

# Petroleos Mexicanos (Pemex)

## Full Rating Report

### Ratings

#### Foreign Currency

Long-Term IDR	BBB+
Senior Unsecured	BBB+

#### Local Currency

Long-Term IDR	A-
National Long-Term Rating	AAA(mex)
National Short-Term Rating	F1+(mex)

IDR – Issuer Default Rating.

### Rating Outlooks

Long-Term Foreign Currency IDR	Stable
Long-Term Local Currency IDR	Stable

### Financial Data

#### Petroleos Mexicanos (Pemex)

(USD Mil.)	LTM	
	3/31/15	12/31/14
Revenue	106,461	119,398
EBITDA	45,731	57,198
EBITDA Margin (%)	43	48
FFO	2,455	4,805
FCF	(14,065)	(10,470)
Cash and Mkt. Securities	8,487	8,017
Total Adj. Debt	183,058	177,832
Total Adj. Debt/EBITDAR (x)	3.4	2.6
FFO-Adjusted Leverage (x)	12.8	9.5
EBITDA/Gross Interest Expense (x)	11.7	14.8

### Related Research

Fitch Affirms Pemex's Foreign & Local IDRs at 'BBB+'/'A-' & National Scale at 'AAA(mex)'/F1+(mex)' (May 2015)

### Analysts

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### Key Rating Drivers

**Strong Linkage to Government:** Petroleos Mexicanos (Pemex) is the nation's largest company and one of the Mexican central government's major sources of funds. During the past five years, Pemex's transfers to the government have averaged 52.6% of sales, or 108.4% of operating income, and contributions from Pemex have averaged 30%–40% of government revenues. Despite pari passu treatment with sovereign debt in the past, Pemex's debt currently lacks an explicit guarantee from the government.

**Oil Production Decline Stemmed:** Cure oil production, which is currently at approximately 2.3 million barrels of oil per day (mmbopd), has continued to marginally decline in recent years, although not at the same speed as it did during a precipitous fall in 2008–2009. The company's goal to increase production to 3mmbopd in the medium to long term will depend on its ability to implement new technology on mature fields, improve operations and increase production from a diversified number of fields. The diversification of the oil production asset base, with Cantarell oil field representing less than 20% of oil production, reduces the risk of large production declines in the future.

**Energy Reform Long-Term Positive:** Although Pemex's credit ratings will continue to be highly linked to those of the sovereign, the reform would likely give the company financial flexibility through budgetary independence and greater investment flexibility. The company would also benefit by partnering with international oil and gas companies to share exploration risk. The reform's overall impact on Pemex will be positive but gradual and the company will continue to face heavy tax burdens, while its current tax regime remains unchanged.

**Negative FCF from Taxes/Capex:** Fitch Ratings expects the company to show negative FCF over the foreseeable future, considering Fitch's price deck, as it continues to implement sizable capital investments to sustain and potentially increase current production volumes. The company's historical significant tax burden has limited its access to internally generated funds, forcing a growing reliance on external borrowings.

**Strong Pretax Credit Metrics:** Pemex's leverage at LTM March 31, 2015 was strong on a pretax basis, with total debt/EBITDA of 1.8x and adjusted leverage of 3.4x. Total debt was USD84.4 billion, which more than doubles to USD183.1 billion when adjusting for the unfunded pension plan and other post-employment benefits. Positively, Pemex has adequate liquidity of USD8.5 billion as of March 31, 2015. The company has committed revolving credit lines for USD4.5 billion and MXN23.5 billion; as of March 31, 2015, USD1.55 billion and MXN3.5 billion were available.

### Rating Sensitivities

**Rating Triggers:** An upgrade of Pemex could result from an upgrade of the sovereign coupled with a continued strong operating and financial performance and/or a material reduction in Pemex's tax burden. A negative rating action could be triggered by a downgrade of the sovereign's rating, the perception of a lower degree of linkage between Pemex and the sovereign, and/or a substantial deterioration in Pemex's credit metrics.

## Pemex and Energy Reform

### Linkage to Sovereign to Continue

Fitch does not expect Pemex's ratings to change as a result of the energy reform. The company will continue to be challenged by the heavy cash transfers to the central government in the short to medium term, as the reform seeks to maintain the federal government's reliance on inflows from oil and gas at historical levels. The reform calls to maintain federal revenues coming from oil and gas at 4.7% of GDP, in line with those observed during 2013. The two main benefits of the reform for Pemex are that the company is now able to find partners with whom to share risks and it gives Pemex greater budgetary independence, which benefits the company's planning and investing flexibility.

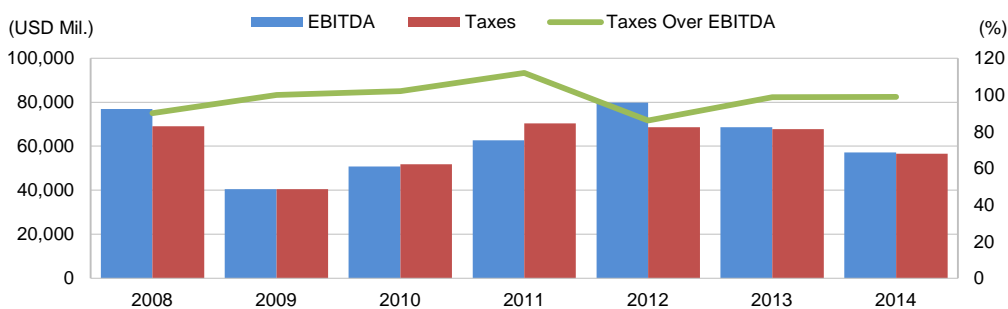
### Reform to Lower Pemex Business Risk

The reform allowed Pemex to partner with international oil and gas companies to share risk and benefit from their technologies and expertise. Business risk could be potentially lowered and return on invested capital increased by diversifying its asset base. The reform changed how the company had been operating for the past few decades given that, since approximately 1938, the company has been the entity solely responsible for developing the country's oil and gas industry.

### Pemex Tax Burden Continues in the Medium Term

Pemex's total transfers to the central government could potentially fall in the medium to long term. This could happen to the extent that the energy sector grows and the incremental tax revenues generated by new private sector participants allow the government to lower Pemex total transfers to the central government, while stabilizing federal revenues from the oil and gas sector. Nevertheless, this will very likely be progressive and slow. Pemex is the single-largest source of funds for the federal government. During the past five years, Pemex's share of oil revenue of the total public sector revenue has remained relatively high, ranging between 30%–40%. As a result, Pemex's balance sheet is weak, which was illustrated by a negative equity.

### EBITDA and Taxes — Pemex



Source: Company filings, Fitch.

#### Related Criteria

[Corporate Rating Methodology — Including Short-Term Ratings and Parent and Subsidiary Linkage \(May 2014\)](#)

[National Scale Ratings Criteria \(October 2013\)](#)

[Evaluating Corporate Governance \(December 2012\)](#)

### Pemex's Production Increases Unlikely

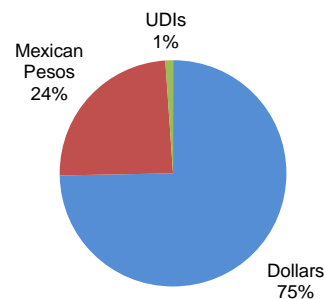
It seems rather unlikely for Pemex to increase production volumes from the current 2.3mmbopd unless its annual cash capex is materially above the average USD16 billion invested during the last four years. The company's investing capacity has been constrained by its limited budgetary flexibility and a high tax burden. Although the reform gives the company budgetary independence, increasing capex will be challenging for the company if the tax burden is not reduced. Pemex's stated goal is to increase crude oil production to 3.0mmbopd in the medium to long term, which requires a higher capex than otherwise historical levels. Over the short term, it seems more likely that Pemex will fund capex with external borrowings rather than internal cash flow generation, given the level of cash transfers to the government.

### Financial Overview

#### Liquidity and Debt Structure

Pemex's liquidity position is supported by its strong pretax cash flow generation ability as well as by its cash on hand and adequate amortization schedule. The company's liquidity position could be pressured by its onerous tax obligations. During LTM March 31, 2015, the company reported an EBITDA of USD45.7 billion and USD8.5 billion of cash on hand. The company also has ample access to the international capital markets, demonstrated by several international domestic debt issuances during the last several years.

**Debt Structure by Currency**  
(As of Dec. 31, 2014)



Source: Pemex.

Pemex's total debt increased to USD84.4 billion in first-quarter 2015, representing a 21% year-over-year increase from USD69.8 billion reported as of first-quarter 2014, primarily due to new financings for capex.

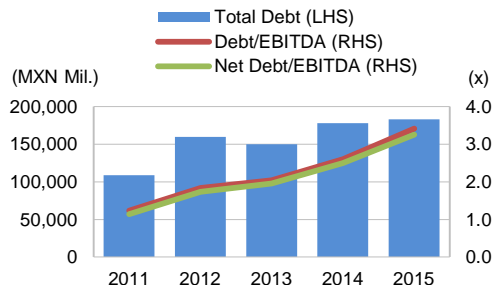
#### Debt Maturities and Liquidity

(MXN Mil., as of Dec. 31, 2014)

2015	145,863
2016	94,093
2017	78,720
2018	87,071
2019 and Beyond	737,502
Cash Flow from Operations	91,409
Cash	117,989
Undrawn Committed Facilities	—

Source: Company reports.

#### Total Debt and Leverage Ratios



Source: Company reports.

### Pension Liabilities Analysis

Pemex’s financial profile continues to be significantly affected by its growing unfunded pension and other post-employment benefits obligations, which as of March 31, 2015 amounted to USD99 billion, or 54% of total adjusted debt. This compares with USD53.5 billion of unfunded pension obligations as of year-end 2010 and highlights the need to reform the company’s dated defined-benefits pension plan. Costs for pension and other employment benefits during LTM March 31, 2015 amounted to approximately USD10 billion, which translates to an adjusted leverage ratio as measured by total adjusted debt to EBITDAP of 1.8x.

The company’s defined-benefits retirement plan dates back to 1942, when the company established the qualifying age for retirement at 55 years and 25 years of tenure with the company. Since then, increase in life expectancy has caused a significant and unexpected rise in retirement obligations. The company has yet to reform its pension plan, even after other government entities, such as Comision Federal de Electricidad and the country’s development banks, modified their pension plans to define contributions with higher retirement thresholds and began funding pension obligations more aggressively.

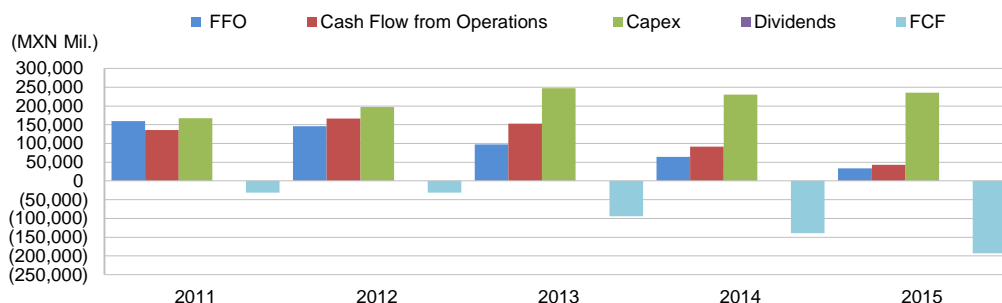
### Cash Flow Analysis

Pemex’s sizable capital-investment program requires the financial flexibility afforded not only by external financing but also by internal cash generation. The company’s historical significant tax burden has limited access to internally generated funds, forcing a growing reliance on external borrowings.

Pemex cash flow metrics are weak due to the company’s high cash transfers to the government in the form of taxes and production duties. Pemex’s FFO-adjusted leverage has averaged approximately 5.8x over the past five years and at LTM March 31, 2015 stood at 12.8x. This high tax and production duties burden has resulted in an average net income of approximately negative USD8.5 billion per year over the past five years and hindered Pemex’s investment ability.

The levels of total transfers to government, coupled with Pemex’s capex, have resulted in negative FCF generation over the past five years. Pemex’s cash capex has averaged approximately USD16 billion over the past four years. The company’s FCF generation will likely moderate, yet remain negative as the energy reform progressively allows the company to retain more internal cash flow, which will likely be allotted for capex.

### Cash Flow Performance



Source: Company reports.

Pemex's total transfers to the central government could potentially fall in the medium to long term. This could happen to the extent the energy sector grows and the incremental tax revenues generated by new private sector participants allow the government to lower Pemex's total transfers to the central government, while maintaining federal revenues from the oil and gas sector stable. Nevertheless, this will very likely be progressive and slow. Pemex is the single-largest source of funds for the federal government.

### Peer Group

Issuer	Country
<b>A</b>	
ConocoPhillips Co.	U.S.
<b>BBB-</b>	
Petrobras	Brazil
<b>CCC</b>	
PDVSA	Venezuela

### Issuer Rating History

Date	LT IDR (FC)	Outlook/ Watch
May 7, 2015	BBB+	Stable
May 9, 2014	BBB+	Stable
May 14, 2013	BBB+	Stable
June 29, 2012	BBB	Stable
July 8, 2011	BBB	Stable
May 4, 2010	BBB	Stable
Jan. 26, 2009	BBB	Stable
Sept. 21, 2007	BBB	RWP
April 2, 2007	BBB-	Positive
April 24, 2006	BBB-	Stable
Dec. 7, 2005	BBB-	Stable
Nov. 24, 2004	BBB-	Stable
Jan. 15, 2002	BBB-	Stable
May 3, 2000	BB+	Positive
April 11, 2000	BB	RWP
March 9, 2000	BB	—

LT IDR – Long-Term Issuer Default Rating. FC – Foreign currency. RWP – Rating Watch Positive. Source: Fitch.

Fitch's expectations are based on the agency's internally produced, conservative rating case forecasts. They do not represent the forecasts of rated issuers individually or in aggregate. Key Fitch forecast assumptions include:

- WTI crude prices average USD50 per barrel (bbl) in 2015, increasing to USD70 per bbl by 2017.
- Continued difficulties increasing production over the next four years.
- Transfers to central government remain high at approximately 100% of pretax income.

### Peer Group Analysis

(USD Mil.)	Conoco Phillips Company	Petroleo Brasileiro S.A. (Petrobras)	Petroleos Mexicanos (Pemex)	Petroleos de Venezuela S.A. (PDVSA)
LTM as of	12/31/14	12/31/14	12/31/14	12/31/14
Long-Term IDR	A	BBB-	BBB+	CCC
Outlook	Rating Outlook Negative	Rating Outlook Negative	Rating Outlook Stable	—

#### Financial Statistics

Revenue	52,524	143,657	1,587,755	105,271
EBITDA	19,167	25,410	898,318	14,989
EBITDA Margin (%)	36	18	57	14
FCF	(3,984)	(18,031)	(139,231)	(11,019)
Total Adjusted Debt	26,357	132,158	2,617,337	45,736
Cash and Cash Equivalents	4,512	25,978	117,989	7,911
Funds Flow from Operations	16,232	23,785	63,898	24,957
Capex	(17,085)	(34,750)	(230,640)	(24,634)

#### EBITDA/Gross Interest Coverage

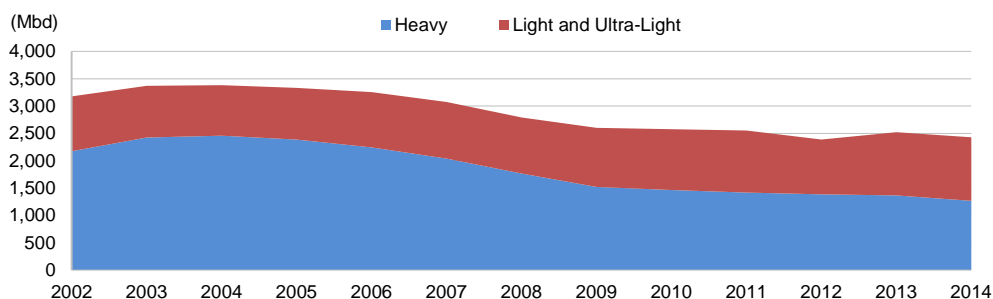
EBITDA/Gross Interest Coverage	11.9	5.8	4.7	3.7
Adjusted Debt/EBITDAR	1.4	5.2	2.9	3.1

IDR – Issuer Default Rating. Source: Fitch.

### Company Profile

Pemex is Mexico's largest oil and gas company and ranks among the world's largest vertically integrated petroleum enterprises. Since the company began operating in 1938, Pemex has had the exclusive right to exploit the hydrocarbon resources of the country with limited private sector participation. As of December 2014, it reported total crude oil production of 2.4mmbopd and a refining capacity of 1.69mmbopd. The company reported hydrocarbon proved reserves of 12.4 billion barrels of oil equivalent as of Jan. 1, 2015. Pemex's proved reserves life was 9.6 years and its reserve replacement rate has been decreasing over the past two years to 67.4% in 2014, from a four-year average of 85% between 2011 and 2014.

### Pemex Crude Production by Type



Mbd – Million barrels per day. Source: Company reports.





**Financial Summary — Petroleos Mexicanos (Pemex)**

(USD Mil., Year Ending December 31)

	LTM 3/31/15	2014	2013	2012	2011
<b>Profitability</b>					
EBITDA	45,731	57,198	68,621	79,535	79,989
EBITDAR	53,614	67,553	73,535	86,881	88,254
EBITDA Margin (%)	43.0	47.9	54.5	63.5	63.9
EBITDAR Margin (%)	50.4	56.6	58.4	69.4	70.5
FFO Return on Adjusted Capital (%)	10.2	13.5	10.7	16.2	22.4
FCF Margin (%)	(13.2)	(8.8)	(5.8)	(1.9)	(2.0)
Return on Average Equity (%)	65.6	59.7	76.1	(1.1)	74.3
<b>Coverage (x)</b>					
FFO Interest Coverage	1.6	2.2	2.4	2.7	3.0
EBITDA/Gross Interest Expense	11.7	14.8	16.2	14.3	15.7
EBITDAR/Interest Expense + Rents	4.5	4.7	8.0	6.7	6.6
EBITDA/Debt Service Coverage	3.0	4.1	6.2	5.6	6.1
EBITDAR/Debt Service Coverage	2.3	2.8	4.6	4.0	4.1
FFO Fixed-Charge Coverage	1.2	1.3	1.6	1.7	1.8
FCF Debt Service Coverage	(0.7)	(0.5)	(0.3)	0.2	0.2
(FCF + Cash and Marketable Securities)/Debt Service Coverage	(0.1)	0.1	0.3	0.9	0.8
Cash Flow from Operations/Capex	0.2	0.4	0.6	0.8	0.8
<b>Leverage (x)</b>					
FFO-Adjusted Leverage	12.8	9.5	10.1	7.2	4.6
Total Debt with Equity Credit/EBITDA	1.8	1.4	0.9	0.8	0.7
Total Net Debt with Equity Credit/EBITDA	1.7	1.2	0.8	0.6	0.6
Total Adjusted Debt/EBITDAR	3.4	2.6	2.0	1.8	1.2
Total Adjusted Net Debt/EBITDAR	3.3	2.5	2.0	1.7	1.1
Implied Cost of Funds (%)	5.1	5.5	6.8	9.5	9.2
Secured Debt/Total Debt	—	—	—	—	—
Short-Term Debt/Total Debt	0.1	0.1	0.1	0.1	0.1
<b>Balance Sheet</b>					
Total Assets	141,413	144,267	156,085	155,585	110,077
Cash and Marketable Securities	8,487	8,017	6,175	9,165	8,254
Short-Term Debt	11,508	9,910	6,921	8,781	7,932
Long-Term Debt	72,931	67,766	57,411	51,700	48,262
Total Debt	84,439	77,676	64,332	60,481	56,194
Equity Credit	—	—	—	—	—
Total Debt with Equity Credit	84,439	77,676	64,332	60,481	56,194
Off-Balance Sheet Debt	98,619	100,156	85,589	99,042	52,479
Total Adjusted Debt with Equity Credit	183,058	177,832	149,921	159,523	108,673
Total Equity	(56,247)	(52,283)	(14,172)	(20,835)	(13,921)
Total Adjusted Capital	126,811	125,549	135,749	138,688	94,752
<b>Cash Flow</b>					
Funds from Operations	2,455	4,805	7,657	11,134	12,842
Change in Working Capital	651	2,069	4,343	1,546	(1,919)
Cash Flow from Operations	3,107	6,874	12,000	12,680	10,923
Total Non-Operating/Nonrecurring Cash Flow	—	—	—	—	—
Capex	(17,171)	(17,344)	(19,351)	(15,020)	(13,425)
Common Dividends	—	—	—	—	—
FCF	(14,065)	(10,470)	(7,352)	(2,340)	(2,502)
Net Acquisitions and Divestitures	—	—	—	—	(1,671)
Other Investments, Net	569	577	225	(139)	(332)
Net Debt Proceeds	19,166	16,239	3,588	2,740	3,020
Net Equity Proceeds	(3,163)	(3,879)	124	—	—
Other (Investments and Financings)	418	334	—	—	—
Total Change in Cash	2,925	2,801	(3,415)	261	(1,484)
<b>Income Statement</b>					
Revenue	106,461	119,398	125,961	125,241	125,271
Revenue Growth (%)	(10.8)	(5.2)	0.6	(0.0)	23.4
EBIT	36,474	43,594	51,936	52,952	54,032
Gross Interest Expense	3,910	3,877	4,235	5,548	5,083
Rental Expense	7,883	10,354	4,913	7,346	8,266
Net Income	(23,942)	(19,839)	(13,320)	198	(8,596)

Source: Company report.

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

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