HEMISPHERE 2000

Series VII, Issue 5
July 27, 1999

Energy Alert:

North American Energy Market Hits A Little Bump in the Road

by Joseph M. Dukert

Anti-Dumping Petition

Although it is not on the official agenda of the hemispheric energy ministerial conference this week in New Orleans (July 28-30), a topic of discussion and some concern is bound to be an anti-dumping petition filed by small independent oil producers in the United States who seek high retaliatory tariffs against petroleum imports from Mexico, Venezuela, and two Persian Gulf countries (Saudi Arabia and Iraq). Fortunately, although such complaints in various fields have often won relief, this one will probably do little more than stir up trouble temporarily. An unintended benefit, however, could be to spotlight the recent birth of a true North American energy market, which seems destined to become ever more robust in spite of this and some other roadblocks it still must surmount.

Overview

- Oil-dumping charge slows progress toward an increasingly solid North American energy market with mutual benefits.
- U.S.-Canadian energy trade still overshadows exchanges across the southern border, but complementary links with Mexico have been expanding.
- The North American Free Trade Agreement (NAFTA), regulatory reform, privatization, and the new "Btu market" have transformed groundrules.

A victory for the dumping petition (whose merits are questionable, to say the least) would force the United States to look elsewhere for at least 30 percent of all the crude oil it now imports, because the tariffs called for would effectively halt Mexican and Venezuelan imports entirely. Energy Secretary Bill Richardson, who was rebuffed when he offered to mediate, warns also that a protective wall of this sort would push up U.S. prices on gasoline, home heating oil and other petroleum products.

However, the petitioners have yet to win official "standing" to pursue their request; and now that world oil prices have recovered from recent lows, the independents may not continue to insist that

Mexico's Pemex and other national oil companies use lower accounting prices for internal use than they are able to charge for exports. After all, the real goal of the petition may well be simply to win some new legislative concessions that will make sure they can continue to operate their own "stripper wells" — whose output of 10 barrels a day or less is economical only if oil prices stay above a certain level. (For a country like the United States — a huge petroleum producer as well as the world's largest consumer — one man's "subsidy" is another man's needed "incentive").

Nevertheless, Mexico was sufficiently startled and offended by the charge that on June 30 Energy Minister Luis Téllez backed away from a unilateral offer that would have totally eliminated all remaining Mexican tariffs on U.S. natural gas the following day — years ahead of the NAFTA schedule. Meanwhile, Venezuela is in the throes of drawing up a new national constitution at the same time it struggles to lift itself from an economic swamp; so energy policy under its new president, Hugo Chávez, is less clearly focused.

Canada Also Concerned

Mexico's instant rejoinder drew quiet attention from Canada as well as the United States, because a continental market for all forms of energy has been evolving inexorably. Although the U.S. is a modest net exporter of natural gas to Mexico, it depends on Canadian gas for one-seventh of all use — and that percentage is rising steadily.
Environmental goals are pushing all three countries in North America (and, indeed, around the world) toward greater reliance on relatively clean-burning natural gas, whose combustion also releases far smaller quantities of carbon dioxide — thought to be a contributor to potential global climate change. But production of gas anywhere responds first and foremost to demand from end-users to whom it can be delivered; and an interconnected market can multiply demand on a year-round basis, instead of being subject to wild "peaks" and "valleys" of both price and supply. Five new pipelines starting up within two years will be able to boost gas imports from Canada by one-third. At the same time, the emergence of electronic trading for gas and the simultaneous opening of the pipeline and energy commodity markets to competition serves as a satisfactory lid on what consumers have to pay. But pennies added to the wholesale price of gas by the residual Mexican tariff are enough to curb sales in that direction for a while.

Mexico has moved more quickly than one might have expected toward allowing this expanding market to set energy prices on its own. Pemex, the national hydrocarbon enterprise, is likely to remain almost exclusively state-owned; but it has come to base its formerly arbitrary internal pricing of gas on a "basket" of wellhead prices at several points in Texas (allowing for transportation differentials). In fact, in this new era, Mexico has even been able and willing to buy gas from Alberta, Canada. It isn't necessary for the actual gas molecules to travel hundreds or thousands of miles from seller to buyer; this becomes a bookkeeping transaction within the network that imputes transportation costs (and even temporary storage if necessary) via a variety of "hubs." But the effect is that sellers are able to sell more gas (at all times of the year) while buyers benefit by being able to shop around for the best price. This is especially meaningful since gas-delivery networks in Mexico are being privatized and traditional energy monopolies in both Canada and the United States are disappearing.

Interdependence and Electricity

A trilateral pattern is also developing in electricity, for which the three NAFTA partners have already eliminated all tariffs. Most of Canada and a portion of Mexico also participate with the United States in the North American Electric Reliability Council (NERC), a planning and coordinating body that is transforming itself into a self-regulating organization with powers to enforce compliance and thus help protect against outages.

Mexico has joined the others in encouraging private generation, and President Zedillo hopes to open up the industry further before his six-year term ends next year. With a fast-growing population and a desperate urge to raise living standards, Mexico knows that it can reach its goals only by allowing private investment in new power plants — and probably by more cross-border trade in electricity too.

Privately financed generating stations are popping up all across the northern part of that country, including some that are fueled by gas being brought in from the United States. Last year one U.S. firm (NRG Energy, Inc.) began what is likely to be a two-year process to get White House permission to build a high-voltage transmission line from the Palo Verde nuclear plant in Arizona all the way to Mexicali. In turn, the San Diego area helps to meet its summertime air conditioning needs with electricity produced by Baja California's geothermal fields. Yet exchanges of electricity between Canada and the United States — invigorated by the bilateral free trade agreement that preceded NAFTA — are still about 40 times as great as those across our southern border.

Within all three countries the boundaries of rivalry that have divided the gas and electricity markets from one another are fading too. "Energy marketers" — who buy, sell, and sometimes produce both commodities — are helping to smooth out both domestic and international trade, making it more efficient and thus trimming costs. They deal matter-of-factly in terms of pure energy content — British thermal units or "Btu's".

Interestingly, all three countries continue to be simultaneous importers and exporters of petroleum. Rich deposits in western Canada enable that country now to supply the United States with more than we buy from Saudi Arabia, if refined products are included. Yet, at least until offshore Newfoundland fields reach full production, it makes economic sense for eastern Canadian provinces to purchase oil from abroad, including some U.S. products that will probably continue to flow even then.

Mexico outranks Canada slightly as a supplier of crude oil to this country, yet it imports almost 150,000 barrels per day of U.S. refined petroleum products. If the now-permissible private investment in Mexico's gas transmission and distribution infrastructure gives Pemex enough wiggle room to finance its own development of gas resources in the northeast, a similar two-way trade in that fuel — split between east and west — could prosper likewise for both countries.

Forthcoming Study

The complex interrelationships of North American energy trade across the board (including the outlook for nuclear power, hydroelectricity and other renewable sources) are treated in a new study to be published by the Center for Strategic and International Studies later this summer. It appears that the bonds have become strong enough to survive temporary setbacks such as the ongoing flap over dumping — and even the nationalistic rhetoric that is almost sure to accompany the Mexican presidential campaign next year.

But this week the energy ministers from a broader community (the whole Western Hemisphere) will be talking gingerly about the unanticipated interposition of the dumping case. It's lucky that in recent years they have institutionalized a forum in which they can discuss such problems calmly and on a regular basis.

ABOUT THE AUTHOR

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