What to Look for When Considering Mexico

Doug Donahue, Vice President, Entrada Group

This article originally appeared in the April 2014 print edition [1] of IMPO. The full article including a sidebar on the differences between contracting manufacturing, standalone, and shelter models can be found there.

Recently one of our long-term clients finalized with us a contract extension to expand the footprint of their manufacturing operation in central Mexico. It was their third such expansion, tripling their initial space since they started with us six years ago.

The company, a midsized U.S.-based auto supplier, now occupies more than 70,000 sq ft in Zacatecas, Mexico with my firm, Entrada Group, a U.S.-based company that helps manufacturers set up operations swiftly and cost-effectively in Mexico.

Typically, when a client extends their contract, we send a press release and help them spread the good news. But this client keeps a very low profile. Any publicity would be a non-starter. To paraphrase his message to us: We trust you because you are honest and good partners. At the same time, we are not necessarily eager to tell everybody about how great things are going for us in central Mexico. We prefer to keep that to ourselves.

Such sentiment is shared by many foreign manufacturers already operating in central Mexico – they don’t want to let the cat out of the bag about the benefits found in the region, known as the Bajio. For companies whose processes are labor-intensive, cost reduction is often paramount, and the Bajio delivers. In central states like Zacatecas, Guanajuato, or San Luis Potosi, total operating costs (direct labor, benefits, utilities, HVAC, etc.) for well-managed operations can be as low as $4.50 to $7.00 per hour.

Opportunity Abounds

At the same time, other companies value location over low operating costs. Some manufacturers must be close to the customers they are supplying. For example, U.S.-based Johnson Controls recently went online with their new plant in Querétaro, where they will produce molded polyurethane foam for automotive seats. The facility is strategically located less than two hours by truck from plants of three OEMs: GM, Mazda, and Honda. To be in position to serve those key customers, however, Johnson Controls is willing to pay a big premium in Querétaro, where real estate is pricier and labor is more expensive and competitive.

Approaches and locations for companies in Mexico differ, but a common theme unites them: Growth prospects. Mexico's status as arguably the most open trading partner in the world – 44 free trade pacts globally – means that companies with a physical presence in the country can take advantage of low- or zero-tariff export to markets in not just North America and South America, but even Europe and Asia. That's a key reason Mexico is the best hub for manufacturing in the entire Western hemisphere.

The challenge is that most small and midsize foreign manufacturers lack the know-how and connections, not to mention the resources, to set up and operate in Mexico and fully leverage opportunities and realize savings. Most big multinationals go it on their own (see "Contract Manufacturing vs. Standalone vs. Shelter"), managing all aspects of setup and ongoing operations internally. But such an approach is cost-prohibitive for smaller companies.

Success in Mexico – According to Our Clients

Having spent more than a dozen years working closely with our clients on their Mexico strategy, we have learned a lot about what small and midsize manufacturers need to do to succeed. Here are four key things they have shared with us over the years.

Choose the right area
The regions near the U.S. border have been well established for U.S. and Canadian manufacturers for decades. They are close and convenient – but proximity comes at a cost. Compared to the center of Mexico, operating costs near border regions can be as much as 40 percent more, due to greater costs for labor and utilities (higher elevation in central Mexico minimizes HVAC costs).

Work with an experienced partner
Manufacturing in a foreign country has its own set of rules. Seek an expert that knows Mexico well and can minimize risks in realms such as import/export, as an example. A seasoned provider will be able to offer highly experienced specialists who handle all the details of your cross-border functions. They will know the ins and outs of aspects such as C-TPAT and Mexican Customs certifications, enabling products to move into the "fast lane" at the U.S. border. It takes years and fanatical attention to details and customs brokerage to earn these certifications.

Outsource the General & Administrative Services

Stay focused on your core function of producing high-quality goods, and hand off non-production-related aspects to a knowledgeable operator. Including things like: HR, compliance with ever-changing Mexican employment laws, unions, payroll and taxes, environmental health and safety, maintenance, security, accounting, customs permits, logistics and warehousing. The list seems endless.

Consider your ramping up period
This is another area where the experience of an expert is invaluable. We commit to having our clients up and running in as little as 90 days; so it pays to choose the right partner.

You will never be able to cover all of your bases prior to setting up in Mexico for the first time, and you're certain to make missteps along the way. But by choosing a service provider with deep knowledge of the country, you'll be on your way to a successful Mexican manufacturing operation.

Links:
[1] http://www.impomag.com/digital-editions/2014/04/april-2014-real-time-visibility