The Political Economy of Energy Reform in Mexico

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Outline

- History: 1879 to 1990
- Partial Reforms: 1991 to 1999
- The Evolving Agenda: 2000 to . .
- Conclusions

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History: 1879 to 1990

- 1879: first thermoelectric generation plant
- 1889: first hydro generation plant
- 1979-1900: lucrative concessions
- 1920s: vertically integrated monopolies
  - wealthiest and most industrialized areas

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History: 1879 to 1990

- **1926: Codigo Nacional Electrico**
  - Changed the Constitution: public service
  - Congress: legislate in related matters

- **1934: Comision Federal de Electricidad**
  - operate as a regulatory agency and liaison between foreign companies and government
  - supply electric service to those areas considered by private companies as not profitable

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History: 1879 to 1990

President Lázaro Cárdenas consolidated power around his party, the PRI
  - Key strength: Unions
    - Sindicato Mexicano de Electricistas

Late 1930s: PRI was firmly in control
  - Land reform
  - Nationalization
  - 1938: Electricity Public Service Act

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History: 1879 to 1990

- 1937 to 1943: low private investment
- Nationalization Process:
  - 1944: CFE acquired Chapala
  - 1940’s and 1950’s: CFE acquired hundreds of regional electricity monopolies
  - 1960: Federal Government acquired *Impulsora* and *Mexican*
    - Creation of LFC

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History: 1879 to 1990

- 1960: Government formalized the arrangement with a constitutional amendment (Article 27, paragraph 6)
- 1960s and 1970s
  - Nationalization
  - Import substitution strategy

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History: 1879 to 1990

1975: Consolidation with the *Ley del Servicio Publico de Energia Electrica* (LSPEE) which declared CFE and LFC as public suppliers of electricity
- CFE and LFC
  - Government offices
  - Host some of the strongest of the nation’s unions
    - Key elements of the PRI power base

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History: 1879 to 1990

Performance of the System
- 1970s: Growth in Installed capacity
- Oil and hydroelectricity
  - Preference for fuel oil
    - PEMEX sold fuel oil to the power sector at around 30% of its opportunity cost
    - Implicit subsidy: USD $1.5 billion a year
  - Tariffs were set below their opportunity cost
    - Deficit around 2.4% of GDP
  - Access to electricity more than doubled

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History: 1879 to 1990

- 1982: Default on external debt
  - Tight fiscal controls
  - Dismantled the import substitution strategy
  - Integration into the world economy
  - Reduction of the role of the state in the local economy

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History: 1879 to 1990

- Electricity and Oil escaped privatization
  - Electricity: drain
  - Oil: source of revenue

- Evidence of key political and constitutional factors at work

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Partial Reforms: 1991 to 1999

- 1992: NAFTA
- 1994: World Trade Organization
- 1997: PRI lost its majority in Congress

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Partial Reforms: 1991 to 1999

- 1992: Amendments to *Ley del Servicio Publico de Energia Electrica* (LSPEE)
  - Allow private participation under different schemes such as Independent Power Production, Cogeneration and Self Supply
    - 1997: First tender (Merida III)

- 1995: Reforms to the Public Debt and the Budget Laws
  - PIDIREGAS
    - June 2003: debt for CFE USD $4.3 billion

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Partial Reforms: 1991 to 1999

1990s: Changes in fuel prices and tariffs
- Tariffs appear still to be at a level below cost
- Net subsidy of USD $5 billion a year
  - Residential: 64.1%
  - Industrial: 17.9%
  - Agriculture: 11%
  - Commercial: 5.3%
- Residential tariffs could be 3% of GDP

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Partial Reforms: 1991 to 1999

Politics: Extremely difficult to raise residential and agricultural tariffs
   - Unions: SME (LFC) and SUTERM (CFE)
   - Leftist PRD
   - Leftist wing of the PRI
   - Some other social organizations and unions

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Partial Reforms: 1991 to 1999

- 1993: Comision Reguladora de Energia
- 1995: Ley de la Comision Reguladora de Energia
  - An autonomous agency in charge of regulating the natural gas and electricity industries
- 1999: President Zedillo proposed structural reforms that would have modified the constitution

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The Evolving Agenda: 2000 to . . .

- September 2000: “shadow market”
- May 2001: President Vincente Fox proposed further reforms to Articles 126 and 135 of the LSPEE
  - Terms and limits of the self-generation and cogeneration

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The Evolving Agenda: 2000 to . .

- 2002: The Mexican Supreme Court ruled that the 1992 law might be unconstitutional

- A myriad of proposals has induced madness in the public opinion
  - Evolution of Tariffs

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Greatest Challenges: Public Opinion

- 2002: poll conducted by Coordinacion de Estudios de Opinion
  - 36% think Fox’s proposal is about privatizing the power sector
  - 5% mention attracting private investment
  - 35% opposed private investment
  - 17% supported new private funds in the industry
  - 49% consider having electricity problems
  - 33% think that high prices as the main problem in the sector
  - 14% said that the quality of electric service was bad
  - 33% said that service quality is good.

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Conclusions

Time is running . . .

Sector is running out of steam . . .

Nothing happens . . .

Unless SOMETHING takes place TODAY