



Mexican and Canadian Energy Monthly

August 2020

| | | | |
|------------------------------------|-----------|---|--------|
| CA - Alberta On Peak | \$77.51 | ↑ | 34.1% |
| CA - Ontario On Peak | \$24.25 | ↓ | -12.6% |
| CA - Union Dawn | (\$0.268) | ↓ | 386.4% |
| CA - Northwest Sumas | (\$0.220) | ↑ | 95.6% |
| MX - Interconnected System Power | \$559.55 | ↑ | 11.6% |
| MX - Baja California Power | \$561.81 | ↑ | 136.6% |
| MX - Average Gas Price (USD/MMBtu) | \$2.37 | ↑ | 11.4% |

* Change vs previous month's close, in local currency

CA - Canada / MX - Mexico

*Pricing data from ICE, CENACE

Managing Editor:

Beau Walker

Contributing Editor:

Jude Clemente

Contact:

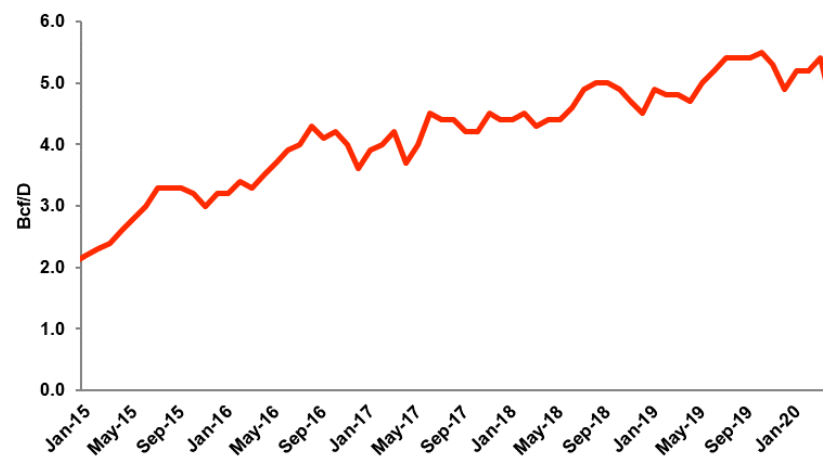
502-214-9400

Mexican and Canadian Energy Monthly is published by Trane Energy Supply Services for exclusive distribution to Trane clients. Data and information published in Weekly Market Summary are gathered and provided through proprietary and public sources and are published with the intention of being accurate. No part of this Mexican and Canadian Energy Monthly may be reproduced, distributed, or transmitted in any form or by any means, including photocopying, recording, or other electronic or mechanical methods, without the prior written authorization of Trane Energy Supply Services.



Mexico

- An improved natural gas pricing environment in Mexico should help present more E&P opportunities. The EIA has gas prices averaging \$1.93 per MMBtu this year but rising to \$3.10 next year. A significant increase in domestic output would be a huge lift for a country that now imports over 80% of its natural gas. In fact, state-utility CFE is being encouraged to form a subsidiary dedicated to gas E&P, given that it utilizes gas for over 60% of its power generation.
- If the EIA forecast for 2021 holds true, that would translate into natural gas prices in Mexico averaging \$3.50 per MMBtu, which is significantly higher than what the country has been seeing. Yet still, higher price forecasts for both Mexico and the U.S. assume lower gas production in both countries, something that rising oil prices might be able to counteract.
- Regardless, Mexico will remain dependent on U.S. gas for many years. Even though Mexico's gas demand is growing fast, state-owned Pemex will remain focused more on crude oil production because it brings in much more money for the government. Oil sales account for some 25% of the federal budget.
- The Energia Costa Azul natural gas export project in Mexico's Baja California is still waiting on federal approval. IEnova maintains that it is committed to the project but there is still no fixed date for a key permit to be granted. The project will be importing gas from the U.S. and then exporting it from Mexico's western coast. Some critics, however, point to the fact that Mexico itself is in desperate need of natural gas to fuel a population that is mostly poor.



Natural Gas Imports from the United States

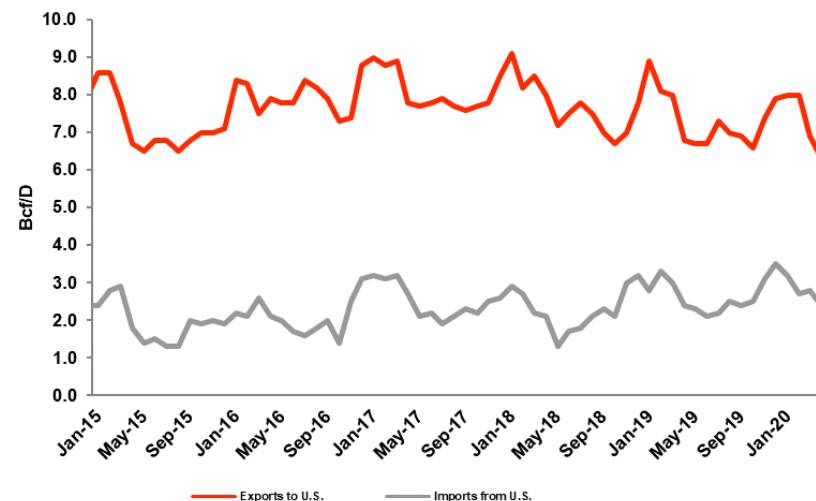
Mexico's gas imports from the U.S. have been provided a boost in the past few weeks. The southern-most segment of the Wahalajara system, the Villa de Reyes-Aguascalientes-Guadalajara pipeline, has been completed. The system is a group of new pipelines that connects the Waha hub in West

*EIA, August 2020



Canada

- For the third time this year, the Petroleum Services Association of Canada is lowering its forecast for drilling activity, forecasting that only 2,800 wells will be drilled in 2020. This would be the lowest level in nearly 50 years and is well down from the 4,900 wells drilled in 2019. Globally suppressed prices and an abundance of supply is limiting drilling activity.
- The Canadian LNG Alliance, the leading advocacy group for the LNG industry in Canada, recently released a report highlighting potential economic impacts of LNG export growth in Canada. The report discusses a scenario where Canada is exporting 56 million-tonnes per year (approximately by 2034, adding over 96,000 jobs along the way). The LNG Canada project, currently underway, is the first export project in British Columbia, though 12 other projects have been proposed on the West coast of the country and an additional five have been proposed for eastern Canada. Canadian LNG would hold a key advantage over Gulf-produced U.S. LNG as it has a much closer shipping route to high-demand markets in Asia.
- Power consumption fell in April and May of 2020 compared to 2018 and 2019 levels, as industrial consumption, the largest consuming sector in Canada, decreased due to COVID-related shutdowns and low oil prices. From mid-April to mid-May, power consumption fell 5.5%, compared to a 2% decline over the same time period in 2019. Residential consumption did increase since stay-at-home orders increased demand.
- Crude oil prices increased in May, though remain well below year-ago levels and may not get back to “normal” levels until 2021 as the market remains oversupplied.



Canadian Gas Exports and Imports

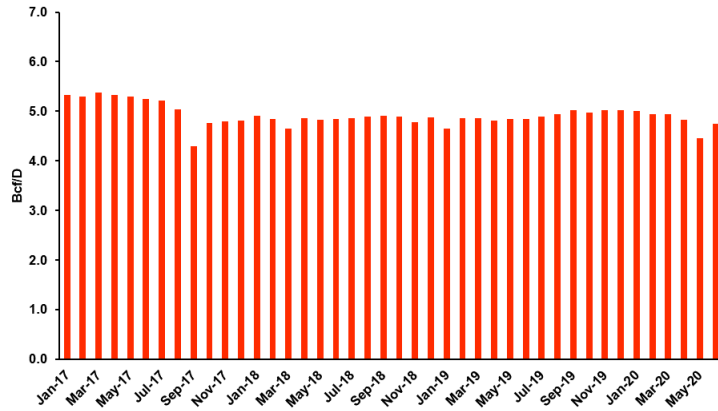
Year-to-date gas exports to the U.S. fell compared to year-ago levels as price spreads between Canadian natural gas and the corresponding U.S. pricing points fell, lowering incentives for U.S. purchasers to import Canadian-produced natural gas.

*EIA, August 2020

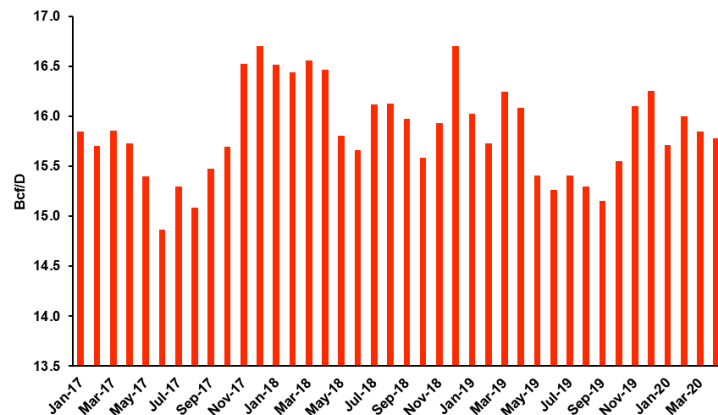


Natural Gas Production

Mexico (SENER, August 2020)

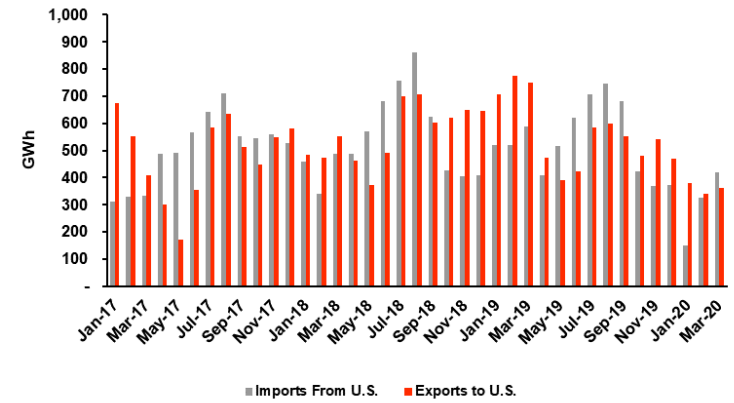


Canada (Canada Energy Regulator, August 2020)

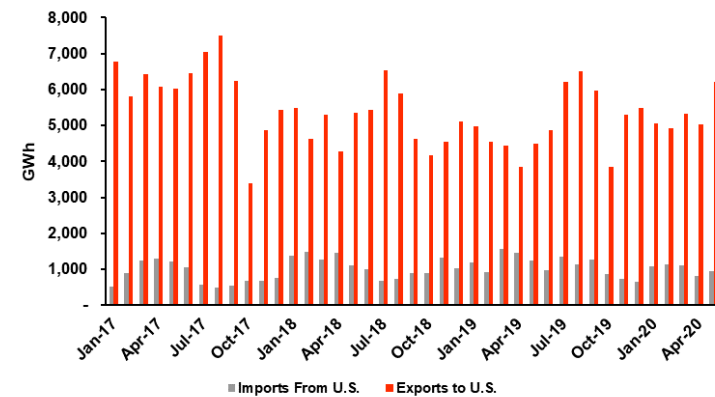


Power Flows

Mexico (EIA, August 2020)



Canada (Canada Energy Regulator, August 2020)





Mexican Deregulation

Natural Gas:

- Gas pricing in Mexico's industrial capital city of Monterrey has been in the \$1.60 to \$2.00 per MMBtu range over the past two months, including transportation and generally tracking the U.S. price. Back in November, prices spiked and almost hit \$3.00, steadily falling since. Monterrey has the natural advantage of being closer to the U.S. border, accessing low-cost U.S. supply. Farther south, for instance, prices in Guadalajara have averaged closer to \$2.50.
- As more pipelines connecting Mexico to the U.S., especially if linked to the extremely low-cost Waha hub, are built, Mexico could see even more downside to pricing. The issue, however, is that Mexico's growing reliance on the U.S. stands in contrast to the 2013 energy reforms that hoped to install more self-sufficiency in the country.
- Energy Regulator CRE has given the greenlight to the country's most recent energy planning document, known as the Plan Quinquenal, over the next five years. One key strategy is to collaborate with private gas market participants and create a northern based gas hub, planned to be called Las Adelitas. More pipelines connecting to south Texas are also critical, with Enbridge and IEnova leading that private effort.

Power:

- Mexico's power generation capacity continues to favor natural gas, although wind and solar capacity is gradually expanding. Overall, gas accounts for some 60-65% of capacity, with wind at 8% and solar at nearly 5%. Hydro represents 16% and has been promoted by the AMLO administration as the renewable source that might have the best chance to significantly increase—despite the country having expansive water shortages.
- The renewable generation providers have been pushing back against a federal order to maintain "must run" rules for CFE to keep gas plants operating. The administration has been accused of unfairly favoring gas under the guise of system reliability. Many feel that the contracts awarded for renewable energy developers under the 2013-2014 constitutional energy reform are being violated by such an order.
- In fact, the federal government is now looking at allegations that officials at CFE signed fraudulent contracts with private energy companies before AMLO took office. Some private firms have been complaining of obstacles that have increased their distribution costs, making them less competitive in the marketplace. The Spanish company Iberdrola has received the most criticism from AMLO. The good news, however, is that private investment in the country remains strong, with many realizing that the upward potential for energy demand remains very strong.