NATURAL GAS — 18 Oct 2018 | 22:24 UTC — Mexico City

Gas shortages in southern Mexico to reach critical levels in November

Author **Daniel Rodriguez**
Editor **Gail Roberts**
Commodity **Natural Gas**

HIGHLIGHTS

LNG penalties lead to $21/MMBtu gas

Industrials seek return to regulated conditions

Mexico City — Gas shortages in southern Mexico will reach a critical point in November as Pemex natural gas production continues declining and users lack access to LNG terminals, industrial users in southern Mexico told S&P Global Platts on Thursday.

Pemex is not nominating gas for several industrial users in southern Mexico as a result of decreasing production, Cleantho de Paiva Leite, director for new businesses with Braskem Idesa, told Platts on the sidelines of the Mexican National Petrochemical Forum.

"The situation could lead to a complete stoppage of the industrial activity in southern Mexico," said de Paiva Leite, whose company operates the most polyethylene capacity in Mexico.

Pemex is allocating its diminishing gas output to fulfill the needs of its subsidiaries and power generators, a second petrochemical company in southern Mexico told Platts at the forum.

PIPELINE CONSTRAINTS

Gas shortages in southern Mexico have become more acute due to infrastructure constraints on gas flows into Coatzacoalcos, Veracruz, one of Mexico's largest petchem and industrial hubs, Paiva said.

This situation will be eased once the Mexican government completes the reconfiguration of the Cempoala compressor station in the state of Veracruz, which is expected to be completed in Q1 2019, according to Mexico's Energy Secretariat (SENER).

The only options for users in this situation is to shut down operations or consume gas without a nomination being sent to Pemex, which would result in steep penalties, Miguel Benedetto, general director of the Mexican

Association of the Petrochemical Industry (ANIQ), told Platts on the sidelines of the forum.

However, consuming gas under or above the nominated level leads to natural gas imbalances in the network that is addressed by system operator Cenagas via LNG injections, Benedetto said.

A large steelmaker in northern Mexico told Platts that some industrials with access to declining Pemex gas fields in northern Mexico also are resorting to taking gas from the system without nominations and incurring imbalance penalties.

Earlier this month, Mexico's business coordinating council, or CCE, told Platts that Pemex also is not delivering all the gas that is being nominated.

"It isn't a good signal. We are having gas supply problems," Roger Gonzalez, president of CCE's energy commission, told Platts. "The reduction has been limited, but this is decreasing system pressure and affecting industrial users' operations."

LNG PENALTIES

Cenagas charges for LNG at spot prices with a 50% penalty, which is hugely uncompetitive, he added. "So, choose how you want to die: by shutting down operations or paying $21/MMBtu gas," Benedetto said. LNG prices in Mexico are three to four times more expensive than continental gas imports.

Pemex, Braskem Idesa and INAQ told Platts that to address the current gas shortage the Mexican government must stop targeted LNG penalties to shippers and end-users and reverse deregulation to a situation in which all users share LNG costs.

Benedetto said the government needs to intervene because the imbalances on the system are a result of gas shortages due to declining Pemex production.

"Before when unbalances happened, LNG expenses were shared by everyone in Mexico, pushing gas prices to $4-$5/MMBtu. Now, we in the south pay gas at $20/MMBtu due to the new balancing regulation," Paiva said.

Recent data from SENER shows the gas demand in the petchem sector has been in free fall, reaching 214 MMcf/d in 2016 from 697 MMcf/d in 2013.

Pemex didn't immediately respond to requests for more information on the southern supply shortages. However, Carlos Trevino, Pemex's CEO, previously told Platts the country is facing irregularities in its gas supply. "Without a doubt, there is not enough gas to supply all the market demand including Pemex and its subsidiaries," Trevino said in an interview at the Mexican Petroleum Congress in Acapulco at the end of September.

REVERSING LIBERALIZATION

Benedetto said ANIQ wants Mexico's Energy Regulatory Commission (CRE) to reverse the liberalization of wholesale gas prices, known as first-hand gas sales or VPM.

CRE previously set the maximum price for gas to be sold by Pemex using a formula based on US prices. VPM prices were regulated under this formula at two hubs, Reynosa on the Mexico-Texas border and Ciudad Pemex in southern Mexico. The switch to free-market conditions was expected to provide Pemex and other independent producers the revenue to reverse the country's production declines.

Pemex's gas production has declined from more than 6 Bcf/d at the beginning of the decade to an average of 3.9 Bcf/d in 2018, SENER's data shows.

Benedetto said no open-market conditions exist today in southern Mexico, adding that lack of infrastructure to move gas south prevents new shippers from servicing users in this region, leaving a captive market under Pemex.

Pemex also isn't reacting to market incentives to boost production in southern Mexico although industrial users are being curtailed or are having to pay LNG gas prices, he added. The regulations anticipated a "competitive market that doesn't exist," Benedetto said.

Braskem Idesa's Paiva said that Mexico can't change overnight from a state monopoly to a free market without ensuring there is enough infrastructure and interconnections in the system. "This has to be an organized transition with the coordination of CRE, Cenagas, Pemex, and SENER," he added.

-- Daniel Rodriguez, **daniel.rodriguez@spglobal.com**

-- Edited by Gail Roberts, **newsdesk@spglobal.com**