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## MEXICO

### Doubling Down on Fossil Fuels

Mexican President Andres Manuel Lopez Obrador's nationalistic energy policy of pumping up hydrocarbons production largely from state entities has raised concerns with global investors, but is also likely to complicate progress with the country's trajectory on the energy transition. The administration has seen myriad investor complaints over recent regulatory changes in the country's downstream and electricity sector, including massive tariff hikes to favor state-led entities, a turnaround from prior reforms that incentivized new players and renewables development. Observers also point out that climate change simply has not emerged as a priority for the populist leader, whose other marquee ambitions include improving the lot of the poor and stemming the tide of violence from organized crime.

"It may be surprising to some of us that a leftist government has been so antagonistic to the renewables industry," Francisco Monaldi, director of the Latin America Energy Program at Rice University's Baker Institute, said in a recent webinar, while adding that his hostility to foreign direct investment is perhaps more expected for a Latin American leftist. "He was raised in an oil-producing state and has a very traditional resource nationalist view that gives fossil fuels a prominent role in the development of the country." Meanwhile, he "is suspicious of the energy transition as something imposed by the countries to the north," Monaldi said.

Under predecessor President Enrique Pena Nieto, Mexico was seen as among Latin American countries taking the challenge of climate change more seriously. The country committed to cut greenhouse gas emissions by 22% by 2030 under the Paris Agreement, while its domestic climate change law also requires the oil and gas sector to make reductions of 14% by 2030. Its 2013 energy reform laid out a well-received framework for the construction of renewable energy power plants aimed at opening up the competitive playing field beyond the state-led utility, the Federal Electricity Commission (CFE).

Lopez Obrador, who successfully campaigned on calling out the global elites he believes have done little for ordinary Mexicans and sees the activities of private business as rife with corruption, saw those reforms as unfair and disadvantageous to the state. As such, the Energy Regulatory Commission (CRE) has made changes to the framework, including tariff hikes and dispatch rules, which determine prioritization for power sources

on the national grid. Both are seen by critics as giving preference to the state-led utility CFE at the expense of privately built renewables plants. Those measures have drawn legal challenges, with Mexico's Supreme Court recently siding with investors in at least one instance.

"The government ... just went into the regulations and said, what can we do to favor CFE and favor the traditional energy sources for CFE and undermine renewables," said Lisa Viscidi, director of the energy, climate change and extractive industries program at the Inter-American Dialogue. "It's going to be impossible for Mexico to meet the specific renewable energy portfolio targets that it's set, with the steps they've been taking."

CFE chief Manuel Bartlett has fired back over criticisms that the administration's policy is inherently against clean energy, citing anticorruption aims. "There is a whole media campaign when it is said that [changes] will affect the generation of clean energy, but no, the goal to is to battle corruption," he said this month.

Lopez Obrador is seen as unlikely to change his approach despite the criticism (EC Apr.17'20). And while slipping in the polls around the Covid-19 crisis, he still retains a strong base of support amid a fragmented opposition (p1). But a few bumps could lay ahead. "The regulatory changes pose meaningful risks to energy security and could inflict serious damage to the economy," the Eurasia Group wrote in a note, adding that combined with a lack of investment in the sector, they "could lead to power supply disruptions, and higher electricity costs."

#### Carbon Heavy

Similarly, the administration's hydrocarbons-focused policies would appear to have higher emissions as the natural result. Pumping up domestic fuels production from Pemex refineries to improve self-sufficiency has been a particular fixation for Lopez Obrador, although refining is a loss-maker for the company. Those facilities continue to produce large volumes of high-sulfur fuel oil, increasingly out of favor with international markets amid IMO 2020 regulations requiring sharp reductions in maritime fuel emissions. "It seems that CRE changed the regulations to fuel oil dispatch over intermittent renewables," Viscidi said, with part of the reason behind that "to find a market for Pemex's dirty fuel."

(continued on page 2)

## MEXICO (continued from 1)

On the upstream side, the Lopez Obrador administration has tasked Pemex with ramping up exploration and production efforts, including at 20 priority field development projects. Those actions have so far helped boost production modestly but contributed to a loss of more than \$20 billion in the first quarter of 2020 (EC Feb.28'20).

The company has already acknowledged that the policy change played a role in an emissions footprint that was reported to be more than 30% higher in 2019 than 2018. In its annual report to the US Securities and Exchange Commission, Pemex disclosed 2019 emissions of 48 million tons of carbon dioxide, which the company said was a 3% annual increase after it implemented an “updated methodology” to increase certainty and adjust to legal requirements. But the numbers showed a larger shift: The 2018 figure prior to the adjustment was 36.5 million tons, which had been a 5.5% drop from 2017. ■

Kathrine Schmidt, Houston

## I Compass Points

- **SIGNIFICANCE:** Mexico will struggle to meet its emissions goals on the books for climate change while Lopez Obrador pushes a hydrocarbons-focused energy policy that largely ignores the issue, complicating the country's path through the energy transition.
- **CONTEXT:** Lopez Obrador's distrust of the private sector when it comes to electricity and renewables projects and limitations of state-led companies may make it difficult to fulfill the administration's goals of providing stable, secure and affordable energy supplies.
- **NEXT:** Watch to see how much traction is gained by legal challenges to electricity sector rules, and whether Lopez Obrador will attempt broader policy changes such as trying to alter energy reforms enshrined in the country's constitution.