumption is closing in on industrial demand at 51%, while residential/commercial-sector demand is at only 2%. An additional 20 GW of generating capacity is expected to come on line over the next five years, including 4.8 GW in 2016, 3.3 GW in 2017, 6.2 GW in 2018, 2.7 GW in 2019 and 3.1 GW in 2020.

Gas-fired power demand growth will be limited by competing non-fossil capacity, Diaz said, as the government implements new rules, but natural gas capacity will make up the largest portion of the power stack through 2022.

Mexico faces the challenge of meeting that growing demand even as its natural gas production has been declining since 2010. The 24% drop in output since 2010 has increased the country's reliance on imports to feed its steadily growing appetite for the fuel.

By 2014, the U.S. provided 36% of the natural gas consumed in Mexico, an increase of about 2.9 Bcf/d, or a 45%, year over year, Diaz said.

Most of the production growth coming from the U.S. to feed demand across the Mexican border has come from the Northeastern U.S. and that trend is expected to continue over the next five years. "We expect North American gas production growth to top out at 5.3 Bcf/d by 2021, mostly coming from the U.S., with all of the U.S. production [growth] coming from the Northeast," Diaz said.

Looking at infrastructure, supply is clearly surpassing demand in the Northeast. The Northeast supply/demand imbalance creates a supply push from the Northeast. Canada, the Rockies and the Gulf Coast pipes will experience continued displacement, Diaz said. New infrastructure will be able to bring Northeast natural gas to growing demand areas by way of exports to Mexico and to global LNG markets.

"We see 4.5 Bcf/d of new [pipeline] capacity being built out through 2017 to bring natural gas to the Gulf Coast and Texas," Diaz said. Two Texas-to-Mexico border crossings will add 3.1 Bcf/d and 5 Bcf/d of capacity to the U.S.-Mexico border, with that supply being distributed into the Mexican market to serve demand in central Mexico.

Mexico has plans to improve its own ailing infrastructure with 18 new natural gas transportation projects on tap that would result in 10,000 kilometers of additional pipeline across Mexico by 2018, Lujambio said.

Much of this planned infrastructure is designed to increase U.S. imports, not to transport domestic production to demand centers, Diaz said.

Mexico continues work to reform its energy industries. After creating its energy regulatory commission known as CRE in 1993, and after failed efforts to reform the market through amendments to the Petroleum Law, a new CRE law and natural gas presidential rules in 1995, there was a paradigm change in December 2014 to a free-market model with state participation and regulation where needed.

Nine new laws were created and 12 laws were amended and put in force in August 2014. New presidential rules have been in force since November 2014, and dozens of administrative regulations from 2015 to 2016 are redesigning Mexico's oil and natural gas industry.

The process to open the oil and natural gas markets has been slow, however. Exploration and production opportunities failed to incite major interest. Round one in a bidding process for exploration state shallow waters production sharing contracts had 14 blocks offered with only nine participants and two contracts awarded. Round two offered five blocks with nine participants and three contracts awarded, round three for extraction state terrestrial license contracts offered 25 areas with 40 participants and all 25 contracts awarded, while round four for exploration state deep waters license contracts with 10 areas offered has yet to be determined.

Near-term, Mexico's natural gas production is forecast to remain flat, Diaz said. This will leave Mexico dependent on natural gas imports and U.S. natural gas will continue to look south.

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