

## Round 2.4 – Another successful auction outcome with 66% of fields allocated

- The *National Hydrocarbon Commission* (CNH) announced the winners of Round 2.4
- This round contemplated 29 deep-water fields in the Gulf of Mexico, spanning a surface of 41,276 sq. miles
- Out of the 29 fields tendered, 19 were allocated (66%), nearing the 69.5% historical average and standing significantly above the government's own expectation (~24%)
- We consider that the allocation was highly successful, showing a continuing interest of companies in the development the Mexican energy sector
- The next step in the allocation process will be Round 3.1, which will take place on March 27, and it will include 35 fields in shallow waters in the zones of Burgos, Tampico-Misantla-Veracruz and the Southeastern Basin
- The result of the today's auction is another example of how well the energy reform has been implemented, which also does not reflect any concern about the electoral process that Mexico will hold next July
- Crude oil prices have recovered substantially, although we believe that room for further appreciation is limited

**Round 2.4.** The *National Hydrocarbon Commission* (CNH) announced the winners of the fourth tender under the so-called Round 2 (a.k.a. Round 2.4). We highlight that this round represents the eighth effort by the government to allow private-sector investments to invest in full-blown oil-related projects. Nineteen bidders came forth, 4 being individual companies and 15 associations between 2 or more companies. All 19 took part in the final process and 11 won a contract. This group of projects included 29 production blocks in shallow water fields, which covered a total area of 66,427 km<sup>2</sup> (41,276 sq. miles). Nine are located in the shores of Tamaulipas in an area known as *Cinturón Plegado Pérdido*. Ten other areas are located in coasts of Veracruz, known as *Cordilleras Mexicanas*. Finally, the other ten fields are in Tabasco and in the southern coasts of Veracruz, also known as *Cuenca Salina* (as shown in the map on the following page). According to the Ministry of Energy, these zones mainly contain hydrocarbons such as oil as well as dry and wet gas.

**Excellent allocation.** It should be noted that in Round 2.4, 66% of the possible blocks were assigned, where we highlight that Shell, either in a consortium or individually, got 9 assignments. It also highlights the participation of Qatar Petroleum that participated in 5 contracts. For its part, Pemex had 4 blocks, 2 in a consortium and 2 individually.

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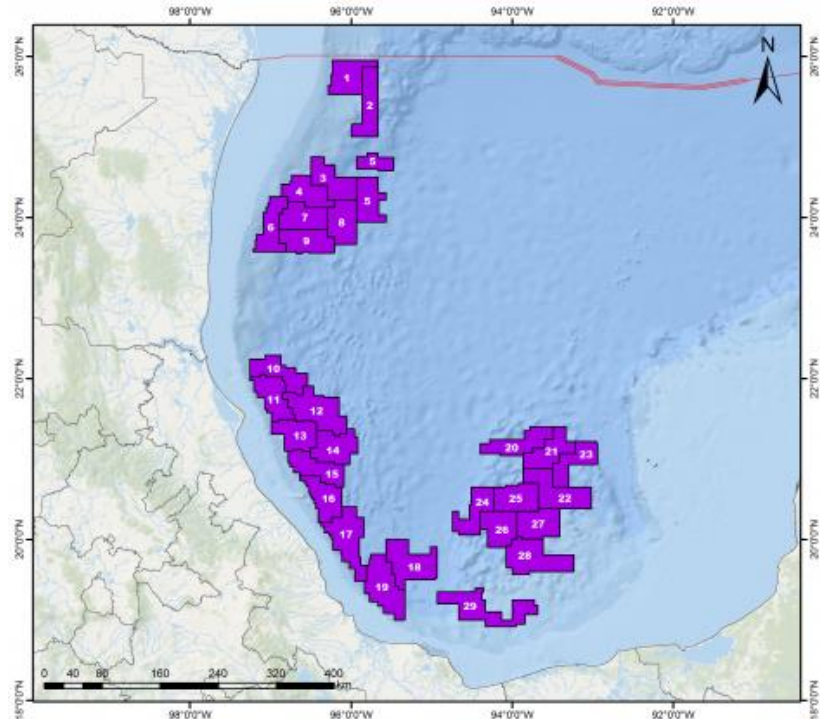
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This result was higher than the one expected by the Federal Government, who expected an allocation of around 24% due to the difficulty involved in the development of projects in deep waters. In this sense, we consider that the success achieved in this round continues to reflect the interest from companies to continue investing in this type of projects in Mexico. The result of the auction today is another example of how well the energy reform has been implemented, which also does not reflect any concern about the electoral process that Mexico will hold next July.

#### Blocks tendered in Round 2.4



Source: National Hydrocarbon Commission

#### Allocations of Round 2.4 (1/2)

Area	Surface (sq. mi.)	Hydrocarbon to exploit	Bidder	Country of origin	Government's additional profit margin (%)	Additional investment factor	Weighted value of the economic proposal
1. Cinturón plegado perdido	1,235	Oil	Deserted				
2. Cinturón plegado perdido	1,333	Oil	Shell and Pemex	Netherlands and México	15.02	1.0	80.789
3. Cinturón plegado perdido	1,281	Oil	Shell and Qatar	Netherlands and Qatar	10.03	0.0	40.120
4. Cinturón plegado perdido	1,181	Oil	Shell and Qatar	Netherlands and Qatar	10.03	1.0	58.533
5. Cinturón plegado perdido	1,698	Oil	Pemex	Mexico	6.23	1.0	41.585
6. Cinturón plegado perdido	1,175	Oil and dry gas	Shell and Qatar	Netherlands and Qatar	20.00	1.5	114.500
7. Cinturón plegado perdido	1,223	Oil and wet gas	Shell and Qatar	Netherlands and Qatar	20.00	1.5	114.500
8. Cinturón plegado perdido	1,281	Wet gas	Deserted				
9. Cinturón plegado perdido	1,248	Oil	Deserted				

Source: National Hydrocarbon Commission

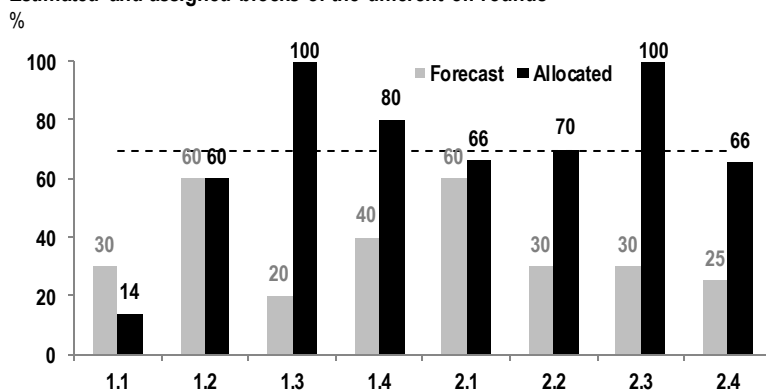
### Allocations of Round 2.4 (2/2)

Area	Surface (sq. mi.)	Hydrocarbon to exploit	Bidder	Country of origin	Government's additional profit margin (%)	Additional investment factor	Weighted value of the economic proposal
10. Cordilleras mexicanas	1,242	Oil, wet and dry gas	Repsol, PC Carigali and Ophir	Spain, Malaysia and UK	20.00	1.5	114.500
11. Cordilleras mexicanas	1,244	Oil, wet and dry gas	Deserted				
12. Cordilleras mexicanas	1,926	Dry gas	PC Carigali, Ophir and PTTEP	Malaysia, UK and Thailand	20.00	1.0	103.000
13. Cordilleras mexicanas	1,222	Oil	Deserted				
14. Cordilleras mexicanas	1,393	Wet and dry gas	Repsol and PC Carigali	Spain and Malaysia	19.98	0.0	79.920
15. Cordilleras mexicanas	1,269	Wet gas	Deserted				
16. Cordilleras mexicanas	1,272	Oil and dry gas	Deserted				
17. Cordilleras mexicanas	1,870	Dry gas	Deserted				
18. Cordilleras mexicanas	1,813	Wet and dry gas	Pemex	Mexico	7.11	1.0	45.510
19. Cordilleras mexicanas	1,866	Dry gas	Deserted				
20. Cuenca salina	1,292	Oil	Shell	Netherlands	20	1.5	114.500
21. Cuenca salina	1,261	Oil	Shell	Netherlands	20	1.5	114.500
22. Cuenca salina	1,789	Oil	Chevron, Pemex and Inpex	US, Mexico and Japan	18.44	1.0	96.042
23. Cuenca salina	1,151	Oil	Shell	Netherlands	10.08	1.0	58.756
24. Cuenca salina	1,194	Wet gas	Eni and Qatar Petroleum	Italy and Qatar	9.53	1.0	56.303
25. Cuenca salina	1,309	Oil	PC Carigali	Malaysia	19.98	0.0	79.920
26. Cuenca salina	1,261	Oil	PC Carigali	Malaysia	20	1.0	103.000
27. Cuenca salina	1,316	Oil	Desierto				
28. Cuenca salina	1,906	Oil	Shell	Netherlands	20	1.5	114.500
29. Cuenca salina	2,022	Oil and wet gas	Repsol, PC Carigali, Sierra Nevada and PTTEP	Spain, Malaysia, Mexico, Thailand	20	1.5	114.500

Source: National Hydrocarbon Commission

**Continuing success in oil field auctions.** The bidding process for the oil rounds has had an average allocation of 69%, while the last round allocated 66%. It should be noted that round 1.3 and 2.3 have been the most successful, having allocated 100% of the blocks, as shown in the following graph.

**Estimated and assigned blocks of the different oil rounds**



Source: Banorte, National Hydrocarbon Commission

**Round 3.1 will take place on March 27.** It will involve 35 shallow water fields, of which 11 are set in the *Burgos* basin –in the coasts of Tamaulipas–, 13 are located the region known as Tampico-Misantla-Veracruz in the coasts of Veracruz. Finally, the remaining 8 are situated in the Southeastern Basin –in the coasts of Veracruz, Tabasco and Campeche–.

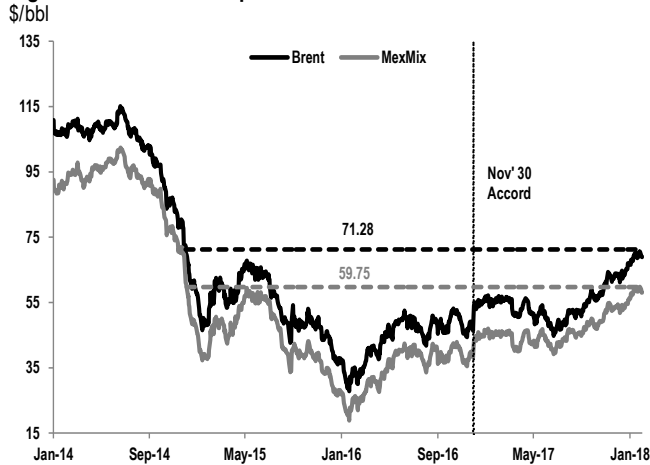
*From our fixed income and FX strategy team*

**Crude oil prices have recovered substantially, although we believe that room for further appreciation is limited.** Oil is scoring this month its strongest start for a year since 2013, with global benchmarks at their highest since prices collapsed in 2014 (see Figure 1). Specifically, a week ago Brent was touching a maximum of 71.28 \$/bbl and WTI of 66.66 \$/bbl. In this sense, January’s rally will print at 3.1% and 6.6%, respectively. This recovery is mainly explained by the combination of two factors: (1) The effect from the [supply cut agreement](#) led by OPEC and Russia; and (2) robust global consumption dynamics in 2017, with trading in recent weeks supported by the prevailing narrative of synchronized growth along a meaningful depreciation of the USD.

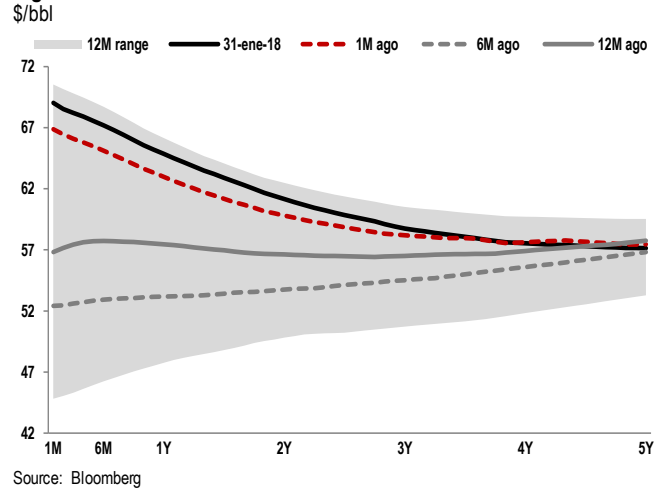
As depicted in Figure 2, the futures curve is currently trading in backwardation, which means that front-end prices are higher than longer tenors, contrary to what happened a year ago or in earlier periods. The change in the curve’s shape is consistent with global inventories depleting due to the success of the supply pact, occurring in parallel with healthier world demand. Moreover, this is relatively more convenient for OPEC producers than U.S. shale. In particular, these low-cost producers have the opportunity of selling their output at higher prices as most of their transactions are in the spot market. Simultaneously, the relative incentive to increase production for high-cost participants (particularly U.S. shale) becomes weaker if the curve’s slope becomes increasingly negative. This is driven by the fact that a greater proportion of their sales are hedged through futures markets, with the latter allowing them to access financing at more competitive rates. In this sense the curve’s structure is a key driver.

Additionally, besides signaling a tighter relationship between demand and supply, it is a more attractive setup for speculative and/or purely financial participants as it implies a positive carry and roll-down (given that that futures trade lower than the spot price). As result, this situation has been reflected in spec positions, recently breaching all-time highs in terms on net longs.

**Fig. 1 Brent and MexMix performance**



**Fig. 2 Brent futures curve**



Going forward, it is our take that prices are more likely to show a downward correction in coming months than to extend the recent rally. The latter is mainly because of the high probability that inventory dynamics begin to deteriorate and that, considering the imminent reactivation of higher-cost production, supply and demand balances could decouple again in an actual context of a moderate deficit. To this situation it is also important to add that OPEC and its allies are likely to acknowledge an exit strategy for their current agreement, a process in which very high compliance levels seen in the past could lessen. Despite these, we do not expect a violent fall in prices nor substantially lower levels due to a stronger outlook for aggregate demand, as evidenced by strengthening PMIs, upward revisions for economic growth and favorable consumption expectations. In this sense, we expect an average price for Brent this year between 59 and 65 \$/bbl, closing 2018 at the higher end of the range but below the current level of 69 \$/bbl.

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