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Stuck in the Mud: The Politics of Constitutional Reform in the Oil Sector in Mexico

Importante

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Abstract

The energy industry plays an important role in the Mexican economy, and energy trade is a major component to the U.S.-Mexico relationship. The Mexican government relies on the oil industry for 35% of total government revenues, including taxes and direct payments from Petróleos Mexicanos (Pemex), the state oil company. Mexico is the third-largest foreign crude oil supplier to the United States. However, with declining production and rising demand, Mexico could become a net oil importer in the coming decade. President Calderón pushed for energy sector reform in Mexico, but more reforms will be needed for Mexico to reverse its current path toward importer status. This study identifies the dynamics of the political trends in Mexico that will impact future energy policy. The aim of this study is to promote a better understanding of the challenges facing Mexico's oil sector and to enhance the debate among policymakers, the media and industry on these important issues.

Resumen

La industria de la energía juega un papel fundamental en la economía mexicana, y su comercio es un componente importante de la relación México-Estados Unidos. Los ingresos del gobierno mexicano se basan en la industria petrolera que conforman el 35% de los ingresos públicos totales, incluidos los impuestos y los pagos directos de Petróleos Mexicanos (Pemex), la empresa petrolera estatal. México es el tercer proveedor de petróleo crudo a Estados Unidos, sin embargo, una disminución de la producción y la creciente demanda, podría convertir al país en un importador neto de petróleo en la próxima década. A pesar de que el presidente Calderón impulsó una reforma al sector energético en México, más reformas serán necesarias para que México dé marcha atrás en su camino hacia el Estado importador. Este estudio, publicado por el James A. Baker III Institute for Public Policy y el Programa de Estudios sobre México del Nuffield College Oxford University, identifica la dinámica de las tendencias políticas en México, que tendrán un impacto en la política energética en el futuro. El objetivo de este estudio es promover una mejor comprensión de los desafíos que enfrenta el sector del petróleo en México y reforzar el debate entre los legisladores, los medios de comunicación y la industria.

Introduction

Mexico remains one of —if not the— most restrictive oil regimes in the world. Certainly it is the least open of any oil-producing country. The Pemex monopoly prevails in most areas and the constitutional rules regarding the oil industry today are more restrictive than the ones that were written after the oil expropriation of 1938.

Yet, the country has changed dramatically in the last 25 years. Starting in 1985, important economic sectors were privatized; the ejido communal property system was overhauled, effectively cancelling the agrarian reform of the early 20th century, and Mexico entered the North American Free Trade Agreement (NAFTA). Moreover, Mexico became democratic. The transition did not come from the left, as was expected after the 1988 presidential election when the PRI was almost defeated. Instead, in 2000, a right-wing party, the PAN, won the presidency. The PAN was the only significant political party openly against the government monopoly in the oil sector. During the 2000 presidential campaign, PAN candidate Vicente Fox said he would liberalize the sector. However, he quickly retracted his statement after strong criticism of the media and of the PRI and PRD presidential candidates.¹

Neither the PRI market-oriented economic reformers of the late 1980s and 1990s, nor the PAN democratic governments after the year 2000, have done any substantive reform in the oil sector. A significant reform would be a constitutional or legal change that opens the sector, not the mere promise of more efficiency through minor changes.

Either the presidents could not embark on a reform, as in the case of Felipe Calderón and perhaps Ernesto Zedillo, or they did not want to, as in the case of Carlos Salinas and Fox. The logic of power prevailed over economic optimization. Ideology might have influenced these decisions, but the main explanation for this lack of reform is the power of those potentially affected and the political use of Pemex and its resources.

A state oil firm or national oil company (NOC) usually plays two roles simultaneously. The first is a political one, as a patronage instrument, and the second is economic: extracting oil. The tension between the two objectives can lead to very low economic efficiency and to corruption. However, it has been argued that the most profitable business on earth is a well-managed oil company. The second best is a poorly managed one.² State oil firms can survive for a long time being highly inefficient.

¹ After its creation in 1929, the PRI was in power with different names until the year 2000 when it lost the Presidency with the right wing party the PAN. The other important party is the left wing PRD that was formed by dissidents of the PRI that merged with the former Mexican Communist party after the 1988 presidential election when Cuauhtémoc Cárdenas was defeated.

² This phrase is attributed to David Rockefeller.

There are three ways to try to regulate a NOC. The first mechanism is with direct control —different management techniques that seek to enhance the efficiency of the firm. This has been the route followed by Mexican presidents since economic reforms started after the 1982 crisis and was the same route followed by President Fox. The second option is through a strong regulatory agency or other control mechanisms, such as a robust and independent board, as President Calderón is now supporting. The third option is to promote competition by opening the sector to new players. There are many variants of these strategies, but a good example for Mexico is the experience of Brazil, after the reform of Petrobras that started in 1997. This is the sort of reform in real life that enhances efficiency. This route, to my knowledge, has never been considered as a serious option by any Mexican administration. The exception is Calderón's 2008 reform initiative, which did consider opening refining oil and oil ducts to competition from private industry, but was nullified by Congress.

This paper will try to understand why the country has moved significantly in areas that were perceived as very difficult to change, but the oil sector in Mexico is “stuck in the mud”. The paper begins by describing the tough constitutional restrictions in this sector, which require constitutional reform for almost any substantial change. It then tries to explain why President Salinas, the most aggressive reformer in Mexico's history, was prepared to negotiate and sign NAFTA to privatize several state-owned firms, conclude agrarian reform and allow ejidos to be transformed into private property, but did not attempt to open Pemex to competition. The next section will briefly describe the weak efforts of Zedillo, overwhelmed by the 1994/95 crises, in the oil sector. The paper then analyzes what happened when the PRI lost power, focusing on Fox's failed efforts to modernize Pemex by managing it as a private firm, without attempting to change its monopolistic structure. The last section will describe the failure of Calderón to pass a significant oil reform and how he has so far implemented the weak reform that was approved.

One of the central questions is whether a significant reform in the sector is possible. The conclusion of this paper is simple: Do not expect any significant constitutional reform until a massive crisis becomes an imminent possibility, Pemex faces a major accident, or, in the context of declining production, the trade union picks an unpopular fight against a popular and capable reform-minded leader.

But no crisis, no matter how serious it is, will ensure reform, without a president that can explain why a profound shift is needed and a society that believes him, as well as some sort of coalition that is capable of including relevant and powerful actors. These vested interests can prolong agony for a long time, as even a declining Pemex can be very profitable to all those actors that extract rents from the oil industry's current organization in Mexico.

I. The Constitutional Chains

Mexican presidents prior to democratization had a lot of power. The system was authoritarian, although the president had to negotiate with several actors and confront a constitution that included very specific details devised to protect any gainer of a reform from future losses, as including such reforms into the constitution made change difficult.

The president could and did make constitutional reforms, but needed two thirds of the votes of each of the national legislatures and half-plus-one of local legislatures. With democracy after 1997, reform became even more difficult. Any major group had potential veto power.

The Mexican Constitution includes the most extraordinary details. For example, it states the amount of money that shall be given to political parties from the federal budget. It describes how this figure is obtained by multiplying the total number of citizens registered to vote in the Electoral Registry by 65% of the daily minimum wage; 30% of this money is to be distributed evenly among the parties registered and 70% according to the percentage of the vote obtained in the last election of federal deputies.³ Propaganda for electoral campaigns in television and radio is also regulated in detail by the Constitution. Section III of Article 41 states that the Instituto Federal Electoral (IFE) will be the only authority responsible for administrating state-owned airtime in both radio and television. This section also specifies that the IFE will have 48 minutes daily, divided in blocks of two and three minutes every hour. Of this time, political parties will have one minute for each hour of transmission in every radio and television station. These minutes are to be distributed with the same formula as the money is.⁴

The constitutional restrictions on the oil industry are equally detailed. Article 27 currently states that:

"It corresponds to the Nation the direct ownership of all natural resources of the continental shelf and the submarine shelf of the islands... oil and all solid, liquid and gaseous carbides ...

this ownership is inalienable and indefeasible and its exploitation, the use of the resources in question by individuals or companies incorporated under Mexican law, cannot be done except through concessions granted by the Federal Executive, according to the rules and conditions established by law. ... Regarding oil and solid, liquid and gaseous carbides ... no concessions or contracts will be granted⁵, nor will the ones already

³ Point II of Article 41 of the Mexican Constitution.

⁴ Part A paragraphs a) to e) of Section III of Article 41 of the Mexican Constitution.

⁵ Added in the 1940 reform.

granted will subsist and the Nation will carry out the exploitation of these products, under the terms established by the respective Regulatory Law.”⁶

Many other restrictions can be found in the Regulatory Law of Article 27 of the Constitution, such as the state monopoly for refining oil. This law, in its second article, states that: “... only the Nation may carry out the various oil holdings, which constitute the oil industry.” Regarding the oil industry, Article 3 of the same law, in its first point, states that the oil industry comprises: “The exploration, exploitation, refining, transport, storage, distribution and first hand sales of oil the products obtained from its refinement.” Article 6 also clearly states that the payment of a contract will always be in cash and that the property of reserves cannot be used to pay any contract.

The restrictions were not always so severe. Lázaro Cárdenas's constitutional reforms following the 1938 expropriation could have allowed service contracts based on incentives.⁷ Starting with Ruiz Cortines,⁸ and then more clearly with López Mateos, the law limited service contracts, incorporating into a reformed Constitution the last sentence of the paragraph just quoted.⁹

Businessmen who were worried about future expropriations after the abrupt bank expropriation of September 1982 at the end of José López Portillo's term needed to be appeased, as well as the left-wing PRI Party members, who feared the liberal reforms the new president wanted to implement. Thus, Miguel de la Madrid, shortly after his inauguration in December 1982, decided to more clearly define strategic sectors in Article 28 of the Constitution. Paradoxically, these reforms made the oil sector even more restrictive, as can be read in the Article 28, as reformed by de la Madrid:

“The functions exercised exclusively by the State in the following strategic areas will not be considered as monopolies: coinage; postal services; telegraphs; radiotelegraphs and satellite communications; issuance of paper money through a single bank, a decentralized body of the federal government; oil and other hydrocarbons; basic petrochemical industry; radioactive minerals and generation of nuclear energy; electricity; railways

⁶ Extracts form paragraphs four and six of Article 27 of the Mexican Constitution.

⁷ In this sense, Article 7 of the Regulatory Law of Article 27, published on November 9, 1940, stated that “contracts with privates could be celebrated, with the object that these would be carried out on behalf of the federal government, to perform the works of exploration and exploitation, and these would be compensated in cash or a percentage equivalent of the products they obtain.”

⁸ In 1958, the regulatory law of Article 27 was reformed so that Article 6 stated explicitly that the “remunerations established in this (work and service) contracts (celebrated with privates), will always be paid in cash and in no case ... percentages of the product or participation in the results of their works or services will be conceded.” Article 6 of the Regulatory Law of Article 27 of the Constitution in the oil industry, published November 29, 1958.

⁹ This reform was published on December 26, 1960, and at the time this modification added a last sentence to the fifth paragraph of article 27 of the Constitution.

and the activities expressly identified in the laws issued by Congress of the Union.”¹⁰

Restrictions on Pemex's management extend beyond constitutional and legal barriers. Trade union representatives sit on the administrative council (the equivalent to the board of directors) of Pemex. From there, they can try to water down any administrative change.

II. Becoming an Oil Exporter and its Fiscal Consequences

Pemex, from 1938 to 1978, was basically a very conservative company that was designed to give energy security to Mexico and promote industrialization. This changed in 1976 with the discovery and development of Cantarell, the third largest oil field in the history of the world. Pemex was transformed into one of the largest oil firms globally and Mexico into one of the leading oil exporters in the world and a key player in the United States market.¹¹ This discovery came after the price of oil had increased dramatically, first as a result of the creation of OPEC in 1973 and then with the Iranian Revolution of 1979.¹²

During the López Portillo years, oil production increased dramatically. By 1980, Mexico was exporting over 302 million barrels of crude oil, with a value of US\$9.44 billion; crude oil exports represented 52.4% of total Mexican exports in that year. With the oil boom came a dramatic increase of Mexico foreign debt that went from US\$42.774 billion in 1979 to US\$92.974 billion in 1983.¹³ It was expected that these new resources would allow Mexico to deepen its industrialization. But a decrease in oil prices, an increase in interest rates, and general administrative disorder and corruption in the Mexican government, particularly in Pemex, led to a major economic crisis. The peso was devalued from 26.8 pesos per US dollar on February 17, 1982, to 149.2 pesos per dollar by December that same year.¹⁴

The Mexican state is one of the worst tax collectors in the world. Mexico's average tax take, compared with other countries, is one of the lowest globally. One important reason for this is that public finances historically have been dependent on revenue incoming from natural resources. A good part of

¹⁰ “Decreto que reforma y adiciona los artículos 16, 25, 26, 27, fracciones XIX y XX; 28, 73, fracciones XXIX-D; XXIX-E; y XXIX-F de la Constitución política de los Estados Unidos Mexicanos”, *Diario Oficial de la Federación*, February 3, 1983: p 5.

¹¹ In 1983 16.4% of US oil imports came from Mexico. Source available at <http://www.eia.doe.gov/aer/petro.html>.

¹² According to data from the *Oxford Latin American Economic History Database*, oil prices rose 491% from 1970 to 1974, 68.77% from 1972 to 1973 and 386% from 1973 to 1974; from 1978 to 1979, oil prices increased 251% and 625% from 1979 to 1980. Data from petroleum prices available at <http://oxlad.qeh.ox.ac.uk/search.php>

¹³ Data from *Oxford Latin American Economic History Database*, Total external debt in millions of US dollars. Available at <http://oxlad.qeh.ox.ac.uk/search.php>.

¹⁴ Data from Banco de México, monthly average of peso-dollar exchange rate, available at: <http://www.banxico.org.mx/sistema-financiero/estadisticas/mercado-cambiarior/tipos-cambio.html>.

the revenue obtained in New Spain, the predecessor to Mexico, was dependent on taxes on minerals, especially gold and silver.¹⁵

Mexico is hardly unique. Countries with important natural resources frequently collect less from other taxes. As José Antonio Cheibub has shown,¹⁶ the presence of oil—or of any other “gift” from nature as a source of financing—makes it less necessary to extract wealth directly from citizens. If public expenditure can be covered with revenue from oil, why incur the political costs that a greater tax collection implies?

Although finite raw material reserves are theoretically everybody's property, born and unborn, future generations are unable to influence their exploitation. Only the living can protest, so it is more politically profitable to collect fewer taxes from them and spend the oil-based public revenue to satisfy their demands, than to invest all these natural resource revenues in the future.

Since oil reappeared in the 1970s, Mexico's public finances have been significantly dependent on this “gift” of geology that has generated an additional average income of around one third of all government revenues—as much as 44.2% of public revenue in 2008.¹⁷ In 2009, for example, without the rents from oil, it would have been necessary to collect more than 488 billion pesos just to maintain the level of expenditure of that year.¹⁸ In other words, without the revenue generated by oil, Mexico we would have needed to raise the collection of the income tax by 91%—or the collection of the value-added tax by almost 120%.¹⁹ The evolution of revenue from oil and hydrocarbons rights since 1980 is further discussed in Figures 1 and 2.

¹⁵ The average net revenue from 1794 to 1799 was of \$4,512,191 which represented 22.06 per cent of the total revenue of the viceregal government, this percentage is similar to the revenue that oil represents nowadays for the Mexican government. For more details refer to tables 1 and 2 in Carlos Marichal, “Una difícil transición fiscal. Del régimen colonial al México independiente, 1750-1850”, in Carlos Marichal y Daniela Marino (comps.), *De Colonia a Nación: Impuestos y política en México, 1750-1860*, (Mexico: Colegio de México, 2001): pp. 25-29.

¹⁶ Véase José Antonio Cheibub, “Political Regimes and the Extractive Capacity of Governments: Taxation in Democracies and Dictatorships”, *World Politics*, vol. 50, no. 3, 1998: pp. 349-376.

¹⁷ It is important to clarify that this percentage only includes revenue coming from the payment of rights to oil. Normally, the oil-based revenue includes the value-added tax and IEPS paid by Pemex and other taxes on fuels. These taxes are paid by Mexicans but collected by Pemex. Even in many countries that don't extract oil, taxes on gasoline can represent a greater income for the government than in the case of Mexico. Data obtained from SHCP, *Estadísticas oportunas de Finanzas Pública*, available online.

¹⁸ Based on *Estadísticas oportunas de Finanzas Públicas*, Secretaría de Hacienda, available online.

¹⁹ Estimation made without taking into account the costs of not having this dollar income or, even worse, the cost of being forced to generate this currency to satisfy our oil needs if Mexico was a net importer of crude oil. However, if, all of a sudden, we didn't have oil, the exchange market would reach an equilibrium at a value significantly greater. In other words, we would be poorer in dollar terms.

**FIGURE 1. PUBLIC REVENUE FROM RIGHTS TO OIL, 1980-2010
(AS A PERCENTAGE OF GDP)**

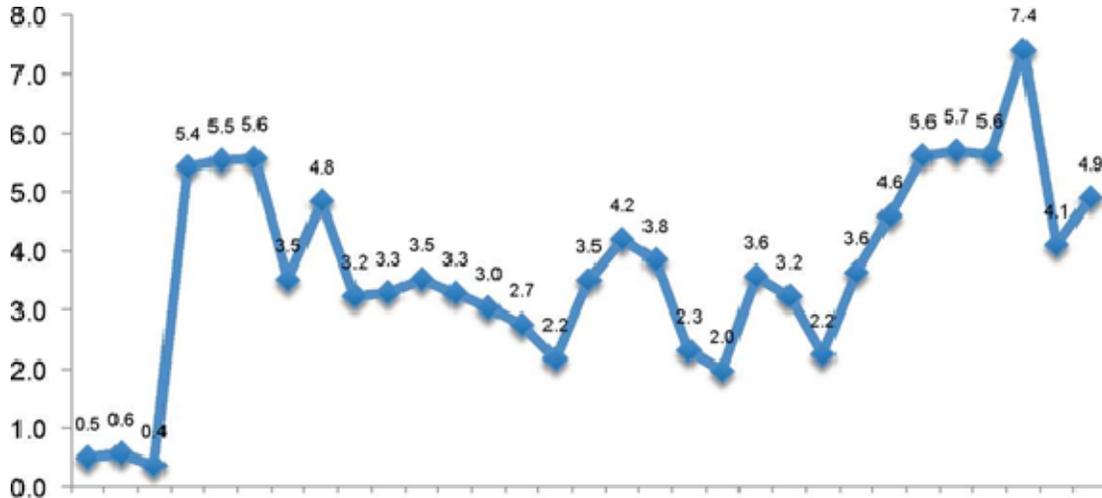
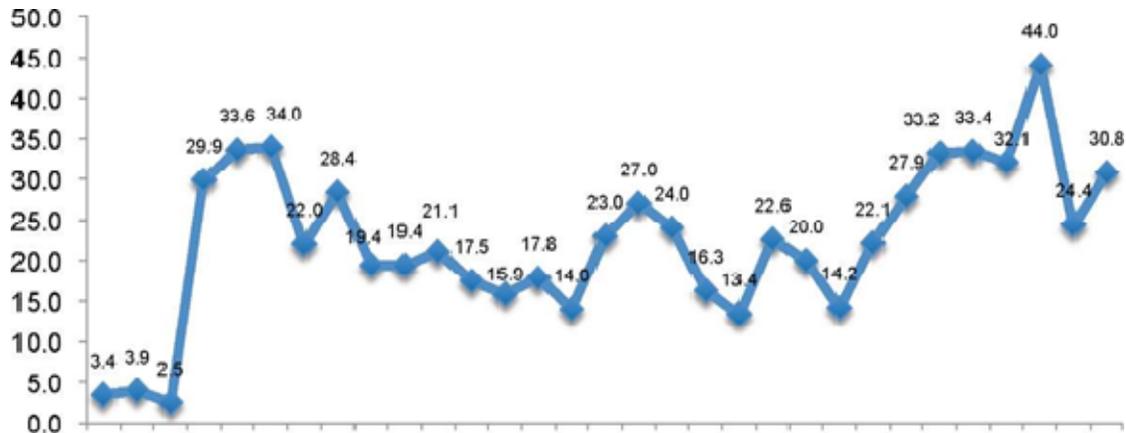


FIGURE 2. REVENUE FROM RIGHTS TO OIL AS A PERCENTAGE OF FEDERAL GOVERNMENT REVENUE/ 1980-2010



Oil resources have also sheltered a heavy and costly public administration and arrangements with unions during the years of increasing debt and dreams of abundant wealth. Union pensions, social security, and other benefits are expensive and unfair in comparison with those available in the private sector. These arrangements are not only expensive, but make it even more difficult to manage public expenditure for the benefit of society.

The fiscal accounts are balanced today thanks only to oil. When oil ceases to produce this revenue, Mexico will be forced to reform its tax law or try to

extract oil in a more efficient way. But meanwhile, the country can live off the cash that comes from oil.

III. After the Economic Crisis

President de la Madrid (1982-1988) inherited the new oil production platform and a significant flow of resources, but also a major macroeconomic crisis and the need to pay a large dollar-denominated debt. Although market reforms started in his administration, the oil sector was not a reform priority. What mattered was regaining control over the money generated in Pemex, limiting expenditures and trying to make Pemex more efficient. This led to a confrontation with trade unions, but no major institutional reform was attempted.

President Salinas (1988-1994) was much more aggressive in his reform agenda. However, no constitutional overhaul took place in the oil sector during his term. Some legal reforms did take place in electricity generation in 1992, although these were probably unconstitutional, as they gave private firms the possibility of producing electricity, but there was no mechanism then to challenge a law perceived as unconstitutional.

Salinas is the most complex puzzle with respect to the lack of reform in the sector. He was the last president with full control over the political process, especially after the midterm elections of 1991, when the PRI had again a wide margin and won 64% of seats in the Chamber of Deputies.

Contrary to what some critics thought would happen, he did not use NAFTA to open the oil sector. Instead, Salinas explicitly excluded oil from the agreement. In fact, in 2010, at a lecture in Madrid, Salinas claimed he rejected an offer by President George H.W. Bush to open the US labor market in exchange for Mexico opening in its oil sector.²⁰

Despite constitutional restrictions as described above, President Salinas did change Article 27 to end agrarian reform and to allow *ejidos* to be transformed into private property. The reform also made possible the association of *ejidatarios* with private producers. It was a major shift in the face of the regime's radical rhetoric and challenged one of the totemic myths of the Mexican Revolution.

²⁰ According to the newspaper *La Razón* Salinas said the following: "Durante las negociaciones sobre el TLC, en 1990, entre los presidentes de México y Estados Unidos, George Bush padre le propuso a Carlos Salinas que permitiera la inversión de empresas estadounidenses en el petróleo nacional a cambio del libre movimiento de mexicanos hacia el lado norte de la frontera:

—Imposible: ni ahora, ni conmigo— le respondió Salinas.

—Pero el petróleo también es una mercancía. El TLC se trata del libre flujo de productos. ¿O no?— insistió Bush, quien gobernó su país de 1989 a 1993.

—No, definitivamente no. El petróleo es un tema muy sensible y la apertura a la inversión extranjera en esa área no le toca a mi gobierno, ni a mi momento político ni a mi generación", in *La Razón*, October 26, 2010: p. 11.

Although agrarian reform was achieved, peasants were divided on its benefits. According to a survey conducted by the Office of the Presidency in 1991, more than 35% of the peasants interviewed expressed a preference for being small landowners, over 60% agreed with the freedom of associating with whomever they saw fit, and 51% said that they thought their land could be more productive if they could do business freely. However, when these same peasants were asked if they supported the possibility of *ejidatarios* selling their land, more than 61% were against it. Also, when asked about the possibility of transforming *ejidos* into small properties and being able to sell them, more than 55% of the peasants interviewed did not see a benefit.²¹ It was an unpopular reform, but Salinas used his power in Congress to get it approved.

Restoring relations with the Catholic Church also required a constitutional reform as clergy were banned from any political participation or even wearing religious clothes in any public space, except a church. The same thing was done to privatize the banks. After the nationalization of the banks in 1982, the Constitution was reformed in November of that year to make it very hard for de la Madrid to return banks to the previous owners. The new Article 28 was even harsher with respect to banking than Article 27 was with respect to oil.

However, the constitutional restrictions on the oil industry were not the only ones that remained unchanged. Article 123, which regulates workers conditions, was also left alone. In the cases of both Articles 27 and 123, any reforms would have affected the core of PRI support, the trade unions.

Salinas, however, did use his power to exert control in the oil sector. The leader of the Pemex trade union, Joaquín “La Quina” Hernández Galicia, was arrested on January 10, 1989. He was accused of murder, tax evasion, and stocking arms among other crimes. Everything seemed staged and a reaction to “La Quinas” criticism of President Salinas, but at the time, this arrest was viewed by some as proof of Salinas's will to reform Pemex by eliminating one of the fiercest opponents to this reform.²²

However, the real objective seemed to have been to oust a disloyal and autonomous leader in favor of a Salinas ally, and to try to modernize Pemex without opening the sector. “La Quina” had previously confronted President de la Madrid and had publicly criticized Salinas's policies when he was minister of budgeting and finance. He was also thought to have provided financial

²¹ Office of the Presidency of the Republic, *Ejido: Reforma al artículo 27 constitucional*, survey published on November 26, 1991, compiled by CIDE. Questionnaire and results available at CIDE at: <http://biiacs-dspace.cide.edu/handle/10089/446>.

²² Antonio Caño, “El ‘caso la Quina’ confirma la voluntad de Salinas para democratizar México”, *El País*, January 13, 1989.

backing for a book that described the shooting death of a Salinas family maid during a game, when Carlos Salinas was only a few years old.²³

When Salinas' presidential candidacy for the PRI was announced, "La Quina" instructed the members of the oil union to vote for the PRI only on Congressional elections and quietly supported the opposition's candidate for president, Cuauhtemoc Cárdenas, son of former President Lázaro Cárdenas. The results were that all the oil union candidates running for the PRI for Congress won, but Cárdenas won in almost every oil district.²⁴

Salinas realized the Pemex trade union was helping Cárdenas during the presidential election, and he prepared to ally with Luz y Fuerza del Centro (LyFC) and the its trade union, SME. He maintained this alliance throughout his term, even though it went against his goal of opening and modernizing the economy.²⁵

After the arrest of "La Quina", the government installed Sebastián Guzmán Cabrera as the new leader of the union, without holding elections as the law required. Guzmán used several of the same tactics "La Quina" used to get control of the union. His subsequent cooperation with the president's policies demonstrated that the change in union leadership was more about the necessity to control, rather than eliminate corruption in Pemex—or any resistance to major constitutional reform that was never attempted.²⁶

Some minor reforms in the sector were, however, undertaken. Two basic principles guided the reform of Pemex: clarifying the concept of Pemex as a "state enterprise" and operating the company based on economic criteria rather than political motivations—that is, maximizing income, production, etc.²⁷

The economic logic of this new arrangement was to preserve the monopoly of exploration and production of oil while opening certain services associated with natural gas to private capital, national or international. With this logic in mind, Pemex was split into one corporate company with four subsidiaries. By decentralizing power, each subsidiary had its own responsibilities and, by separating the company, functional units were separated from the ones with a persistent deficit. Another principle that motivated this division was to create

²³ "La Quina" publicly denied that he paid for the printing of this book written by José Luis González. See, Fabiola Martínez, "'Quiero ver a Salinas en el banquillo de los acusados', clama La Quina", *La Jornada*, June 19, 2004.

²⁴ Andrew Reding, "Mexico under Salinas: A Façade of Reform", *World Policy Journal*, vol. 6, no. 4, 1989: 701-702.

²⁵ In a speech delivered on February 1988, Salinas made clear his intentions of making an alliance with the SME, after the union had withdrawn from the CTM (Confederation of Mexican Workers) and established its independence from the PRI. A deal was struck with the union leadership to guarantee the union's existence and consult with it about the liquidation of LYFC. By doing this, Salinas was able to assure the union's support instead of confronting it directly. Reding: p. 701.

²⁶ *Ibid.*, 702-703.

²⁷ Isabelle Rousseau, "Reforma de las empresas públicas de México, dos visiones opuestas de reforma organizacional: el caso de Petróleos Mexicanos (1989-2004)", *paper prepared for the CLAD IX International Congress on State and Public Administration Reform*, Madrid, Spain, November 2-5, 2004: p. 8. Available at: <http://www.ij.derecho.ucr.ac.cr/archivos/documentacion/inv%20otras%20entidades/CLAD/CLAD%20IX/documentos/rousseau.pdf>.

a “micro-market” within Pemex, so the prices at which each part of the company would buy or sell its products were always compared with the export price, thus incorporating the “opportunity cost” principle within the operation of a publicly owned monopoly.²⁸ It was thought that this would encourage more efficient transactions within the company.

Part of the changes to make Pemex more efficient included reducing operating expenses. This resulted in the dismissal of 30,000 short-term employees out of a total of more than 86,000,²⁹ and the termination of overtime pay rates for permanent workers. These dismissals, allegedly, violated the terms of the union contract.³⁰ In May 1989, Pemex and the union's secretary general agreed to de-unionize 10,000 technical and professional workers. This eliminated the legal obligations of the company as stipulated in the union's collective contract with these workers.³¹

Reforms were also introduced in the electricity sector. The government was afraid that when the economy started growing quickly again (which did not happen), Mexico might face blackouts without private investment. The Comisión Federal de Electricidad (CFE), the most important state owned electric company, retained control of transmission and distribution, so the reforms were not perceived as a menace, but as a means to modernize. The trade union was promised representation of any workers hired by the private sector.

The electrical industry reform focused on three fundamental areas: the reforming of rates, restructuring CFE and LYFC, and a partial opening of the sector to private capital. The idea behind these reforms was to ensure a certain level of investment given the reduction of public deficit and the liberalization of the economy and curtailment of the state's role. The rate increase started in 1990 under the principle that the rates should be similar to international rates, such as those in the United States, while still maintaining some competitive edge.³²

The restructuring of the public enterprises, with emphasis on the reform of CFE given its national relevance, sought to keep the most strategic activities in the hands of the Mexican government. Private self-generation of electricity was promoted with legal reforms, in order to reduce pressure on public investment to satisfy the demand for electricity. There were also

²⁸ *Ibid.*, 9.

²⁹ Number based on calculations obtained from the worker census used in internal union elections in Fabio Erazo Barbosa, “La reestructuración de Pemex”, *El Cotidiano*, no. 46, March-April 1992. According to these figures Pemex had a total 178,745 workers (86,985 transient and 89,316 permanent) in 1988 and this number descended to 142,637 workers (53,321 transient and 89,316 permanent) in 1991 due to these reforms.

³⁰ Salvador Corro, “Violaciones al contrato, vigiladas por el sindicato”, *Proceso* magazine, no. 654, May 15, 1989.

³¹ Gerardo Galarza, “Pemex echó a 30,000 transitorios, confirma Guzmán”, *Proceso* magazine, no. 655, May 20, 1989.

³² Víctor Rodríguez Padilla, “Impacto de la reforma económica sobre las inversiones de la industria eléctrica en México: El regreso del capital privado como palanca del desarrollo”, *Serie Reformas Económicas* 18, ECLAC, February 1999: p. 17.

important reforms to increase productivity, efficiency, and to improve customer service. Some operative areas were decentralized, internal evaluation of performance was implemented, and several productivity agreements were signed with CFE's trade union, the SUTERM.³³

The last element in the reform was the participation of private business in the generation of electricity. Power generation, transformation, and distribution were restricted to the state, so a new law was passed that more narrowly defined the concept of a public service in electricity. This new law excluded several activities from the definition of public service, including: the generation of electricity for self-consumption, co-generation of electricity, selling electricity to CFE with long-term contracts, export of electricity that is not for public use, emergency use of electricity, and importing electricity only for consumption.³⁴ According to Dr. César Hernández, this reform helped the electric sector by making private investment more productive, but CFE, when compared to similar firms, is still overstaffed and unproductive.³⁵

The decision to exclude oil from NAFTA was made following a discussion between cabinet members. Technocrats defended opening the sector, while the more traditional politicians, under the influence of the Pemex management, argued for the modernization of Pemex without opening the sector.³⁶ Technocrats accepted the deal, rather than risk jeopardizing the approval of the treaty by the US and by the PRI members, the *priistas*. If oil was opened to competition, it could derail approval in Mexican Congress,³⁷ as pushing for both fundamental reforms (NAFTA and Pemex) would have galvanized the opposition. Instead of just dealing with NAFTA opponents, treaty supporters would also have had to contend with trade union leaders and firms that benefit from Pemex, as well as politicians and ideological opponents. The myth of the oil expropriation was still very strong, and contrary to the situation of the *ejido*, where reform was perceived as unavoidable, many thought Pemex could just be better managed.

The evidence suggests that Salinas never tried to open the oil sector. The main reasons behind this decision seem to be the following.

First, it was a source of discretionary power and resources for the government. Pemex is patronage in its very pure form. It is also the power base for a very diverse set of actors, former trade union leaders, *contratistas* (businessmen in the transport, construction, machinery, and other sectors related to the industry), powerful local politicians (such as municipal presidents linked to the trade union in those areas where Pemex workers live), and other organized groups that have traditionally received Pemex

³³ *Ibid.*, 21.

³⁴ *Ibid.*, 25-26.

³⁵ César Hernández, *La reforma cautiva: inversión, trabajo y empresa en el sector eléctrico mexicano*, México: cidac, 2007.

³⁶ Interview with Jaime Serra Puche, September 23, 2010, at SAI Derecho & Economía, Mexico City.

³⁷ *Ibid.*

subsidies. These actors have a lot of legal and illegal resources to pressure politicians, and have used them in the past. The trade union is both an instrument of political control and a relatively autonomous and very important source of power. Paradoxically, once Salinas imprisoned “La Quina” and had fundamental control over his successor, there were fewer incentives for profound reform.

Second, in theory, the rents can be better extracted with more competition, which should decrease the role and extracting capacity of the trade union, managers and *contratistas*. However, competition implies a new set of rules with less discretion for doing illegal business or for quickly appropriating resources with fiscal purposes. This was important in the middle of a fiscal crisis that demanded resources to pay Mexico's external debt, as still was the case during the first half of the Salinas administration.

Third, oil sector reform was not very popular.³⁸ The nationalization of the oil industry in 1938 played a key role in consolidating the Mexican post-revolutionary government and helped drive industrialization. The expropriation was an important symbol of Mexico's control of its own resources. As part of Mexico's historic mythology, and in the light of the other Salinas reforms, the expropriation was one of the few remaining and visible legacies of the Mexican Revolution. Although this ideology was important, agrarian reform was also part Mexico's historic mythology. The fact that the oil sector remained closed reflected political, rather than ideological, constraints.

Fourth, the failure to regulate international oil companies in the early 20th century, a conflict that ended with the expropriation of March 1938, made it difficult to argue that regulation could work in the future.³⁹ A weak state, without strong autonomous regulatory agencies, might lack the skills to open a sector to competition where the players are very strong.

Fifth, in a more competitive electoral system, as the one that emerged after the contested 1988 presidential elections, with increasing controls over the resources used by the central administration, Pemex becomes even more valuable politically. It can channel resources with more flexibility than the central government. This aim of distributing resources for political reasons became entrenched in the administration itself. The position of adjunct general director of Pemex frequently went to politicians well known for experience in managing elections. Such was the case for Cesar Augusto

³⁸ A survey conducted in July 1992 revealed some public support for the selling of public companies (55% agreed with this policy, 7% agreed partially and only 23.5% disagreed with it). Curiously enough, this wasn't seen as an abandonment of revolutionary principles (53% of the people surveyed manifested that this privatization policy didn't abandon the principles of the Mexican Revolution). Office of the Presidency of the Republic, *Privatización de la banca*, survey published on July 17, 1992, results compiled by CIDE and available at: <http://biiacs-dspace.cide.edu/handle/10089/157>.

³⁹ After the experience with the privatization of TELMEX, this view seemed to be validated. TELMEX is, however, a more efficient firm by far and it does face competition.

Santiago from 1993 to 1999, and of Humberto Lira Mora, as corporate administrative director of Pemex, from the beginning of the Zedillo administration until 1997.⁴⁰

IV. Zedillo and the New Crisis

Although President Zedillo would have probably been ideologically in favor of some liberalization of the oil sector, the economic crisis that exploded 18 days after his inauguration forced him to concentrate on stabilizing the economy during the first half of his administration. The crisis of 1994-95 did lead to privatizations, but most of the firms sold or liquidated were losing money.

The only major privatization during this period was of Ferrocarriles Nacionales de México, Mexico's state-owned railroad company, which had an average deficit of about \$400 million per year.⁴¹ In the oil sector, Zedillo only managed to open to competition the distribution of natural gas in 1996.⁴² The other important reform in 1997 was the introduction of a system of pensions based on contributions by workers, but only for those worker hired by the private sector.

Privatization and liberalization became dirty and unpopular words after the 1994-95 economic crisis. The banks were being rescued at a high fiscal cost, nearly 20 percentage points of GDP;⁴³ the devaluation had eroded savings; and high interest rates were choking indebted firms.

The Salinas reforms had lost most of their appeal. At the end of the Salinas presidency in October 1994, one public opinion study found that 52.2% of the people favored the privatization policies undertaken, 38.2% were against them and only 9.6% remained undecided.⁴⁴ After the crisis, public opinion changed significantly. By April of 1995, only 24.4% favored the privatizations made while 51.4% were against them; only 5% didn't express an opinion either for or against the privatizations made.⁴⁵

Furthermore, any thoughts of reforming were countered by the fact that Pemex was a cash cow, and its flow was the collateral for the US\$48.8 billion

⁴⁰ I owe this point to Ignacio Marván.

⁴¹ Number from Richard Sharp, "Resultados de la privatización de ferrocarriles en América Latina", *Transport Paper* no. TP-6, The World Bank Group, September 2005.

⁴² The Regulatory Law of Article 27 was reformed and published on November 13, 1996.

⁴³ An estimation was made that the total fiscal cost of all the programs for banking support, in June 1999, was of 19.3% of GDP. M. Naranjo, "Evolución del seguro de depósitos en México", Working Paper no. 2000-02, Comisión Nacional Bancaria y de Valores, Mexico, 2000.

⁴⁴ Surveys made by the Presidency in October 1994.

⁴⁵ Office of the Presidency of the Republic, *Opinión sobre la privatización de Pemex*, results compiled by CIDE and available at: <http://hdl.handle.net/10089/3394>

credit that the U.S. gave to Mexico to avoid a financial meltdown.⁴⁶ The main objective of the administration was to ensure oil would continue flowing and confront a potentially declining Cantarell. This led to an ambitious effort to quickly expand the production of Cantarell. There was a debate about whether this decision led to higher short-term production, at the expense of lower capacity to oil in the future.

The government tried to sell the petrochemical plants of Pemex in 1995. It proved very difficult to convince the PRI of the need for such a change. The difficulties in obtaining a price with potential buyers that could justify the privatization in fiscal terms weakened the position of sale supporters. Moreover, most of the plants were in former *ejido* lands that had been expropriated for public use, and any privatization might oblige the government to return the land to the *ejidatarios*.⁴⁷ The attempt failed.

By the time the crisis was over, a large segment of the PRI was increasingly dissatisfied with Zedillo and, in an unusual rebellion, the party changed the rules regarding the characteristics of the future PRI presidential candidate. To avoid another technocrat like Zedillo becoming president, all candidates would now be required to have previously won an election.⁴⁸ Moreover, the PRI lost the majority in the lower chamber in the midterm election of July 1997; and Cuauhtémoc Cárdenas of the PRD, Salinas' former rival, was elected mayor of Mexico City.

Reforms based solely on presidential will, as in the past, were no longer possible, as was made evident with the failed opening and privatization of the electricity state-owned firms. The reform proposed in 1998 by President Zedillo failed. The PAN openly did not support it, but the PRI, although less open than the PAN, was clearly against it.⁴⁹ No major reform took place in the second half of the Zedillo administration.

⁴⁶ The Mexican government agreed to deposit the revenue from oil exports of Pemex in a revolving account of the Federal Reserve Bank in New York. Nora Lustig, "The United States to the rescue: financial assistance to Mexico in 1982 and 1995", *CEPAL Review*, no. 61, April 1997: p. 59.

⁴⁷ Interview with Rogelio Gasca Neri, October 4, 2010.

⁴⁸ These changes were expressed in the XVII National Assembly of the PRI in 1996. As a result, the reformed statutes of the party included an assertion of the PRI's identity as defender of the national sovereignty and as a revolutionary party. That meant to restore the banners of social justice as a core value of the PRI. The other important modification in that Assembly was the introduction of restrictions for becoming the party's Presidential candidate, such as having previously occupied an elected position. These reforms were seen as a rebellion of the party against the traditional Presidential leadership, and they also imply an ideological move away from the liberal agenda that Salinas and Zedillo exemplified.

⁴⁹ In fact some *Panistas* have argued that they opposed it because it was evident that the PRI would not approve it.

V. After the Democratic Transition

Should democracy make it easier or more complex to confront the powerful interests behind the PRI's status quo in the oil sector? In principle, well-designed reforms that promote competition in the oil sector should be in the interest of the majority. However, several factors have stood in the way since 2000. Citizens are poorly organized. With the exception of businessmen, no one with power in society is demanding an opening in the sector. Even businessmen are not entirely united. Carlos Slim, the world richest individual according to Forbes, is publicly against reform.⁵⁰

Moreover, the PAN has never had the majority in any of the legislative chambers, let alone the two-thirds majority needed to reform the Constitution of Mexico. The two dominant opposition parties, PRI and PRD, have been against any major reform for both ideological and, more importantly to the PRI, political reasons. The PRI has been allied with some of those actors who extract rents and gain from Pemex, including the trade union and the *contratistas*, the private firms that sell goods and services to Pemex.⁵¹ Moreover, after the 1994-95 crisis, all reforms lost public support, as I argued in the previous section.

Although many constitutional reforms have been enacted since Mexico became a democracy,⁵² none has affected the core interests of the PRI, which include trade union leaders who are virtually unaccountable for the resources they control and who have reelected themselves almost eternally, and governors with their growing fiscal resources, for which they are not accountable. As described above, major changes in the oil sector require constitutional reforms. Building the coalition to pursue such a goal is very complicated; it would be necessary to incorporate the PRI. It would also need to include, in case of any constitutional reform, at least half plus one of the local chamber of deputies, usually under the control of the state governors—the great winners of the democratic transition in terms of the power they have gained.

Any change in the oil sector is a very sensitive issue, since oil income has played a central role in funding our transition to a democracy. Moreover, in

⁵⁰ Israel Rodriguez, "Carlos Slim, contra la apertura de Pemex al capital privado", *La Jornada*, October 10, 2006.

⁵¹ Luis de la Calle, former undersecretary of commerce, has argued that just making public who are the owners of these *contratistas* would undermine these powerful groups.

⁵² There have been a lot of constitutional reforms since 1999, the articles reformed in each year were: in 1999, articles 4, 16, 19, 22, 25, 58, 73 (3 reforms), 74, 78, 79, 94, 97, 100, 102, 107, 115 and 123; in 2000 articles 4, 20 and 73; in 2001, 1, 2, 4, 18 and 115; in 2002, 3, 31 and 113; in 2003, articles 63, 73 and 77; in 2004, 65, 73 (2 reforms), 74 and 89; in 2005, articles 14, 18, 21, 22, 46, 73 (2 reforms), 76 and 105; in 2006 1, 26, 73 (2 reforms) and 105; in 2007, articles 6 (2 reforms), 29, 41, 55, 73 (3 reforms), 76, 82, 85, 89, 90, 92, 93, 95, 97, 99 (2 reforms), 108, 110, 111, 116, 122 and 134; in 2008, 16, 17, 18, 19, 20, 21, 22, 69, 73 (2 reforms), 74, 79, 88, 93, 115, 116 (2 reforms), 122, 123 and 134; in 2009, articles 4, 16 (erratum), 73 (3 reforms), 75, 115, 116, 122, 123 and 127 and only article 122 in 2010.

the Fox years, oil production and oil prices rose. Everyone was happy, and a weak tax collection system continued without the need for tough decisions.

If the only problem of Mexico were the *priistas* (members of the PRI) that controlled the government, as Fox stated,⁵³ there would be no need for reform. Pemex only had to be managed better (in theory). With this goal in mind, President Fox hired a former president of Dupont Mexico, Raúl Muñoz Leos,⁵⁴ to more efficiently administrate Pemex.

In the words of Muñoz Leos, "I was convinced that, with the application of business criteria to its administration, the value of the parastatal could increase."⁵⁵ He was quickly disappointed when he discovered, in his words, "that the new administration did not have any plans whatsoever regarding Pemex despite its enormous importance for public finances."⁵⁶ The basic strategy followed by Pemex was incorrect. The new director thought that "[w]hile the world tendency was to bring about mergers with the objective of taking advantage of synergies and increasing efficiency, in Mexico the changes were on the contrary. Pemex was divided in autonomous agencies that, already dragging with structural weaknesses in areas like strategic planning, operated with their own agendas and, in many occasions, quarreling between them, with all its implications, like raising communication barriers."⁵⁷

Muñoz Leos' first task was to liberate Pemex from regulations that fostered financial rigidity and even corruption. The excessive fiscal burden had been limiting company investments, since the strategy imposed on the company, until then, was to emphasize its role as a great fiscal contributor.⁵⁸ A change in the fiscal regime of Pemex was of the utmost importance. There was a continuous effort to reduce operational expenses, but other steps needed to be taken. Pemex needed to have management autonomy, which implied that the Administrative Council must have the power to properly establish a corporate government fully responsible for operational and financial results, instead of being subject to the standards of public entities that do not invest or generate any revenue.

Legislative changes were also needed to give Pemex the freedom to associate with national and foreign firms and to develop diverse projects along the productive chain. This would expand the scale of the company's operations, achieve a more efficient implementation capacity, and lead to

⁵³ Vicente Fox declared in an interview: "Este es el momento preciso de dar el primer gran paso para echar a esos barbajanes (the PRI) de los Pinos (the home of the Mexican Presidency)". Francisco Ortiz Pinchetti, "Fox insiste en la alianza por la Cámara para 'sacar a los barbajanes de los Pinos'", *Proceso*, no. 1055, January 19, 1997.

⁵⁴ Muñoz Leos started his professional career in Du Pont in 1964. He was Executive Vicepresident and General Director of Du Pont Mexico. He was also national Vicepresident of COPARMEX. It has been argued that the operation of Du Pont was controlled from the United States and Muñoz Leos was some sort of political liason, more than actual manager, although he argues in his biography that he had a very active role.

⁵⁵ Raúl Muñoz Leos, *Pemex en la encrucijada*, (Mexico: Nuevo Siglo Aguilar, 2006): p. 21.

⁵⁶ *Ibid.*, p. 79.

⁵⁷ *Ibid.*, p. 82.

⁵⁸ *Ibid.*, p. 92.

broader processes of direct investment and greater access to new technologies. Pemex would increase production without putting national sovereignty in jeopardy since the company, seven decades after its founding, was mature and strong enough to establish productive alliances with companies of any size and nationality.⁵⁹

In Muñoz Leos' view, he never had the full support of the president in confronting all of these challenges. Moreover, he had to deal with two controversial issues soon after taking office. First, Carlos Slim, Alfonso Romo, Lorenzo Zambrano, and Rogelio Rebolledo were appointed the government's representatives on the Administrative Council of Pemex, which created a major political turmoil, including the accusation that this decision was the first step in the privatization of Pemex. Second, the government's decision to prosecute the secretary general of Pemex's trade union for transferring resources of the union to the PRI in during the 2000 presidential election the so called Pemex-gate, made internal negotiations even more difficult. These decisions were made without his consultation.

Nevertheless, Pemex's central aim was to have more money and to invest it properly. In Muñoz Leos' words, "By carrying out a physical annual investment level, starting next year [2002] and until 2006, two times greater than the average investment level in recent years—that is, close to \$33 billion in the whole period—the previously stated critical level would be reached and a greater flow of cash would be reached compared with the one would be obtained if the current investment rate was maintained. The production of crude oil could be elevated to close to 3.8 million barrels daily and the gas production could reach just over 6 billion cubic feet daily.⁶⁰ ...There were clear indicators that the Mexican oil reserves could double in volume."⁶¹ Thanks to that flow of money, it appeared that the resources invested since 2002 to locate new sources of hydrocarbons were yielding results, so it was very important to confirm news that was so crucial to the future of the nation, according to Muñoz Leos.⁶²

He got the money. Investments in the exploitation of hydrocarbons between 2001 and 2004 were 253 billion pesos, or 63 billion annually—an investment level significantly higher than the 40 billion pesos invested annually between 1990 and 2000. The investment between 2001 and 2004 was approximately 160 billion pesos, or 14.667 billion annually, a number significantly greater than the 2.371 billion pesos invested from 1990 to 2000.

⁵⁹ *Ibid.*, p. 159.

⁶⁰ *Ibid.*, p. 105.

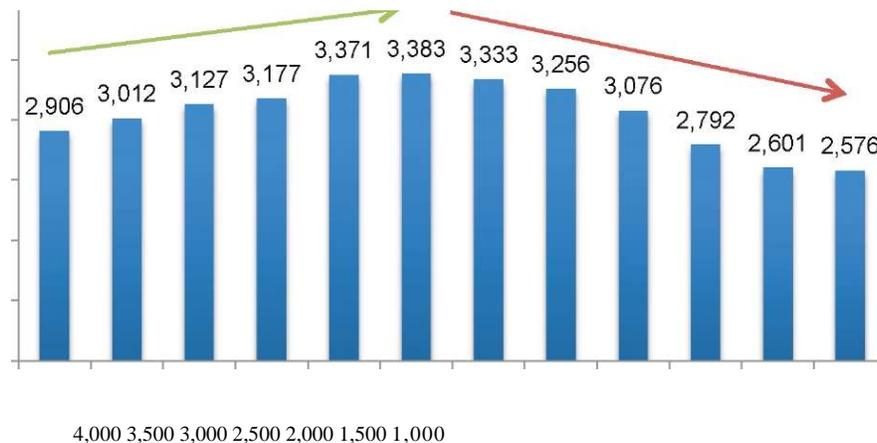
⁶¹ *Ibid.*, p. 163.

⁶² The Chincontepec project was already seen as the most important project there was an estimated 130 billion barrels of crude oil, the equivalent of 37% of the total oil reserves. This was the greatest accumulation of hydrocarbons ever discovered in Mexico. The project would start with a initial phase with a cost of 6 billion pesos, and included the drilling of 300 oil wells and the construction of 177 kilometers of pipelines. The project would be completed over 15 years, and it contemplated the drilling of 13,500 oil wells, with an investment estimated in 310 billion pesos. From Muñoz Leos, pp. 147-148.

This brought about an increased production of oil and gas, equivalent to 1.9 billion barrels of crude oil, as well more than 400 billion pesos in revenues. The investments made during this period were the most profitable in the country. Every additional peso invested generated 2.5 pesos of revenue.⁶³

But in spite of all of the money allocated to Pemex and the good short-term results, Pemex's situation started to deteriorate as oil production declined in 2007 and reserves continued to fall. While in 2000 proven reserves were over 25 billion barrels, by 2010 they had dropped almost 50% to its current level of 13.99 billion barrels.⁶⁴ The decline in oil production and reserves can be observed in Figures 3 and 4 and in Table 1.

**FIGURE 3. PRODUCTION OF CRUDE OIL, 1999-2010
(THOUSANDS OF DAILY BARRELS)**

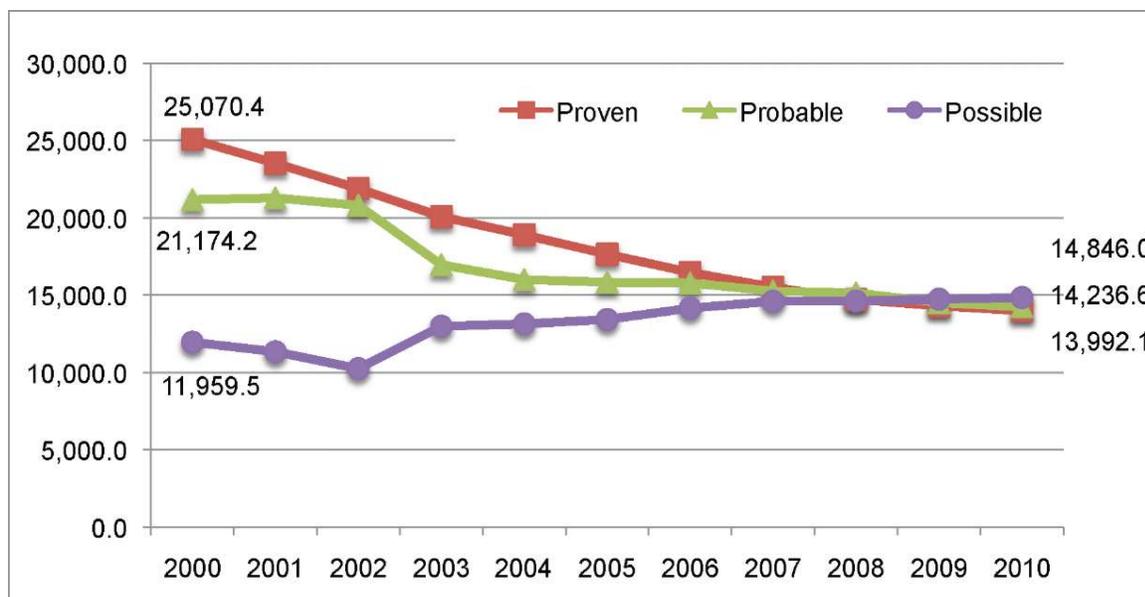


Source: Secretaría de Energía, *Sistema de Información Energética* (Energy Information System), Mexico. Available at: <http://sie.energia.gob.mx/sie/bdiController>

⁶³ *Ibid.*, p. 187.

⁶⁴ Petróleos Mexicanos, *Statistical Yearbook 2010, Exploration and Production*, Mexico: Pemex, 2010. Available at: <http://www.ri.Pemex.com/index.cfm?action=content§ionID=135&catID=12322>.

FIGURE 4. OIL RESERVES, 2000-2010 (MILLIONS OF EQUIVALENT BARRELS)



Source: Petróleos Mexicanos, *Statistical Yearbook 2010, Exploration and Production*, Mexico: Pemex, 2010. Available at: <http://www.ri.Pemex.com/index.cfm?action=content§ionID=135&catID=12322>

TABLE 1. OIL PRODUCTION AND RESERVES, 2000-2010 (MILLIONS OF EQUIVALENT BARRELS OF CRUDE OIL)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
TOTAL	58,204	56,154.	52,951	50,032.	48,041.	46,914.	46,417	45,376.	44,482.	43,562.	43,074.
PROVEN	25,070.	23,525.	21,892.	20,077.	18,895.	17,649.	16,469.	15,514.	14,717.	14,307.	13,992.
PROBABLE	21,174	21,285.	20,807.	16,965.	16,005.	15,836.	15,788.	15,257.	15,144.	14,516.	14,236.
POSSIBLE	11,959	11,343	10,251.	12,990.	13,140.	13,428.	14,159.	14,604.	14,621	14,737.	14,846.
DRY GAS RESERVES	55,507	55,515	50,648.	48,796	49,008.	48,649.	46,715.	47,367.	45,858.	44,622.	44,712.

Source: Pemex, *Statistical Yearbook 2010*

VI. Calderón's Reforms

President Calderón took a different route than his predecessor. He believed reforms in the energy sector were needed, but Calderón was politically weak, and had a very thin list of allies, when he took office. Just being able to govern was almost a miracle. Thus, he knew he could not start his term with divisive reform measures. At the beginning of the *sexenio* (or, his six-year term), he defined a series of reforms, beginning with a relatively uncontroversial one –the reform of the Mexican State Institute for Social

Security Services (ISSSTE). The failure of the previous *sexenio* to prioritize the reforms justified this new strategy, although starting with an easier reform increased the difficulty of the proposed future reforms.

The energy and labor reforms were considered the most complicated in the new administration's agenda, especially because of the symbolic weight of the oil expropriation. It was thought that the second year of his term was the best time to undertake the most complex changes. At that point, the administration would have gained a certain expertise, but would also have a certain distance from the mid-term elections of 2009. It was believed that energy reforms could polarize the three parties, particularly the PAN and the PRI.

In its approach to energy reforms, the government followed the successful negotiation model of the ISSSTE reform—that is, the PRI and the main actors potentially affected by reforms, in this case the oil trade union, agreed on the basic reforms before they were sent to Congress. As the

PRI required that the constitution remain untouched, this implied that the reforms had already been “watered down” by negotiations. With the text already settled, the idea was to approve it quickly in Congress, leaving the PRD without any time to react and stall the reform.

In the case of the ISSSTE, the reforms had been approved by the time the opposition realized what the government had done. The only recourse left for the PRD was social protest or an injunction (an *amparo*). However, it was too late to actually nullify the reform. The protests became a mere nuisance to the government.

Nevertheless, Pemex is not the ISSSTE, and the PRD learned from its experience with the ISSSTE reform. Also, the oil reform was publicized in advance. López Obrador, the PRD presidential candidate in 2006, was in a position to influence public opinion against the “privatization” of Mexican oil, and seized the vacuum left in the media when the government negotiated the contents of the reform with the PRI. Once the initiative was presented in the Senate, and before it could be approved, the PRD seized the Senate platform. They achieved their objective: stopping a fast-track approval of the reform. The PRD agreed to release the Senate platform in exchange for a 71-day debate of the issue. The PRI members who opposed the PRI's legislative leadership on this issue took advantage of the postponement of the vote to push for further erosion of the reform. This was done for ideological reasons, to flex their muscles before the party leadership, or to ask for more money from the government in exchange for their support for the reform, or a combination of these three reasons.

The government did not use the 71 days of debate to actually defend the proposed reform. Far from taking advantage of this time to emphasize the need for a significant change, the government delegated the defense of the reform to the PAN senators. The PAN senators were overwhelmed by the

superior debating powers of the PRD and its allies, including, at times, an important faction of legislators from the PRI. The Ministry of Energy, after an appearance by its minister before the Senate, was virtually absent from this debate.

For the PRI, the objective was to dilute the initiative even more and give Pemex a new structure of government that permitted the PRI to place people loyal to the party onto the administrative council. Having the power to fill long-term positions during any potential reform is one of the fundamental strategies of the PRI. It has been one of their most interesting “currencies” in any negotiation.

As part of its negotiation strategy with the PRI, the government chose a very limited reform initiative. Thus, there was very little to negotiate with the PRI before it was approved in Congress. Not only does the PAN need the PRI to approve any reform, but it usually opts to include the PRD as well. This approach leads to gradual and contradictory reforms that must accommodate the demands of parties with very different positions. Nevertheless, by accepting some of the PRD demands, the PAN managed to divide the PRD and isolate López Obrador— although it was López Obrador who had started a movement to derail Calderon's reform efforts.

Even though Calderon's initial proposal was watered down,⁶⁵ he decided to celebrate with champagne. The president also delivered a message in

⁶⁵ Calderón's initiative included several modifications that, after the long debate, were not included in the final reform. Some of these include the following:

The President proposed a regime change, so that private companies could participate in the distribution, transport and storage of products derived from oil refinement, gas and basic petrochemical products, since this was not against the Constitution. The Legislative reform approved excluded any specific mention to this activities except for the sale of these products, but the regime of transport, storage and distribution of these products remains a responsibility of Pemex and the reform approved for the Regulatory Law of article 27 did not make explicit the possibility for private companies to take part in these activities, which was the intention of the Executive.

While the initiative of Calderón incorporated the transfer of more managerial capacities and autonomy to the Administrative Council of Pemex, it did not include a modification of its conformation, however, the reform approved included the figure of four professional councilors that were named by the Executive and ratified by the Senate. This modification has, allegedly, politicized the administration of Pemex instead of making it easier.

The Presidential initiative included some modifications of the financing regime of Pemex, giving it the capacity to acquire credit and debt but restricted to the approval of these by the Treasury. The Legislative reforms approved included these modifications, but also permitted Pemex to raise funds without the authorization of the Treasury.

Calderón's initiative contemplated a broadening of the capacities and obligations of the Energy Regulation Commission with the clear intention of opening the hydrocarbons market to the participation of more actors and to promote competition in the sector. However, since the Legislative reforms approved didn't include explicitly any activities in which private participation was permitted, these new functions proposed for the Commission have not been included.

Finally, the Executive initiative included the creation of the Oil Regulating Commission that would support the Ministry of Energy in the planning of its activities regarding the oil sector, and also assisting it with technical elements and evaluations of oil exploration and exploitation activities, hydrocarbon reserves measurement and other technical elements. The creation of this Commission was replaced by the legislators with the creation of a National Hydrocarbons Commission, that will also regulate the gas industry. The important change introduced by the Congress was the appointment method of the Commissioners, nominated by the President and ratified by the Senate every five years but not all at once, and it was introduced in the law that these Commissioners could not be replaced till they finished their period, thus making these Commissioners a more independent body that the Executive intended originally.

television. He stated that, "Thanks to the patriotism, the vision and the high-mindedness of our legislators, Mexico has accomplished an achievement that can be described as historic, since this is the most important reform in this matter since 1938, when the oil industry was nationalized."⁶⁶ Both moves—the champagne celebration and the television message—were later shown to be mistakes.

The PAN governments have not only been poor reformers but also never wanted to confront the union. No major improvements in the labor contract have occurred in recent years. One example of the union's privileges is that Pemex cannot dismiss workers if their job isn't required anymore. For instance, if an oil well dries up, workers cannot be dismissed. Pemex is paying an estimated 11,000 workers for, literally, doing nothing. Some have estimated that this costs Pemex around 4 billion pesos per year.⁶⁷ Nothing public has been done regarding the generous though unfunded pension package of Pemex workers. At the end of 2009, the unfunded reserve for employee benefits was 576 billion pesos.⁶⁸

Although there was an attempt to confront the so-called Pemex-gate case, in the end, the government decided to negotiate with Carlos Romero Deschamps, the leader of the Pemex union, rather than prosecute him—even though it was demonstrated that money from Pemex went to the presidential campaign of Francisco Labastida, the PRI candidate for the 2000 elections, through the union, and that the PRI was sanctioned with a history-making fine of 1 billion pesos.

To make the trade union leaders happy, the first PAN-Pemex administration gave them resources that were not always clearly legal. Raúl Muñoz Leos, for example, was responsible for transferring 1.724 billion pesos to the union without the authorization of the Administrative Council. This violated several internal regulations.⁶⁹ The transfer helped the Minister of

Hacienda weaken Muñoz Leos but, as an indirect effect, strengthened the trade union vis-à-vis the Pemex administration.

The most evident sign of the weakness of the PAN administrations is the increase in the number of employees and the expenditures on personal services. These expenditures have increased 99.6% in real terms since 2000.⁷⁰

⁶⁶ Presidency of the Republic, *Reconoce el Presidente Calderón a legisladores que aprobaron la reforma de Pemex; se trata de un logro histórico, afirma*, speech made Mexico, October 28, 2008. Available at: <http://www.presidencia.gob.mx/index.php?DNA=85&Contenido=39711>.

⁶⁷ Data from the diagnostic elaborated by the outgoing director of Pemex in 2006. Quoted by Alma Hernández, "Mantiene Pemex a ociosos", *Reforma*, December 28, 2006: p. 1.

⁶⁸ Data from Pemex, *Estados Financieros Consolidados Al 31 de diciembre de 2009 y 2008, with the report from independent auditors*.

⁶⁹ Jorge Ramón Pérez, "Inhabilitan a ex director de Pemex", *El Universal*, front page, July 27, 2007. Available at: http://www.eluniversal.com.mx/hemeroteca/edicion_impresa_20070727.html.

⁷⁰ Own calculations from Pemex, *Balance primario y balance financiero de Petróleos Mexicanos y sus Organismos Subsidiarios con inversión PIDIREGAS, years 1997 to 2009*. Available at <http://www.ri.Pemex.com/index.cfm?action=content§ionID=14&catID=12148>.

Also, at the end of the Fox administration in the year 2006, Pemex had over 154,000 employees; by 2009, and considering that there has been a significant decline in oil production, it had more than 163,000 employees.⁷¹

Confronting the trade union is not easy. A strike could leave Mexico City and other major cities without gasoline in less than a day. For the same reason, it is difficult to confront other interests, like firms that transport gasoline. However, in the end, the weakness not only made reform unlikely, but they also hindered the distribution of labor and resources in general.

The PAN's moral authority to open up Pemex was undermined by very visible examples of PAN-related corruption at Pemex. The corruption was linked to areas that interacted with the private sector. An example of this was the case of the late Juan Camilo Mouriño, the former secretary of government, whose family owned a gasoline and fuel transport company, Ivancar. Mouriño, as legal representative of the company, signed contracts with Pemex valued at nearly 100 million pesos when he was undersecretary of the Energy Commission of the Chamber of Deputies in 2002. In 2003 he became chief of staff for Felipe Calderón, then secretary of energy, and the number of contracts signed increased. Although these contracts were actually allocated by the CANACAR, a trade association representing individual carriers within the Mexican trucking industry, through a stable formula used for years, the increase in the number of contracts was impossible to explain. In his defense, Mouriño argued: "It is petty to be accused of extracting economic benefits from politics, when politics was exactly what motivated me to resign to a legitimate patrimony, product of my personal and my family's effort."⁷² His defense was politically unconvincing and damaging. By claiming he had made a sacrifice by working in the government and was earning less, he was perceived as cold and distant or a liar. This case of alleged corruption was made public by Andrés Manuel López Obrador and was the beginning of a fierce opposition by several leftist parties to the oil reforms proposed by President Calderón.⁷³ The legitimacy of imposing reforms on the sector was undermined.

⁷¹ Data from number of employees of Pemex taken from Pemex, *Informe de Responsabilidad Social 2009 and 2006*, available at *Informes de Responsabilidad Social 2009 y 2006*. Available at:

<http://desarrollosustentable.Pemex.com/portal/index.cfm?action=content§ionID=2&catID=1181>.

⁷² Quoted from, "Versión estenográfica del mensaje del Secretario de Gobernación, Juan Camilo Mouriño Terrazo", Los Cabos, Baja California, February 28, 2008. Available at:

http://www.gobernacion.gob.mx/es/SEGOB/Sintesis_Informativa?uri=http%3A%2F%2Fwww.SEGO.B.swb%23swbpress_Content%3A830&cat=http%3A%2F%2Fwww.SEGO.B.swb%23swbpress_Category%3A3

⁷³ It has not been the only corruption scandal in the sector. Two of the sons of the wife of former President Fox were involved in a series of scandals linked to Pemex, a former Director of Refining of Pemex, Juan Bueno Torio, and now Senator, also came from a family with interests in the sector. According to several newspapers, Bueno Torio authorized a contract of 375 million pesos with a company named Aquapress, of which he was suspected to be a partner. However, this contract was assigned directly to the company, without any sort of contest, and it was signed, accounted for and closed on the same day. Roberto Garduño and Enrique Méndez, "Como director de Pemex Refinación, Bueno Torio benefició a la empresa de la que es socio", *La Jornada*, November 8, 2007.

The accusations linked to Mouriño show the power of this interest group. These contractors are not pro-market. They are happy in a world of crony capitalism, although they will always claim that they defend nationalism. They have the capacity to impose high prices and distribute the spoils among themselves. According to a high-level official, 6% of the total cost of gasoline is the result of collusion in the distribution of fuels. In an open market, such as the one in the United States, the cost of distribution is only around 3% of the cost of gasoline.

VII. After Calderón's Mild Reforms

To understand whether new reforms will take place, it is important to say a few words on whether recent reforms will work. If they do, new reserves will be found, production will increase, and there will be few incentives for further reforms.

A group of deputies of the Chamber of Deputies began a constitutional controversy against the law that regulates Pemex, the regulatory law from Article 27, and the administrative regulations enacted by the president. The arguments of this controversy are quite baroque. It claims that Article 2 incorporates a legal figure called the "state oil industry", which contemplates all of the activities that correspond to Pemex. According to the claimants, the group of deputies, if this definition of state oil industry is accepted, it would imply that another legal figure existed: a nonstate oil industry. This would contravene Articles 25, 27, and 28, which only refer to an oil industry as a concept inherent to the strategic area of hydrocarbons in possession of the State. Also, Article 21 states that the Ministry of Energy and the will impose the regulations under which the other decentralized organizations must operate regarding transport, storage, and distribution, as well as first hand sales destined to the national market. These provisions and the definition of firsthand sales allegedly conflict with the concept of nationalized oil industry, because it has been established that the State has to have absolute control over all links of the industrial chain of the national oil industry. Article 28 of the regulatory law for Article 27 of the constitution states that representatives of Pemex and its subsidiaries can sign contracts with persons or corporations to do specific work or services. According to the evidence

In the case of Manuel and Jorge Bribiesca, sons of Martha Sahagún, the special commission that investigated their case concluded that they negotiated with the director of Pemex, Muñoz Leos, that Pemex assigned contracts to a company named Oceanografía, in exchange for a commission. According to allegations made by the president of the Navy Commission of the Chamber of Deputies, this company was virtually bankrupt, and owed over 21 million pesos to the revenue service around 2000. However, by 2003 its capital was of more than 126 million pesos thanks to the contracts obtained by the Bribiesca brothers. During all of the Fox administration this company received contracts for almost 6 billion pesos. (Roberto Garduño and Enrique Méndez, "Empresa cercana a los Bribiesca fue beneficiada con millonarios contratos", *La Jornada*, October 18, 2007).

presented, this validates the so-called “risk-contracts” that are constitutionally prohibited.⁷⁴

The new law created new regulations, but none of the old regulations were abolished. The original idea was to deregulate, but the result was over-regulation. Furthermore, Pemex has had to suffer an extra layer of control in the form of the professional members of the board –positions created by the reform measures. The appointments of the professional board members were politically motivated; as is usually the case when the Senate has to approve a group of allegedly independent counselors, they are less independent than expected or intended. Moreover, as they are working fulltime and chairing important committees, they start acting more like managers than advisers. The Organisation for Economic Co-operation and Development (OECD) has criticized the role of these professional counselors, accusing them of acting more in accordance with political or group interests outside of Pemex and thus hindering the correct implementation of the 2008 reform.⁷⁵

Nevertheless, the professional board members play a critical role that should help increase accountability, although this can be painful for an administration used to few criticisms. For example, Rogelio Gasca Neri, one of the professional advisers, has stated that the Pemex business plan is not based on the company's needs, so its goals are unrealistic. He has said that the money invested in Pemex has not led to expected production levels, since funds are allocated according to the federal government's budgetary concerns instead of the real ability of Pemex to extract and export oil. In 2005, he has stated, it was said that with an investment of US\$20 billion, Pemex would produce between 6 and 7 million barrels of oil per day and up to 14 billion cubic feet of natural gas. Though the investments were made as scheduled, Pemex only extracts around 2.6 million barrels of oil daily.⁷⁶

Pemex officials also tend to complain of the active role played by another entity created by the new law, the Comisión de Hidrocarburos, which has as its main objective to supervise the exploration and extraction of oil and gas. Nevertheless, the commission has helped Pemex focus on the problems at Chicontepec.⁷⁷

The more evident gain of the reform was the authorization of a new type of contracts, that pay the *contratista* based on its results.⁷⁸ The new rules, however, have been very difficult to implement. The dispute with respect to the constitutionality of the reform is, of course, one reason behind the delay, but there was a lot of resistance within Pemex. The Supreme Court declared,

⁷⁴ Israel Rodríguez, “Admite SCJN la controversia constitucional de los diputados contra la ley de Pemex”, *La Jornada*, October 27, 2009.

⁷⁵ Alma Hernández, “Descalifica OCDE a consejo de Pemex”, *Reforma*, June 17, 2010.

⁷⁶ Margarita Palma, “Irreal plan de negocios de Pemex por modelo mixto de gestión”, *El Economista*, July 5, 2010: 28.

⁷⁷ Alma Hernández, “Quema Pemex millones”, *Reforma*, business section, March 22, 2010.

⁷⁸ Risk contract are linked to the value of the oil produced. The Pemex is based on a success fee linked to the number of barrels found. The oil found belongs to Pemex.

in February 2011, that the new Pemex law and the regulations enacted by the president are in accordance with the Constitution of Mexico. The new law for contracting services is now in effect, but it took more than two years after its approval to actually implement it.

Finally, these new contracts seem to be ready to operate, and, at least publicly, the general director of Pemex is confident the new rules will enhance the ability of *contratistas* to do their jobs. However, contrary to expectations, Pemex will start using this new legal framework for only three marginal oil camps.⁷⁹

Do those who enacted the reform want to defend it? In the PRI, the problems of implementing the new law are blamed on the shortcomings of the *panistas* (members of the PAN party) in government. In the government, some are beginning to believe that they were trapped, but this is difficult to say publicly, as President Calderón praised and celebrated the reform after Congress approved it.

Pressure to pick up the pace of reform came from our borders. For instance, the United States was to start drilling in common areas of the Gulf of Mexico in 2011,⁸⁰ although the BP oil spill has made this issue less pressing.⁸¹

As David Shields commented, Pemex continues to be “an atrophied, bureaucratized, politicized, and over-regulated institution.”⁸² In a personal interview with him, Shields gave a single example: Pemex's inability to buy five ships for moving oil products. The bid took thousands of hours and in the end it was annulled.⁸³ If they cannot buy ships, what do they expect when they decide to contract for more sophisticated services? Many international companies are just not interested in bidding, as Mexico's laws are too complex, and many others use a Mexican firm to bid. This increases the costs of actually providing the service by no less than 10%.

The view from Pemex's administration is more optimistic. In a presentation to businessmen in Mexico City on October 7th, 2010, the current general director of Pemex, Juan José Suárez Coppel, said that reforms gave Pemex the obligation to enhance the value of our oil and gas reserves for all

⁷⁹ <http://www.reforma.com/negocios/articulo/581/1160480/>

⁸⁰ This issue doesn't seem to be so urgent to attend at the moment, since a moratorium has been signed to delay the drillings till 2014, so it will be an issue that the next Mexican president will have to deal with. Foreign Relations Ministry, *Comunicado conjunto de los gobiernos de México y Estados Unidos de América*, Mexico, June 23, 2010. Available at: http://www.sre.gob.mx/csocial/contenido/comunicados/2010/jun/cp_193.html.

⁸¹ Some critics in Mexico have argued that the accident shows these big firms are lousy; so Pemex should do it directly. In fact they are starting to do it with three large platforms recently arrived. One of the challenges Pemex faces if performing this duty directly and alone is that all the potential liabilities would lay on the shoulder of Pemex and of the Mexican Treasury, although some argue that as a sovereign entity any claim should have to be settled in Mexico, not in the US courts, so the risk is much smaller.

⁸² David Shields, “Visión de Pemex”, *Reforma*, Business section, October 13, 2010: p. 4.

⁸³ Interview with David Shields, October 14, 2010.

Mexicans. The law could be better, but it gives the administration the means to achieve that end.

The main message offered by Suárez Coppel is that production is stabilizing and should start growing slowly. In his view, the limitations faced by Pemex are mainly technical. However, contracting services, plus investments in management and technology within Pemex, should allow the company to increase reserves and production as current geological information shows there is still a lot of potential.

Nonetheless, an investment of around \$26 billion or around 360 billion pesos per year from 2010 to 2019 will be needed to maintain or grow production. This is the real challenge, although Pemex's investment expenditures have been growing in the last year (see Figure 5).

In the view of Suárez Coppel, one should blame the very high taxes paid by Pemex, and not the workers, for the lack of resources. The payroll amounts to around 100 billion pesos, so excess personal is not a key problem, although current labor obligations amount to 650 billion pesos. They will have to be funded by the government. In his view, the lack of funding for these obligations is not the responsibility of Pemex or its workers.

In my view, most of Pemex problems are not technical, but organizational and strategic due to the lack of competition. The methods they are adopting will preserve production for a few years but offer no long-term solution. Additional funds have given Pemex more room to maneuver, but nothing fundamental has changed. It is likely that production will continue to decline, so Mexico will be obliged to start thinking about the need to associate with other firms. It will also need to favor competition as the means for disciplining a firm that is so big and that has so many stakeholders profiting from the current and relatively inefficient status quo.

Conclusions

Although Mexico was seen as a leading economic reformer throughout the 1990s and democracy finally arrived in the country in 2000, the government barely touched the energy sector. All presidential administrations have tried to address the Pemex challenge by basically proposing that Pemex can fulfill its objectives without the pressure of competition. Because Pemex is so inefficient, they have also believed there is ample space for improvement. It is only a question of managing better Pemex, the presidents say.

In the Salinas administration, better management meant Pemex was divided into subsidiaries. The Fox administration tried, unsuccessfully, to reunite the subsidiaries into a single entity. The current administration believes that the new rules will allow the implementation of better mechanisms for contracting services—it is just a question of political will and managerial capacity. In their view, Pemex does not lack resources or technical and managerial capabilities.

If Pemex does manage to maintain and increase production, the pressures for reform will decrease. However, one of the reform measures resulted in additional funds for Pemex, so now we can start to discuss whether Pemex is efficient or not. Pemex can no longer claim it has been left to starve.

The current situation, in which the most important actors defend the status quo, is based on the idea that oil production has stabilized and can even start increasing again. For those opposed to any major reforms, it is critical that Chincontepc, the biggest known reserve in Mexico and one that is currently being drilled at a high cost, operates efficiently. If it does not, especially after all of the money given to Pemex, we could enter a period of crisis.

A crisis does not imply that we are suddenly left without oil, but that such an event is perceived as inevitable. In this case, there will be a lot of fiscal pressure. Higher taxes or less government spending will be needed to keep public finances in order. Both tax and expenditure reforms are highly divisive and politically complex to achieve. Mexico's government and society are addicted to oil. Only with withdrawal symptoms will there be the incentive to start moving in a different direction.

Nevertheless, a crisis does not automatically lead to reform. It has to be agreed that the crisis is unavoidable and not just a question of better management for Pemex. It has to be a profound crisis and not just a continuation of current unproductive paralysis.

The trade union is, without a doubt, an important constraint. However, dubious *contratistas* and corrupt, or just incompetent, administrative decisions are likely to be even more costly to Pemex. As accountability is weak, no one pays a price for inefficiencies or for avoiding tough decisions.

Pemex is a monopoly whose problems stem from its centralized management. The solution is not as simple as having a better general director of Pemex. It seems unlikely that the situation at Pemex will improve without competition in all relevant markets, including exploration and production. Only a breakthrough similar to the discovery of the Cantarell field could allow Pemex to continue within its current institutional framework.

Nationalist ideology helps those who profit from the status quo to justify the current rules. Antimarket forces are strong in Mexico and were reinforced after the 1994 economic crisis. Nevertheless, the most pro-market presidential candidates have won the two presidential elections that were open and competitive, those of the years 2000 and 2006, although this election was contested by López Obrador. Ideology did not impede change in other areas, as discussed throughout this paper. Currently, a majority of Mexicans are in favor of NAFTA, for example.

No leader of a political party in Mexico has invested his or her political capital trying to change public opinion about oil sector reforms. No president has wanted to risk confrontation with the powerful interests behind the status quo and since production and resources are balanced in the public account, there are few incentives to reform the oil sector.

A confrontation with special interests is probably needed to reform the energy sector. According to Jonathan Kartt, Petrobras reform was possible in Brazil because “Cardoso politicized unpopular oil worker strikes to demonize leftist and nationalist opposition to reform. Thus, reforms depended on the appearance of a politically capable, reform-minded leader, and on a confluence of events favorable to reform; without these circumstances, steps to clean up the energy sector might not have occurred.”⁸⁴

How to convince people that the trade union, *contratistas*, and bureaucrats are hijacking the state symbol, Pemex? In a democracy, demands for more efficient management and more rational institutional frameworks should be observed. But for this to happen, you need a political system that effectively includes the less well-off and that has the capacity to use oil rents to deliver public goods. This will help create a substantial coalition in favor of reform.

Calderon's strategy was to enact smaller changes to create momentum for more significant changes. However, the results of the reform so far are so weak, and they do not seem to have created the momentum for further reforms. As argued, the only impetus for reform is a serious contraction of oil production or a decline of fiscal income due to lower oil prices.

An assessment of the likely evolution of Pemex production and its current capacity to export, which will be addressed in other papers in this series, is, in my view, fundamental for an understanding of the likelihood of reform. It is

⁸⁴ Jonathan Kartt, “It Could Have Been Much Easier: Petrobras and Lessons from the Brazilian Experience with Nationalized Energy”, *Bologna Center Journal of International Affairs*, vol. 10, spring 2007: p. 94.

worth noting that how quickly we reach a crisis point depends not only on the capacity to increase oil production, but also on the growth of domestic demand for oil. These factors will depend on the pace of Mexico's economic growth and the availability of alternative-energy vehicles. The paradox, however, is that because of the lack of reforms, including oil reform, Mexico probably will not grow as much as most models that calculate future gasoline demand predict. Therefore, there will be less demand and less pressure for reform. If alternative-energy vehicles are imported from abroad, Mexico will become less dependent on oil and demand will drop.

It has been argued that the successful dissolution in October 2009 of Luz y Fuerza del Centro (LyFC) will help pave the way for major changes at Pemex. The two cases, however, are very different. The main difference is that the president had the legal right to make the decision about LyFC through a presidential decree, and no privatization issues were involved. CFE took over the management of LyFC, and the services provided by LyFC in central Mexico continued without disruption. It seems that originally the government wanted a new state-owned company to substitute for the LyFC. CFE wanted to avoid such an outcome and, in the end, absorbed LyFC.

If the dispersion of power is one of the reasons behind the inability to push through reforms, is it reasonable to expect a party that won enough seats to successfully enact reforms? Would the likelihood of such an outcome increase, for instance, if PAN again won a presidential election (a scenario that currently seems very unlikely). However, as no party can have the qualified majority it needs (as it is stated in the Constitution), the real changes that require constitutional reforms will still need at least the PRI, which would be reluctant to help. If the PRI were to win the presidency, currently the most likely scenario, it could probably count on the support of the PAN if the PRI wanted to enact reforms (an unlikely situation for the reasons argued in this paper).

Is the solution to ensure that a party that wins the presidency has a majority in the two chambers? First, this scenario is unlikely to happen. It is very unlikely that any of the parties will risk losing their ability to influence future reforms (in case they do not hold the presidency and become the minority party, as in the years of PRI dominance). The PRD is not interested in such changes and could derail any effort in that direction. Moreover, the checks and balances of the current system can be helpful if a president who is against market reforms in other areas gets elected, as in Venezuela or Argentina.

The likelihood of a PRI victory in the next presidential election could make PRI politicians pragmatic with respect to the need of reforms, including oil reforms. In theory, it is a logical scenario, but pursuing "neoliberal" reforms before an election can be very costly when powerful groups are affected and when voters seem to be against such reforms. In the long transition between

the two administrations, it is technically possible to envision such reforms, if the new president is in favor of them. However, this is politically very complicated, as no one is fully responsible during the transition.

The wrong way to confront a complex issue like Pemex reform is to believe there is a magic key that will solve the problem. For a reform to work it has to be quite radical and clear-cut. It must include associated reforms, such as a strong regulatory agency to ensure that no player goes beyond what is authorized. Moreover, if Pemex becomes a private company, it would have to pay a share of its profits to the workers, as does any firm in Mexico, according to the country's constitution.⁸⁵ Any reform should include a transparent method of selling reserves to Pemex, which currently assumes all oil in Mexico is its property.

Poorly designed reform measures can be stalled for a long time or give new actors too much power. An example of stalling involves a constitutional reform that allowed *ejidos* to become private property. Few *ejidos* were actually privatized because of, among other reasons, bureaucratic resistance. A constitutional or legal reform can always be undermined through bureaucratic politics, as has been the case with Calderón's mild reforms. An example of the risk of giving new actors too much power involves the privatization of TELMEX, the communications company. Power and resources were transferred to a private firm that was poorly regulated. Mexico is still suffering the consequences. Such a fiasco could happen with oil, and, as bad as the situation seems today, bad reforms could make them even worse.

⁸⁵ From an interview with Jaime Serra, *op. cit.*

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