Oil And Gas Is Under Attack In Latin America

By Nick Cunningham - Mar 08, 2018, 5:00 PM CST

“The energy reform has a lot of benefits to the country, to the people, so the worst case scenario in my point of view is that the speed that we are implementing the energy reform will be reduced,” the CEO of Mexico’s state-owned oil company, Pemex, told the CERAWeek Conference this week.

Carlos Trevino was referring to the upcoming presidential election in Mexico, in which the frontrunner, Andres Manuel Lopez Obrador (aka AMLO), has hinted that he might roll back the historic energy reform passed a few years ago that opened up the country's energy sector to the private sector. "Someone who doesn't believe in the energy reform may reduce the speed very much and I think that would be a shame in Mexico," Trevino said, clearly referring to AMLO.

AMLO was originally against the privatization effort, which has allowed the participation of international oil majors after decades of state-owned monopoly over energy. More recently, however, he has softened his tone, voicing skepticism rather than outright opposition. Still, AMLO says he will slow down the pace of auctions, perhaps halting them until "success" can be demonstrated from all of the offerings already awarded to international companies.

"There won't be new oil auctions until we assess the results delivered by the first auction," Rocio Nahle, a Congresswoman and expected pick to be AMLO's energy advisor, told the WSJ in a recent interview. But the AMLO administration would not cancel contracts as some in the oil industry fear. "Investors can be calm, we'll respect the law," she said.

According to Bloomberg, more than 90 contracts have been inked with companies such as Royal Dutch Shell, Chevron, ExxonMobil, Eni and others. The most attractive assets, as of now, are in Mexico's deepwater in the Gulf of Mexico. However, it will be several more years before the fruits of this effort can be realized, which raises questions about what the AMLO administration might do in the meantime.

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Pemex's Trevino says rolling back the energy liberalization would be "almost impossible because to change the energy reform you will need to change the constitution."

Still, AMLO could slow the effort and put an end to new auctions. Moreover, his administration has sent signals that it would focus on increasing downstream capacity while curtailing crude oil exports. Slumping refining output has forced the country to step up imports of gasoline and diesel. Public investment in refineries could reverse that trend, his campaign argues. "In a three-year period, at the latest, we need to try to consume our own fuels and not depend on foreign gasoline," Nahle told Reuters.

Ultimately, an AMLO election, as seems the most likely scenario at this point, raises a lot of questions in regards to what happens with Mexico's energy policy.

However, Mexico isn't the only country in Latin America that presents some political risk to oil and gas. A new report from Verisk Maplecroft says that Latin America's election "super-cycle" presents a series of potential obstacles for ongoing oil and gas development. Mexico may top the list, but voters are also heading to the polls in Colombia, Brazil and Venezuela this year.

A common thread that runs through all of these countries is a growing impatience on the part of voters with traditional establishment political parties. Unconventional candidates pledging to clean up corruption are resonating.

In Colombia, "[o]il output will continue to slip and new investment will dampen if the incoming administration fails to provide greater legal certainty surrounding permits," Verisk Maplecroft said. "Colombia's extractive sector has been under unusual stress over the last two years," the global risk firm said, pointing to environmental opposition to oil and gas drilling. A large number of candidates outside major political parties makes it difficult to predict the outcome.

Meanwhile, there is just as much uncertainty regarding the upcoming election in Brazil. The deeply unpopular current president is not running, while the candidate leading in the polls – former President Luiz Inacio Lula da Silva – might be barred from running. Verisk Maplecroft says that the oil and gas sector would face greater risk if Lula were to win. Absent his candidacy, his former environment minister Marina Silva could prevail, who has trumpeted a greater focus on renewable energy and environmental protection.

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Still, the risk in Brazil is lower compared to elsewhere. "We do not expect either of them to have the congressional support required to undo Temer's reforms," says Jimena Blanco, Head of Americas Research at Verisk Maplecroft. "Given the scale of the investment needed to fully develop the pre-salt, no government is likely to stray too far from the current trajectory."

No country presents more supply-side risk than Venezuela, where increasingly autocratic President Nicolas Maduro is hoping to kill off the last vestiges of democracy. He is expected to win out, despite the dramatic economic meltdown, although "[s]ocial turmoil could force the military to assume a caretaker role if things take a significant turn for the worse though," Verisk Maplecroft says.

The past few years have seen business-friendly governments court oil and gas companies in many parts of Latin America (aside from Venezuela), but the tide now seems to flowing in the other direction.

By Nick Cunningham of Oilprice.com

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