Opportunities and Risks: Financing Shipping in Mexico's Oil and Gas Market

By Eduardo Corzo | September 18, 2024

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The shipping industry in Mexico continues to be active in the offshore oil and gas sector. One of the main components of Mexico's economy is the production and trade of hydrocarbons, in which *Petroleos Mexicanos* (Pemex) – has a high share. Shipping companies see in Mexico an opportunity for business whether with Pemex or with other players in the private sector, as the energy market is still a national priority.

During the last two years, Pemex has suffered budget constraints generating internal cashflow shortage for Mexico's national oil company. The financial crisis of Pemex goes back many years, and payment delays to its contractors has unfortunately been a regular practice. Pemex contractors often struggle financially to maintain a healthy working capital and operating expenditure. Some past liquidity solution attempts to this problem have included factoring schemes, debt restructures, Pemex debentures in capital markets and other alternative payment structures explored both by Pemex and its creditors. These attempts have had a very low rate of success, as these measures are not sufficient to resolve the issues at hand.

Mexican oil and gas "service" companies continue to have an interest in Pemex for business opportunities. It seems as if the state-owned company is a business "going concern" despite its poor financial position. Contractors are making enormous financial efforts to honor and perform the "Pemex Contracts". Not doing so may be an exit door and result in them missing out on doing business with Pemex, as well as the resulting cost of contract rescission such as: excessive penalties, calling performance bonds, standby letters of credit, corporate guarantees, plus claims for damages and lost profits for breach of contract, if Pemex pursue a claim against them.

As the Pemex risk is growing, contractors are looking into other segment opportunities with larger scale companies such as International Oil Companies (IOC) and other foreign operators with more diverse business transactions worldwide, including Mexico. One of these opportunities is the chartering of vessels in Mexico for the oil and gas offshore industry to conduct works mainly in the Gulf of Mexico, usually for charterers whose end-client is Pemex.

With the new government administration to take office in Mexico at the beginning of October, together with the current stressed financial scenario of Pemex, companies are being conservative in their decision making and are seeing less alternatives for liquidity, other than bank debt. We anticipate seeing significant growth in bank loan placements within the next 12 months by both Mexican private commercial banks and government development banks. Banks are however expected to be cautious in not accumulating too much Pemex risk as it is likely to jeopardize the bankability of any project. Banks will likely prefer to finance other "service agreements" as opposed to traditional Pemex contracts, such as contracts entered by the borrowers in their capacity as contractors directly with IOC and foreign operators as counterparties, whose financial condition would be stronger than Pemex and with a higher level of performance, particularly when it comes to payment obligations (i.e. charter payments or service fees).

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Ship financing in Mexico is an option. Shipowners and/or charterers are finding that Mexican development banks are an attractive source of financing mainly for the purchase and construction of vessels, and for working capital, for their business ventures in Mexico. These financing structures are based on the underlying “service contract”, usually the chartering of the vessel, as a stream of income to serve as a preferred payment source of the bank debt. This is traditionally structured as an assignment of collection rights directly to the bank or to a specific vehicle such as a Mexican trust (lock-box) for the benefit of creditors, together with the creation of a security interest upon the vessel, such as a traditional Mexican-law ship mortgage or alternatively a more sophisticated guaranty trust. Time will tell whether these solutions address the issues which are currently facing the shipping industry operating in Mexico’s oil and gas market.

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