The Trump Effect on Foreign Direct Investment (FDI): Alternative Scenarios Involving the Mexican and U.S. Oil and Gas Industries

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Mexico's Energy Reform of December 2013 was designed to completely revamp its fossil fuel sector. Under this action several constitutional amendments were enacted in order to open up the hydrocarbon and power sectors to private and, most importantly, foreign investment (Alpizar-Castro and Rodriguez Monroy, 2017). This historic breakthrough is significant given that since the late 1930's (in the case of oil) and the 1950's (in the case of power), only Mexican public capital was allowed into these industries. Now, new arrangements such as profit and production sharing contracts may be enacted, as well as joint licenses for exploration and production.

These reforms were passed, among other things, under the expectation that there would be a robust trading relationship between the U.S. and Mexico, and the ultimate success of this energy reform relies strongly on the unimpeded flow of foreign capital into the oil and gas sector. In 2016 energy accounted for 9% U.S. exports to Mexico, and 3% U.S. imports from Mexico (EIA, 2017). U.S. natural gas exports doubled between 2009 and 2016, mostly due to increasing exports to Mexico (EIA, 2016). As part of the Reform, there are plans to further develop the natural gas pipeline network, including an underwater pipeline through the Gulf of Mexico. The expansion of the network may double the pipeline natural gas exporting capacity of the U.S. to Mexico (EIA, 2017).

Recent political changes in the U.S., however, have cast considerable uncertainty on this whole enterprise. In the wake of pressure from the new U.S. administration in the form of punitive threats, Ford, Carrier, and General Motors have all decided to shift their new investments to the U.S. The automotive industry would seem to be the initial target of the administration's new trade policy, but a report from the Institute of Finance International (2017) indicates that overall U.S. investment in Mexico in 2017 may be trimmed by over 40% to $13 billion this year, the lowest in five years and the highest drop in percentage terms. While such cutbacks would most certainly affect thousands of manufacturing jobs, its implications for the fossil fuel industry remain clouded in uncertainty, both in the short and the long run.

At the present time it would seem that the Trump Administration is not inclined to curb foreign investments by U.S. oil and gas corporations. The public perception of foreign activities by fossil fuel interests is quite different than those of manufacturing firms, especially when they involve cutbacks in domestic manufacturing jobs. Indeed the fossil fuel industry has been given virtual "carte blanch" with respect to its activities, and during the first month in office Trump repealed a Securities and Exchange (SEC) rule (under the 2010 Dodd-Frank financial reform) that required energy companies to disclose their payments to foreign governments.

That being said, however, fossil fuels themselves could still be subject to tariffs or quotas as part of an overarching U.S. protectionist policy directed towards Mexico. If such policies were to be implemented, there could be a significant downside for Mexican energy production. In exploration and production, for instance, 39 contracts have been or will soon be signed between the Mexican Government and private companies, both national and international. Potential investments for the next 10 years are estimated in more than 41 billion U.S. dollars. A significant fraction of these investments will come from 6 U.S. oil and gas companies that were awarded contracts in the first round of tendering processes. The results of a simulation we conducted using a computable general equilibrium (CGE) model of Mexico indicates that under a U.S. protectionist policy Mexican petroleum production could be seriously curtailed, leading to lower investment, a decline in economic growth, and a loss in consumer welfare.

Over the longer term, other factors may also conspire to negatively impact FDI in the Mexican petroleum sector. The positive signals that the Trump Administration has given to resume controversial Canadian pipeline construction and accelerated exploration and drilling on the U.S. public lands may seriously dampen the interest that American oil and gas companies have in future joint ventures in Mexico. If this were to happen, then Mexico would be forced to seek FDI from other sources such as companies in Europe and Asia. While joint ventures with such companies would certainly be viable, they may not prove to be as efficient as partnering with U.S. firms since (1) they lack the geographical proximity of U.S.-based firms, and (2) they may not have ready access to the vast physical and financial capital reserves that large corporations in the U.S. typically enjoy. Finally, since most of the natural gas fields in question are located in the north of Mexico, much of the appeal for their development lies in the possibility of a pipeline linkup with the United States. Thus, uncertainty about the ongoing economic relationship between the U.S. and Mexico may have a chilling impact on long run FDI in Mexico's fossil fuel sector, regardless of the source of foreign capital.

References:

Alpizar-Castro, I. and Rodríguez-Monroy, C. (2016), Review of Mexico´s energy reform in 2013; Background, analysis of the reform and reactions, Renewable and Sustainable Energy Reviews, 28, 725-736.

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EIA (2016), U.S. natural gas exports to Mexico continue to grow. November 29, 2016.

EIA (2017), U.S. energy trade with Mexico: U.S. export value more than twice import value in 2016. February 9, 2017.

IAEE/Affiliate Master Calendar of Events

(Note: All conferences are presented in English unless otherwise noted)

Date	Event, Event Title and Language	Location	Supporting Organization(s)	Contact
2017				
June 18-21	40th IAEE International Conference *Meeting the Energy Demands of Emerging Economic Powers: Implications for Energy And Environmental Markets*	Singapore	OAEE/IAEE	Tony Owen esiadow@nus.edu.sg
September 3-6	15th IAEE European Conference *Heading Towards Sustainability Energy Systems: by Evolution or Revolution?*	Vienna, Austria	AAEE/IAEE	Reinhard Haas haas@eeg.tuwien.ac.at
November 12-16	35th USAEE/IAEE North American Conference *Riding the Energy Cycles*	Houston, TX, USA	USAEE	David Williams usaee@usaee.org
2018				
June 10-13	41st IAEE International Conference *Security of Supply, Sustainability and Affordability: Assessing the Trade-offs Of Energy Policy*	Groningen, The Netherlands	BAEE/IAEE	Machiel Mulder machiel.mulder@rug.nl
September 19-21	12th BIEE Academic Conference *Theme to be Announced*	Oxford, UK	BIEE	BIEE Administration *conference @biee.org*
2019				
May 26-29	42nd IAEE International Conference *Local Energy, Global Markets*	Montreal, Canada	CAEE/IAEE	Pierre-Olivier Pineau *pierre-olivier.pineau@hec.ca*
August 25-28	16th IAEE European Conference *Energy Challenges for the Next Decade: The Way Ahead Towards a Competitive, Secure and Sustainable Energy System*	Ljubljana, Slovenia	SAEE/IAEE	Nevenka Hrovatin *nevenka.hrovatin@ef.uni-lj.si*
2020				
June 21-24	43rd IAEE International Conference *Energy Challenges at a Turning Point*	Paris, France	FAEE/IAEE	Christophe Bonnery *Christophe.bonnery@faee.fr*