

Mexico

Holding its Own in 2005

Since our last report on Mexico in the August 2004 issue of *Area Development*, the Mexican economy has experienced mixed economic results. A broad look at the trends impacting the Mexican economy suggests that throughout North America companies are continuing to make significant investment in Asia in search of more competitive labor costs, as well as investing in economies that have huge market growth potential.

This last point cannot be overstated, as India and China alone represent nearly one third of the world's population. Not only do these two countries represent a huge labor pool from which manufacturing can draw, but they also represent a domestic consumer market that rivals Western Europe and North America. The Asian market is sapping growth not only from Mexico, the United States, and Canada, but is also partially responsible for the depressed economic conditions that are being experienced in Western Europe. In recent years, Mexico has not been immune to the economic pressures that have forced U.S., Canadian, and Western European manufacturing companies to consider locations in Asia. More than ever, Mexico's economy is tied directly to the success of the U.S. economy.

While the offering of incentives to attract and retain business has evolved into a very sophisticated art form within the United States, Mexico lags behind in this respect and will have to catch up in order to compete with the United States for new business. Currently, however, Mexico holds a labor-cost advantage and can rely on this to attract new business and compete with the United States. In time this economic advantage may abate, but for the present, Mexico can offer this unique business advantage to North American

manufacturers, particularly those manufacturers whose core market is North America.

The Economy 2004–2005

Mexico's free market economy has entered the elite trillion-dollar class. It contains a mixture of modern and outdated industry and agriculture, increasingly dominated by the private sector. To make an educated assessment of the state of Mexico's economy, it is necessary to compare it to the world's economy, more specifically to those countries that have recently become notorious for attracting foreign investments (i.e., China and India). It is also interesting to include in the comparison the other NAFTA members: the United States and Canada.

The latest published World Bank and CIA statistics list Mexico's GDP as 14th (\$1.006 trillion) in the world economy rankings. Mexico is the last of 14 countries that fall within the trillion-dollar benchmark. Mexico's economy, however, pales in comparison with India's (which ranks sixth at \$3.319 trillion), China's (which ranks fourth at \$7.262 trillion), and the United States' (which ranks first at \$11.75 trillion). Canada's economy ranks 13th at \$1.023 trillion.

As stated, the Mexican economy is heavily dependent on the U.S. economy. Data reveals that 87.6 percent of Mexico's exports go to the United States, and 61.8 percent of Mexico's imports come from the United States. Given such information, it's no surprise that Mexico's GDP growth on an annual basis (adjusted for inflation) is almost identical to that of the United States. Mexico's GDP real growth rate is 4.1 percent (104th), as compared with the U.S.'s GDP real growth rate of 4.4 percent (101st). Canada only ranks 158th

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Despite the lure of Asia, U.S. firms are continuing to consider **Mexico** in their international location decisions because of its low labor costs and geographic proximity.

Greater McAllen

The Greater McAllen Alliance (GMA) is made up of the leading economic development organizations in the Greater McAllen area and includes the cities of Edinburg, McAllen, Mission, Pharr, and Weslaco. The GMA is an alliance of professionals committed to helping companies explore the opportunities available on the Texas/Mexico border.

at 2.4 percent, but India at 6.2 percent (43rd) and China at 9.1 percent (17th) are experiencing much faster growth rates.

While comparing the GDP real growth rate relative to the annual percentage increase in industrial production of each country, we can conclude that China's and India's individual industrial growth rates are almost double their GDPs. In Mexico,

Canada, and the United States, the industrial growth rates are lower than their respective GDP growth rates. Such statistics support the popular opinion of economic analysts that countries like India and China have the growth and potential to become the industrial production leaders of the future. Its annual industrial growth rate ranks China sixth at 17.1 percent; India, 45th at 7.4 percent; the United States, 86th at 4.4 percent; Mexico, 101st at 3.8 percent; and Canada, 132nd at 2 percent.

Investment and Jobs

Since January of 2004, investment in Mexico has remained fairly stable with regard to net new plants and new jobs, increasing to 2,811 plants from 2,805 a year ago, and 1.144 million workers from 1.061 million workers over the course of the year. If you consider only the border states of Mexico, then the statistics present a more optimistic assessment of the Mexican economy, with a gain of 24 new plants among six states. However, even these modest successes would hardly be considered robust by U.S. standards. Considering the average Mexican direct labor wage (fully loaded) is only between \$1.60 and \$1.90 per hour, approximately a 5.5 percent increase since January of 2004, a company must wonder why Mexico's growth slowed to but a trickle.

Could there be more economic dynamics at play that would give a manufacturer pause to seriously consider if a Mexico location is the best decision? Some of our clients believe this is a case of Mexico being overshadowed by China hype and being plainly underrated. Although our experience shows that for U.S. and European companies language and cultural barriers often create difficulty initially, our clients generally find that the Mexican work force is very eager to work hard and get the job done.



A Look at the Border States

Baja California: From 2004 to 2005 the state of Baja has experienced the best growth with the addition of 27 new plants and 20,392 new jobs. This represents a 3 percent increase in new plants and an 8.6 percent increase in jobs created. The state includes the metropolitan areas of Mexicali, Tijuana, and Tecate.

Chihuahua: From 2004 to 2005 the state of Chihuahua experienced overall growth with the addition of 15 new plants and 9,305 new jobs in two major metropolitan centers. This represents a 4.2 percent increase in new plants and a 3.8 percent increase in new jobs from a year ago. The state includes the metropolitan centers of Juarez and Chihuahua.

Coahuila, Nuevo Leon, and Sonora: Over the past year, the state of Coahuila, which includes the metropolitan areas of Acuna, Piedras Negras, and Torreón, had a flat growth rate. The state of Nuevo Leon, which includes the metropolitan areas of Guadalupe and Monterrey, and the state of Sonora, which includes the metropolitan cities of Agua Prieta and Nogales, also experienced flat growth trends from 2004 to 2005.

Tamaulipas: From 2004 to 2005 the state of Tamaulipas has been unique in that it has reported a significant growth in employment but a decrease in new plants. The state includes the cities of Reynosa, Matamoros, and Nuevo Laredo. These cities combined have grown their employment by 13,919 new jobs, which is a gain of 9.6 percent in the work force, yet have experienced a net loss of plants. Depending on how each state tracks new plants, this could just represent a lag in the data (e.g., tax bills etc.).

While a few states along the border have experienced measurable success in their business growth trends, the interior of Mexico has experienced losses over the past year. In spite of the significant labor cost advantage as compared to the United States, no state within Mexico is experiencing double-digit growth rates. Given the advantages of labor and the close proximity to the U.S. market, perhaps manufacturers servicing the U.S. market should give these regions of Mexico a closer look.

Advantages of Locating in Mexico

North American investment in Mexico (as opposed to Asia) has advantages for all types of businesses. For example, businesses that want to manufacture a product outside the United States — and then import that product back into the states — would benefit from a site in Mexico because of its geographic proximity. Also, should

production problems occur at a site in Mexico, U.S. experts could potentially reach the site in order to deal with the problems in one day or even several hours. Such a quick turnaround would not be possible with operations in Asia and would result in a loss of production days versus just hours.

Another significant advantage of siting a facility in Mexico instead of Asia is shipping time and flexibility. Products can be

shipped via truck or rail from virtually anywhere in Mexico to any U.S. location within days versus weeks from Asia.

Although cultural and language differences within Mexico can be and sometimes are an obstacle with initial business transactions, they are far less formidable than those encountered in Asia. The Latin-American community is quickly becoming the largest minority population in the United States. Its culture and language is at least familiar to many Americans. Asian business culture, on the other hand, can be much more difficult for a westerner to understand.

The federal government of Mexico has a very good and comprehensive job-training assistance program that helps companies financially during an approved training regimen program. The remainder of incentives must be negotiated both at the federal level and the state and municipal levels. These negotiated incentives can be as creative as incentives that are found in the United States. However, as in the states, some Mexican states are easier to deal with and are more professional than others.

Additionally, recent Mexican administrations have expanded competition in seaports, railroads, telecommunications, electricity generation, natural gas distribution, and airports ("Review of the economic situation in Mexico," *Economic and Social Research*, March 2005, Vol. LXXXI, Banamex and Citigroup Global Markets); and trade with the United States and Canada has tripled since the implementation of NAFTA in 1994. Mexico has 12 free-trade agreements with more than 40 countries including Guatemala, Honduras, El Salvador, the European Free Trade Area, and Japan, putting more than 90 percent of its trade under free-trade agreements.

The government is cognizant of the need to upgrade infrastructure, modernize the tax system and labor laws, and provide incentives to invest in the energy sector — however slow the progress may be. Such actions send a signal to the world that Mexico recognizes a need for improvements, but it is still an attractive choice for U.S. businesses.


The global marketplace has forced competitive firms to consider manufactur-

ing operations close to growth centers worldwide. Companies considering alternative manufacturing locations in order to remain competitive in the North American market are giving serious consideration to Mexico. It offers a labor cost approximately one eighth that of the United States, a work force that is hard-working and well-motivated, and the

advantage of close proximity to the market being served.

Statistical data sourced from the CIA's World Factbook, Mexico, May 17, 2005; and Instituto Nacional de Estadística Geografía e Informática (INEGI) 2005.

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Third Coast Faster, cheaper, easier

MCALLEN REYNOSA


The unique location of the Greater McAllen Alliance corridor positions it as one of the most competitive shipping ports to and from Asia, Europe and South America. Considered by many companies as the third coast, this corridor is the cost-effective post 9/11 shipping alternative. Globally produced goods can be consolidated in one location to serve all North American markets.

- World events over the last few years have changed the reliability of our traditional logistic systems. Today, smart companies are looking at alternatives. Shippers have started using the Mexican ports of Manzanillo and Altamira to save time and money. Shipments arriving at these ports are moved by truck or rail to a new dry port in Reynosa, Mexico or distribution warehouses, in the greater McAllen area. From here they are shipped to points across North America. This route can save the shipper 20-25% in transportation costs and an average of three days of shipping time.

With the increase emphasis on logistics cost and speed to market, it is easy to see the the benefits of being able to ship all global production to customers from a single North American location, virtually eliminating the need for restaging or partial shipments to meet customer demands.

Shipping through this new corridor is faster, cheaper and easier. Just another instance of bridging the Americas (and now the world) for international trade.

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