

## Deconstructing Minister Coldwell

*Keynote speaker at the Baker Institute*

**P**EDRO JUAQUIN COLDWELL, 66, Mexico’s energy minister since 2012, was the keynote speaker at the conference on Mexico’s Energy Reform at Rice University’s Baker Institute on September 23, 2016. His presentation, delivered in Spanish and with slides in English, offered an overview of the new oil and power regimes that were created by the energy reform of 2013-14.

This report seeks insight about the engagement and responsibility of the minister in the design and articulation of the upstream energy reform. Matters relating to the power market and natural gas sector will be topics of future reports.

A close examination of his remarks and of his responses to questions from the audience yields insights about how his long career in public service helped prepare him to serve as energy minister. The examination also reveals blind spots and posturing.

In his remarks, he repeated the government’s familiar, number-driven explanation for an energy reform. He spoke about the past and future bid rounds. He characterized the Pemex Trion auction as a “farmout.” He said that he had expected Pemex’s existing risk-service contracts to be converted first to a standard contract model offered by the National Hydrocarbon Commission (CNH).

Asked about the durability of the energy reform were an opposition party were to win the presidency, he assured the audience that there were constitutional padlocks that would make it hard to reverse.

In the section of observations, we offer a critique of his presentation and raise questions about the role of the energy ministry in the energy reform and of the durability of the reform in future presidential administrations.

There is much that a new government could do that would imperil investment economics without changing laws or the constitution.

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### INTRODUCTION

**T**HE CONFERENCE AT RICE UNIVERSITY'S BAKER INSTITUTE that was held on September 23 was jointly sponsored by the Institute's Mexico Center and the law firm **Haynes and Boone, LLC**. The program featured Energy Minister Pedro Joaquín Coldwell as the keynote speaker.<sup>1</sup> Panelists from industry and government participated in discussions of the electricity reform, midstream gas and the upstream auctions of Round One.

#### Speaking Spanish

That the minister gave his presentation in Spanish would not mean that he did not speak conversational English; it would mean only that in formal situations he feels more comfortable in Spanish. Still, of the panelists from Mexico, he was the only one not to speak in English.

At the same time, any senior government official who feels discomfort in speaking in English to an international audience identifies himself as someone who came of age politically before the arrival of presidents with academic degrees from universities in the United States, beginning in 1982 with Miguel de la Madrid. The new, younger generation was cynically named "technocrats," with the implication that their knowledge was limited to books and lecture notes. Politicians who were monocultural and monolingual were termed "dinosaurs." By speaking in Spanish, the minister signaled that he belonged to an older political generation and mindset.

#### Numerology of the Energy Reform

The government's story about the reasons for the energy reform is one that is heavy with numbers. On the oil side, production had declined by such-and-such a level and prices had dropped from a high of \$102/bbl for the Mexican basket. Pemex, meanwhile, was falling behind in relation to the technology of deep water oil plays. The downward trends of both production (with low expectations for Pemex) and prices would be unsustainable in terms of public finances. These physical and economic conditions forced on the government a search for fresh capital from investors and technology via partnerships with Pemex.

On the power side, electricity prices in Mexico were significantly higher than those in the United States, even with government subsidies. Mexico was losing its competitive advantage of proximity to a global market by these high prices. To bring prices down, the government would update the strategy unveiled

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<sup>1</sup> The minister had previously addressed Houston audiences at CERA-WEEK.

in February of 1999 by the administration of Ernesto Zedillo (1994-2000). The strategy entailed creating a wholesale power market with an independent system operator (ISO) that, also, would be charged with the planning of the expansion of the grid.<sup>2</sup>

In short, the need for an energy reform may be seen solely by reference to the numbers. There would be no need to admit mistakes of strategy or implementation; it was as if the strategy and national narratives about the oil and power sectors had been correct all along, only the outcomes, owing to unexpected circumstances, were not those that had been predicted by the strategy.

## BACKGROUND

**N**ONE OF THE TOPICS that are briefly mentioned in this section was discussed during the conference at the Baker Institute. Some of the topics are quite familiar to some readers, but restating the obvious may lead to insights.

### **Pedro Joaquín Coldwell's Public Service**

As with everyone in Mexico, the starting point for an appreciation of a person's place in society is knowing the state or city in which he or she was born and raised. The minister is from Quintana Roo, a state located on the southern edge of the Yucatan peninsula. Cancun is three times closer to the capitals of Cuba and Belize than to Mexico City (300 vs 1,000 miles). Cancun is 1,300 miles from Medellin but only 500 miles further to Miami, a fact of geography and logistics well known to drug dealers.<sup>3</sup>

Cancun is a global tourist and conference destination, so public service, at age 29, as federal congressman from Quintana Roo, and, subsequently, governor of the state (1981-86), would prepare him to serve as minister of tourism (1990-93). From 1998-2000, he was Mexico's ambassador to Cuba.

During the PAN presidency of Felipe Calderón (2006-12), Senator Joaquín was chairman of the powerful Committee on Constitutional issues, and in 2012 became secretary general of the PRI (2012-13) and subsequently energy minister.

### **Mexico's populist oil and power narratives**

Mexico's civic culture is infused with a sense of injustice: some of it is systemic in relation to corruption, organized crime and the marginalization of indigenous peoples. The sense of injustice also applied to actors from abroad, beginning with Hernán Cortés and his army that decimated the political and religious lives of local populations. Centuries later, the perceived perfidy of Texan colonists, and the

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<sup>2</sup> Previously, the dispatching function was done internally by the federal power utility (CFE). As would be remarked by a panelist, the independence of the ISO is compromised by having the energy minister on its board of directors.

<sup>3</sup> A former governor of Quintana Roo, Mario Villarreal, is serving a sentence in U.S. federal prison for money laundering associated with commerce in illicit drugs.



### Additional reading



Year

s Chart

## 2016

Aug 24, 16	<b>Trión Auction: Problematic Issues</b>	816	11	0
<p>This report draws on our critiques of the government's bidding protocols for the three auctions of Round 1 held in 2015. The report identifies risks for the several stakeholders in the Trión auction: the government, Pemex and prospective bidders. In the second part of the discussion, we offer ideas for how to improve the process of partner selection.</p>				
Mar 22, 16	<b>Pemex E&amp;P organizes for Partnerships</b>	807	8	2
<p>This report focuses on the on the way that Pemex' Exploration &amp; Production (PEP) has been reorganized to give priority to partnerships with other oil companies. Table 1 displays the dozen-plus instances where farmouts are mentioned in PEP's Internal Statutes of July 3, 2015. Table 2 lists the names of executives, department heads and managers whose areas have farmout responsibilities.</p>				
Feb 18, 16	<b>Mexico's Upstream Reform in 2015</b>	803	6	6
<p>In this report, 26 elements of the Energy Reform of 2013-14 are selected for scoring on a 5-point scale of value creation, where 5 = strong value creation and 1 = severe value destruction. Each element is scored twice, once for political value, second for commercial value. With few exceptions, political values were higher than commercial ones for any given element of the energy reform. This discrepancy is interpreted as the principal reason why in the three bid rounds of 2015, no major American oil company chose to compete. Bid Round 1.4 is seen as the test of whether the government has taken corrective measures.</p>				

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## Additional reading

Year	Topic	File #	Pages	Chart
<b>2015</b>				
Dec 17, 15	<b>CNH Lease Auction 1.3: Jump-starting small oil producers in Mexico</b> With an expectation by the Energy Ministry that only 5 of 25 blocks would be awarded the third lease auction of petroleum blocks on December 15, it was an euphoric news that all 25 blocks had been awarded. The Hydrocarbon Commission (CNH) was praised for its efficiency in conducting a transparent process. This report looks at the process and outcome from the perspective of the members of the physical and online audiences: there were many places where there was unnecessary confusion. Table 1 lists bidders and winners in alphabetical order. Table 2 lists forced and unforced errors by CNH.	798	8	2
Aug 24, 15	<b>How Goes the Reform? - Report on the 3rd Forum on Energy Strategies</b> This report comments on the energy conference that took place in Mexico City on August 18, 2015, and organized by David Shields, publisher of <i>Energia a Debate</i> . The conference featured as speakers Energy Minister Coldwell and CNH President-Commissioner Juan Carlos Zepeda, plus upwards of a dozen panelists from SENER, CFE, CENAGAS and the private and social sectors. The two main speakers sought to put to rest concerns that the outcome of CNH's bid round on July 15th showed that the government was out of sync with the market.	790	6	2
Jul 28, 15	<b>What was Lost in Round 1.1: How government expectations were not met</b> This report itemizes what went well and what went badly in the seven-month process that culminated in the public auction for 14 exploration blocks that was administered by the Hydrocarbon Commission on July 15 (Tables 1 and 2). For the government, the outcome represented the penultimate worst-case scenario: the worst would have been had there been no bidders at all. We provide consideration for what alternatives could be adopted to minimize the risk of such an outcome happening in the future.	788	10	2
Apr 27, 15	<b>Ideological Constraints in Mexico's Bid Round One</b> In this report, we examine the ideological and political constraints that explain the rationale for the many points of unexpected misalignment between Mexico's new petroleum regime and standard conventions in other jurisdictions. Consider that the petroleum regime must be designed in such a way that it will not become a major campaign issue for populist parties in the general elections of 2018. For this reason alone the regime must give the impression of strict adherence to Mexico's traditional petroleum narrative.	781	9	3



## Additional reading

Year	Topic	File #	Pages	Chart
<b>2014</b>				
Dec 06, 14	<b>Mexico's Upstream Business Model: A Mineral Contract, not a Mineral Lease</b> This report seeks to gain clarity about the nature of the business model that is set forth in the Hydrocarbon Law by contrasting its features with that of a mineral lease in the U.S. and a mining concession in Mexico. The conclusion is that the State is NOT offering a mineral lease; instead, it is a new legal figure: mineral contract. Table 1 lists common terms in use in relation to a U.S. mineral lease (with Spanish translations). Table 2 shows how there are upwards of a half-dozen meanings of "Nación" in Mexico's legal framework.	100200	7	2
Sep 22, 14	<b>Post-Reform Blues: What does the Mexican Energy Reform mean in English?</b> This report observes that many of the concepts that are embraced in the 2014 energy reform have their roots in ideas that had first appeared in previous presidential administrations, for example, the idea proposed during the Fox administration that Pemex's board of directors should include executives from the private sector. The report identifies some dozen key terms that are found in the energy legislation that are either ambiguous or are tropicalized to give a unique Mexican significance.	772	9	1
Jun 06, 14	<b>Rethinking the Award of Exploration Blocks</b> This report asks about the nature of the biddable variable that the Finance Ministry (SHCP) is to provide for each public tender for an upstream block. A bidding criterion of "government-take" will not provide the broader results that the State requires. Instead, a multi-parametric bidding formula is needed to determine the global score of a bidder. The score reflects the weight given to the technical proposal of the bid, as well as the broad interest of the State in making an award of a block (e.g., acquiring subsurface data), as reflected by the fiscal terms offered.	100192	10	4



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