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Mexico Eyes Rapid Development of Gas Industry

Arguably the most striking aspect of the first US-Mexico Natural Gas Forum last week in San Antonio is the unmistakable enthusiasm of Mexico's energy regulators and top officials for developing a natural gas sector mirroring that in the US and Canada.

And they didn't speak of decades of effort, but of how the pieces are falling into place to transform a once-moribund industry within the next five years.

The US side of this equation is well known. By early this year, US pipelines had the capacity to deliver 7.3 billion cubic feet of gas per day into Mexico, with flows on the order of 4 Bcf/d and rising.

With associated gas production ballooning in the Permian Basin, three pipelines from Waha to northwestern Mexico have been built that together have 3 Bcf/d of export capacity, according to RBN Energy analyst Jason Ferguson. Yet together, Roadrunner and Comanche Trail are flowing less than 200 million cubic feet of gas per day south of the border, while the Trans-Pecos Pipeline has yet to start moving gas.

Why? Mainly because the energy infrastructure in Mexico hasn't caught up.

In northeastern Mexico, five pipelines are nearing completion with a combined capacity of around 3.8 Bcf/d, Ferguson said. They will serve four major power plants that will come on line in 2017-19. And the picture is much the same throughout the country, said Guillermo Turrent, CEO of CFEnergia, the national power grid operator.

Private firms have been in the process of adding almost 4,000 miles of new pipeline to Mexico's original 7,000-mile state-owned network, an effort that will prove transformational when the grid is fully operational by the end of next year, Turrent said.

Not only will it feed a growing fleet of power plants, but it will bring gas to new areas and build in needed supply redundancy in areas where gas is now available from a single source, Turrent explained. The newly enhanced pipeline grid will also have ample spare capacity -- a radical departure from decades of deficit -- which will encourage gas growth by giving end-users confidence in supply.

Critical to the effort will be pipelines from northwestern Mexico able to bring more than 3 Bcf/d of Permian supply to the populous central Mexico market. Pipes are also coming on line next year that could draw in another 3 Bcf/d across the border from South Texas.

But increased pipeline capacity alone will not take Mexico's gas sector from a former monopoly to the free market to which the company's leaders aspire. The development of a robust system for trading point-to-point pipeline capacity, as well as for pricing the gas moving on the enlarged grid, is essential. There are also practical concerns, such as an absence of gas storage in the country.

The creation of price hubs within Mexico's 14 market regions is the ultimate goal, because a robust market needs strong price signals to draw gas where it is needed, Turrent said. But the process is only just beginning.

Today, Mexico's gas supply is normally priced off liquid US hubs, such as Waha, Agua Dulce, Henry Hub and mainly the Houston Ship Channel (HSC). Mexico only recently eliminated "first hand sales," a regulated initial price for which state-owned Pemex had to transact deals. For instance, gas bought from the US Southeast was set at HSC minus 20¢.

But Southeast gas was rarely if ever available at that price, Turrent said, so "it was a very good step."

Another important move in this process occurred late last week, when the Comision Reguladora de Energia (CRE) -- Mexico's version of the US Federal Energy Regulatory Commission -- was to begin publishing a monthly price for gas sold in Mexico.

Ruben Rodriguez, CRE general director for natural gas analysis, told *Natural Gas Week* on the sidelines of the three-day conference that it will be based on a weighted average price for all reported transactions, which is mandatory in Mexico. As fixed-price trading becomes more robust, daily price data will eventually be released for different regions, he said.

The lack of storage capacity is also being addressed, said Rosanety Barrios, the Ministry of Energy's head of Industrial Transformation. Regulators plan to release a draft policy regarding gas storage in early September, which will begin a period of regulatory review and consultation with the private sector.

Barrios told NGW that creating a storage facility in Mexico is now next to impossible as the laws governing the sector not only fail to address how storage projects are regulated, but they could be seen as sabotaging them. For instance, current law as written could require that base gas within a cavern be produced and sold, which defeats the purpose**,** she said.

But building indigenous storage may not be critical to initial sector reforms, conference panelists said. Not only are large storage assets available to Mexico in the US border regions, but its three LNG import facilities that will soon be relegated to emergency use. The terminals can store billions of cubic feet of gas even if their import function is idled, and two are strategically located to serve a growing central Mexico market -- Altamira LNG on the Atlantic coast and Manzanillo LNG on the Pacific coast.

"There will be no need for LNG," Turrent said, noting that once the pipeline grid is in place, interconnectivity with the US will triple and the nation's gas deficit will be eliminated.

Tom Haywood, Houston