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Exclusive: Pemex plans debt refinancing, greater output as path to healthier balance sheet

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LEON, Mexico (Reuters) - Mexican state oil company Pemex plans to refinance $2.5 billion in debt this year while trying to revive oil output to boost income, the firm's chief financial officer said, as pressure mounts from ratings agencies over the company's performance.

FILE PHOTO: A sign of state-owned company Petroleos Mexicanos (PEMEX) is seen at a gas station in Monterrey, Mexico June 17, 2019. REUTERS/Daniel Becerril/File Photo

Alberto Velazquez, the CFO, said in an interview that the $2.5 billion mostly includes outstanding bonds. Pemex is trying to stop its net financial debt, which reached $106.5 billion last year, from growing through 2021 and after that the company will seek to cut it, he said.

Velazquez said the refinancing operation would complement the renewal of some $5.5 billion in credit lines the company has with banks, already announced by Pemex but not yet completed.

Besides the domestic and international capital markets, Pemex will explore "bilateral contracts with banks" for the refinancing, even at higher costs after a downgrade by rating agency Fitch earlier this month, he said.

"It is not what you would want in terms of interest rates, but that's the market," Velazquez told Reuters on Thursday afternoon after participating in an oil industry event.

Fitch cut its rating on Pemex's $80 billion of bonds from investment grade to speculative grade, or "junk," with a negative outlook. Many investors expect a second downgrade from Moody's Investors Service to formally confirm Pemex as a junk credit. If that happens, some funds whose mandates prohibit holding such assets would have to sell their Pemex bonds.

Yield spreads on Pemex bonds - indicative of the premium investors demand for holding them rather than safer U.S. Treasuries - have climbed in recent weeks, amid doubts about plans by Mexican President Andres Manuel Lopez Obrador to turn around a company that was once a symbol of Mexico's self-reliance.

Pemex also will likely negotiate again for a 2020 oil hedge to protect its export revenue from an unexpected drop in price, but changes to a price formula for starting talks with banks have not yet been finished, Velazquez said.

Brokers and traders have requested Mexico, a producer of high-sulfur fuel oil, to adjust its oil basket price formula which include that fuel oil variable to reflect new rules by the International Maritime Organization starting next year to reduce maritime fuel's sulfur content.

The changes have contributed to delays in negotiations for Pemex's and the Finance Ministry's hedges for 2020, but Pemex hopes to cover about 35% of its current production level of nearly 1.7 million barrels per day (bpd) with the program.

SKIPPING BAD RATINGS

Velazquez, who believes Pemex has been excessively punished by rating agencies, said the state-run company is focused on addressing long standing issues highlighted by those firms including high financial debt, heavy tax load and insufficient investment in its core business, exploration and production.

"We have put our attention on not neglecting our plans... because that will allow positive ratings in further evaluations," he said.

Pemex is also banking on being able to reduce its tax bill by $8.89 billion between 2019 and 2021, Velazquez said, adding that Lopez Obrador's government already issued a decree for this adjustment and only additional paperwork is needed to complete it.

"We are aware of the risk," Velazquez said, referring to potential new credit downgrades, but added that Pemex is showing better financial results including benefits in April and May, savings from an anti-fuel theft plan, lower costs for exploration and production contracts and cuts to expenses.

On the production side, Pemex expects to add some 260,000 bpd of new crude output from 22 shallow water and onshore fields in the next few years.

There are "core problems that we cannot solve in the short term ... but I think all rating agencies have acknowledged and understood that we are acting in a straight-forward way to

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address these problems," Velazquez said.

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