Mexico Farm-Outs A 'Game Changer'

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The success earlier this month of the first farm-out by Mexico's state-owned **Petroleos Mexicanos** (Pemex) for a deep Gulf of Mexico block has been a "game-changer" for the country's oil and gas reform, says a spokesman for a Canadian junior that is active in the country.

Kevin Smith, vice-president of business development for Calgary-based **Renaissance Oil Corp.**, which this past spring became the first private sector producer to operate in the country in 80 years, said the success of the farm-out bidding for the Trion deep offshore block has led to "a big change" in the country's oil and gas reform process. He said there will now be 168 farm-outs over the next two or three years.

The Trion farm-out, which took place on Dec. 4, at the same time as eight other deep Gulf of Mexico blocks were auctioned off to some of the world's largest producers, saw Australia oil and gas and mining giant **BHP Billiton** outbid Britain's **BP plc** to take a 60 per cent share in the block, in which Pemex will hold a 40 per cent share.

BHP Billiton offered US$624 million, along with a generous royalty pledge to the government and local work commitments, to develop Trion, which is located in the Perdido belt, near the U.S. border. Trion requires an investment of US$11 billion and could be producing 120,000 bbls daily by 2025.

Three other blocks in Perdido were also auctioned off that day, along with others in the country's south.

China's **CNOOC Ltd.** was the winner in bidding for two of the offshore Perdido blocks and is expected to spend billions developing them over the next few years.

Energy giants **Exxon Mobil Corporation** and partner **Total** won the bidding for another Perdido block.

But the Trion farm-out success seems to have opened the government's eyes about the opportunities for Pemex to partner with others.

The success of that farm-out has also convinced financially strapped Pemex that partnerships with the state-owned entity, which still controls about 80 per cent of the oil and gas resources in the country, hold more promise in the future than auctions of blocks. It had to divest of the rest of its holdings as part of the reform process which was launched in 2014. Renaissance won the bidding for four blocks in one of the four auctions that have been held so far.

Pemex, which has a debt of about US$100 billion, as well as pension obligations of US$70 billion, went through a series of significant management changes earlier this year, highlighted by the removal in February of chief executive **Emilio Lozoya**, who was replaced by **Jose Antonio Gonzalez Anaya**, a technocrat closely aligned with the Ministry of Finance.

On Dec. 3, prior to the Trion announcement, Pemex released a new business plan for 2017-2021 which is designed to return it to profitability by 2021. Among measures taken this year is a spending reduction of about 135 billion pesos.

Gonzales Anaya also announced plans to create joint ventures "along Pemex's entire value chain," which includes the downstream, midstream and upstream sectors.

He also revealed at the time Pemex would enter into joint ventures for shallow offshore fields, including Cantarell, once responsible for about 2.4 million bbls daily of production, but now is down to about 400,000 bbls daily, as well as dozens of other shallow and deep offshore blocks and land-based blocks.

In interviews last week with the Mexican media, **Pedro Joaquin Coldwell**, secretary of the Ministry of Energy, revealed just how significant a role farm-outs will play in the future.

He said that in the next six years Pemex will have 20 to 25 "strategic partnerships," adding that it would be "economic nonsense" to rely on the auction approach.

Coldwell said the country will still hold auctions, with one planned next March 22 for 15 shallow water blocks and another auction planned for June. He said the government will announce the timing of three more auctions early next year. However, he left no doubt that farm-outs will play a larger role in the future.

"(T)he success of Trion was fantastic," he said, adding that partnerships with Pemex will be the way of the future, since it leads to a sharing of the risk.

Smith, the Renaissance spokesperson, said the shift to a reliance on farm-outs represents "a very big change from Pemex."

He said the number of offshore and land-based blocks that will be offered starting next year represents a "transformation" of the reform process.

The 168 blocks being offered will encompass areas with billions of bbls of oil and trillions of cubic feet of natural gas, he said. They haven't all been identified yet, but it is clear "Pemex has realized they're no longer a monopoly and they need to have partners."

There will be 12 farm-outs offered next year and 156 in 2018, he said.

Smith said the Mexican government and Pemex seem determined to make the country one of the most attractive areas in the world for oil and gas development.

"They've realized there's a lot of capital that can be deployed from outside their borders," he said. "This is a game-changer."

He said Renaissance will likely be interested in most of the land-based opportunities that are offered by Pemex, especially those made available near its existing blocks, three of which are in the southern state of Chiapas and one in the highly prospective Tampico-Misantla Basin, close to the Chicontepec field, an unconventional reservoir with an estimated 139 million bbls of reserves. A farm-out opportunity in that field will be offered next year.

“A lot of what is being made available is in our geography,” he said. “We’re an established operator in Mexico (it produces about 800 barrels daily now in Chiapas, as well as natural gas) and this is excellent news for us.”

Steve Hanson, CEO of Vancouver and Calgary-based **International Frontier Resources Corp.**, which is partnered with Mexico petrochemical giant **Grupo Idesa S.A.** in Mexican-based **Tonalli Energia**, which also has a block in the Tampico-Misantla Basin, also welcomed the news of the farm-outs that will be offered.

“These large fields [being offered] have lots of potential, with solid existing production and extensive opportunities to infill drill and develop, as well as explore,” he said. “Regionally they are well-suited as we grow our footprint in Mexico. We will continue to evaluate these new opportunities, as well as the announced onshore bid rounds.”