08/12/2016 **Pemex farm-out plans hinge on ceding control of projects to bidders, sources say** - **Analysis**

Proprietary Intelligence

Story

- Control over new farm-out projects will be key for success
- Skepticism remains about local partne
- rNew reserve valuation rules a step forward

The success of **Pemex**'s planned offshore farm-outs will hinge on whether partners will be given complete control over the operation of projects, industry sources told Mergermarket.

The first projects announced, located in the extensively explored "Perdido" area of the Gulf of Mexico, are highly valued and have attracted interest from most deepwater exploration players, however, skepticism remains about how partners would work with Pemex, the sources agreed.

Two Mexico-based industry sources said corruption is still perceived at some levels of Pemex, which continues to behave like it did when it was a monopoly, trying to impose its conditions. Key personnel have left Pemex to form companies or join teams that are now competing against the company, leaving Pemex without the expertise to lead big projects, said the first Mexico-based source, who advises foreign and domestic clients on investments in energy.

Eduardo Rodriguez, founder and head of capital markets at **FlatStone Energy**, a Canada-based investment firm focused on sourcing, negotiating, funding and operating energy projects in Latin America, agreed with the first source and added that given its lack of expertise, Pemex must refrain from giving opinions and watch and learn from the companies who already have done it successfully.

Still, many international firms consider the current requirements of the authority "too high" and some of them have walked away from auctions, including last July when shallow water exploration opportunities awarded by the government went unclaimed, said Rodriguez, who closely follows developments in the country for his clients and has discussions from investment firms involved in the talk, and Ramses Pech, a partner at Mexico City based **Grupo Caraiva y Asociados**, an oil consultancy firm.

A National Hydrocarbons Commission (CNH) spokesperson did not respond to requests seeking comment. A Pemex IR officer declined to comment.

Further, there is the risk that Pemex goes bankrupt before the projects in the contracts are completed said the second source, who works at a law firm in Mexico and advises clients on oil and gas investments. Pemex had total debt of USD 87.3bn and Ebitda of USD 20.7bn in 2015, according to estimates by Barclays Capital. For 2016, its debt is projected to increase to USD 101.68bn and Ebitda to decrease to USD 15.55bn.

Pemex aims to announce farm-out winners in early December.

Trion, the field being farmed-out by Pemex, has been extensively explored by Pemex and others, and companies are now in the process of studying the terms and conditions to better understand the opportunities, said Oscar López-Velarde, a partner at consulting firm **EY** in Mexico City. The government is informing interested parties of the conditions little by little, and people should have all the elements to make an evaluation in the coming months, he said.

In seeking farmouts, Pemex plans to hold a 45% stake in the license to operate Trion while the remaining stake will be divided among at least two bidders. Operating companies are eligible to divide the entire remaining 55% ownership in any way, but financial investors will be limited to a 10% stake, as reported. **Exxon**, **Chevron**, **Total** and **Statoil**, as well as the Mexico-based subsidiary of **Petrobras**, are among the 26 companies that

Bidder	Statoil ASA	TS DS
Bidder	Chevron Corporation	TS DS
Bidder	Exxon Mobil Corporation	TS DS
Vendor	Pemex farm-out partnership opportunities	DS

Sectors	Energy
SubSectors	Oil and gas exploration and production
Topics	Analysis Joint Ventures/Partnerships Market Entry
Intel Type	Cross Border Regulatory issues
Countries	Mexico
Intel. Grade	Strong evidence
Intelligence ID	2284059

have commenced the fourth phase of prequalification, according to information published on CNH's website.

Pemex was a monopoly for over 70 years, and must resist the urge to influence the decision-making process in order to secure outside investment, said Pech.

Because of past corruption, the stripping of its monopoly status, and lack of budget, Pemex cannot operate and has no moral or ethical grounds to have a say in the execution, said Rodriguez. He said contracts for the farm-outs must be based on international standards like those found in Colombia, which replicated the Norwegian model. Pech agreed and stressed that potential Pemex partners will need complete control to develop the projects.

Reserve valuation rules key to funding

As Pemex's farmout process advances, CNH has initiated a procedure to revise Mexico's regulations on how it quantifies oil and gas reserves, a Mexico-based lawyer said. An announcement was made for this purpose at the Federal Gazette on 1st August.

What the authority is doing is opening the door to make the methodology to calculate reserves more transparent to the market, said Rodriguez. Valuation is key to finance projects; in Canada, the US and South Africa there are very clear standards which are not found in Mexico, he added.

The terms and conditions imposed by the government in the first round reflect certain amounts of reserves, but there is the chance that those reserves are lower, and then the price and the conditions could be subject to revision, he said. The authority is acknowledging that even though the model currently in place has worked in the past, a more expeditious and efficient process should be established for new operators that have signed exploration and extraction (E&E) contracts as a result of Mexico's Round One of exploration lease auctions in shallow waters and onshore, he said.

Such improvements will be discussed with a consulting board which will be formed in order to obtain the opinions from the operators and the industry. Once the revised regulation is ready, it will be submitted to the country´s Federal Commission on Regulatory Improvement (COFEMER). This is expected to happen before the year ends, the lawyer said.

by Sheky Espejo in Mexico City

Source Value	Proprietary Intelligence
Stake Value	N/A