INVESTING IN MEXICO PRODUCTION

PLASTICS NEWS EXECUTIVE FORUM

Doug Donahue
Principal & VP of Development
Entrada Group

Entrada Group
Mexico, Delivered

March 5-7 2018

Source: TheRecord.com
Editorial cartoon by Graeme MacKay

Agenda

Changes in Mexico

- Elections
- New Tax Laws

NAFTA Changes

- Other Free Trade Agreements

Peso Devaluation Issues

Availability of Labor

Client Experiences

Changes in Mexico

Changes in Mexico: Elections

Mexico Presidential Elections July 1, 2018			
Candidate	Ricardo Anaya Cortés *Presumptive nominee*	Andrés Manuel López Obrador *Presumptive nominee*	José Antonio Meade Kuribreña *Presumptive nominee*
Party	PAN	MORENA	PRI
Home State	Querétaro	Tabasco	Mexico City

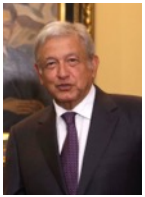
- 6-year term
- PRI is currently in power (Nieto)
- Front runner: MORENA (40%); PAN (31%); PRI (20%)

LA JEUNESSE, FEB. 19, 2018

Changes in Mexico: Elections

Ricardo Anaya Cortes (PAN)

- Supportive of NAFTA
- Economically conservative; free market advocate; internationalist



Andres Manuel Lopez Obrador (MORENA)

- Redirect federal spending to infrastructure and priority social programs
- NAFTA benefits auto and electronics industries but leaves small- and medium-size businesses out of supply chains

Jose Antonio Meade Kuribrena (PRI)

- Foreign policy should work toward the creation of new economic opportunities
- Seeks market growth where Mexico has limited exchange
- Not a true politician; worked under PAN and PRI administrations

Changes in Mexico: New Tax Laws

International manufacturers operating under a shelter provider

- **Before**: Could produce without a permanent establishment, tax-free

- **Now**: Tax-free for first 4 years
  - Can operate for another 4 years without a permanent establishment
  - Must pay a tax through shelter operator; based on value-add in Mexico

Key: **Taxes paid in Mexico are deductible against US tax bill**

NAFTA Changes

NAFTA Changes

- Mexico openness and adaptiveness will outlast the US administration
- Mexico is already competitive. Have been anticipating NAFTA changes
- Since 1985, Mexico has competitively industrialized and implemented structural adjustments in order to embrace the open economy

Working Groups Have Modernized NAFTA

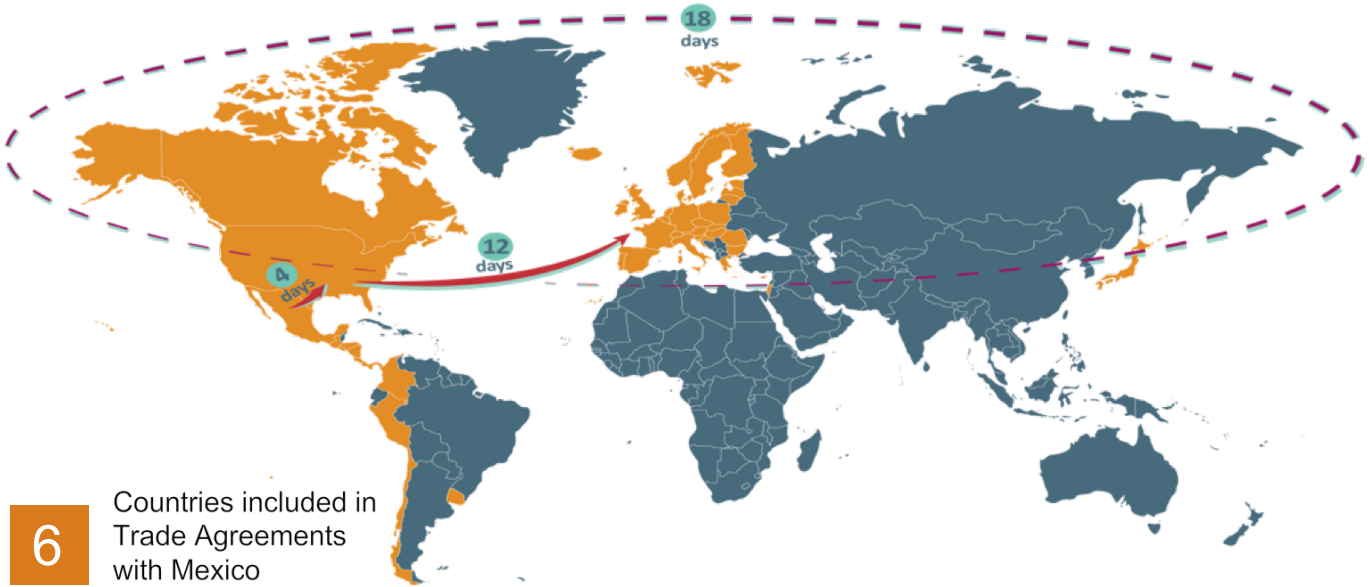
- Have kept the agreement current over the past 20+ years. Agreed-to and ready to go
- Outstanding political issues, mostly related to the auto sector and the US administration, are creating the holdup

NAFTA Impact

"One of the great ironies of the NAFTA renegotiation is that if it fails — which is to say, if the United States withdraws from the trade agreement — the people who will hurt the most are among some of the president's biggest supporters."

The Hill editorial, January 2018

Mexico's Other Trade Agreements



6 Countries included in Trade Agreements with Mexico

Mexico's Trade Bona Fides

Top exports (2016)

- **CARS** $31.4B
- VEHICLE PARTS $26.2B
- AGRICULTURE $23.8B
- DELIVERY TRUCKS $23.4B
- COMPUTERS $21.2B
- OPTICAL & MEDICAL INSTRUMENTS $13B

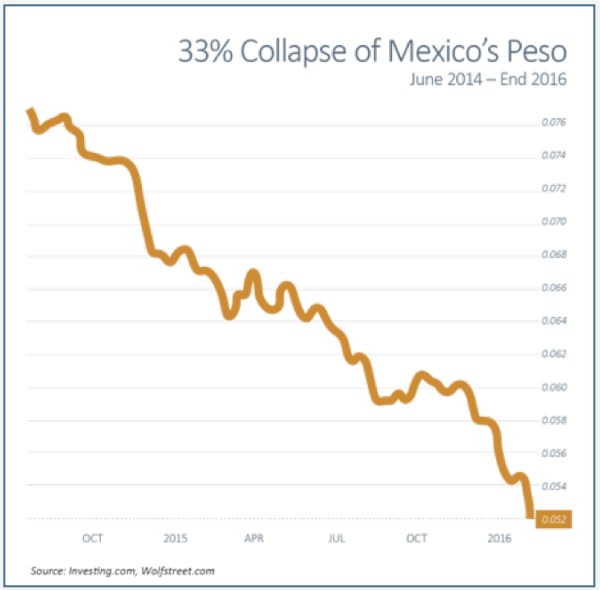
13th largest export economy

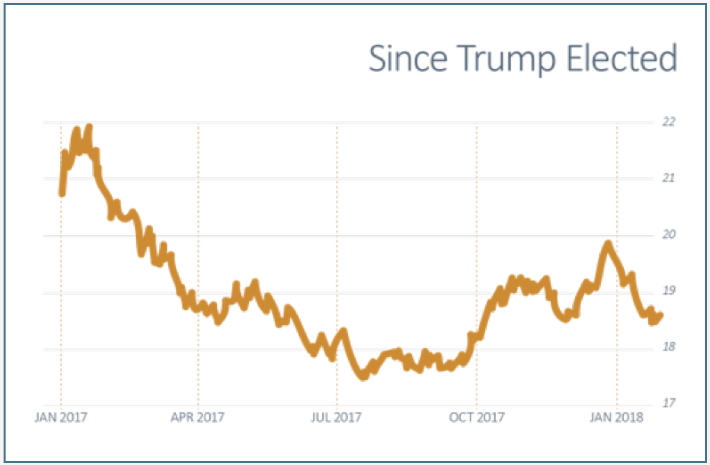
In 2016, Mexico exported $373B and imported $380B

Sources: MIT think tank 2016, OEC; export.gov

Peso Devaluation

What A Difference A Year Makes





Peso Devaluation: Impact

Year	Mexican Peso to the US Dollar (annual average exchange rate)	Entry Level		6 Months	
		Cost / Hr	Cost / Hr in USD	Cost / Hr	Cost / Hr in USD
2018	Mex$18.93	Mex$40.62	US$2.15	MEX$43.66	US$2.31
2017	Mex$18.93	Mex$32.11	US$1.70	MEX$35.80	US$1.89
2016	Mex$20.00	Mex$15.06	US$1.39	MEX$16.70	US$1.54
2015	Mex$16.57	Mex$12.58	US$1.40	MEX$14.13	US$1.58
2014	Mex$13.29	Mex$11.41	US$1.59	MEX$12.96	US$1.80
2013	Mex$12.49	Mex$10.97	US$1.62	MEX$12.58	US$1.86
2010	Mex$12.21	Mex$9.26	US$1.40	MEX$11.41	US$1.73

Availability of Labor

Availability of Labor

- Competition for employees — both finding and retaining — is nudging labor costs upward
- Auto OEM need for talent is driving up the market
- Creative retention and retraining programs are becoming the norm as are employee bonuses (especially for highly skilled)

Labor is Maturing

- Processes in Mexico are becoming more sophisticated
- Shift in emphasis/focus
  - From: Assembly, production, processing
  - To: Value-add, integrated services, engineering
- Win-win
  - Workers want to learn more advanced processes/techniques
  - Companies want to do as much locally as they can

Regional Affects

- Labor rates within Mexico vary tremendously
  - Border states may be as much as a 40% premium over interior states
- Where is competition greatest?
  - Near-border states: Baja, Nuevo Leon, Chihuahua, Coahuila
  - Bajio: San Luis Potosi, Querétaro, Guanajuato, Aguascalientes
- Talented & skilled workers can be recruited to less-expensive cities
  - Key: Sell it to the whole family

Our Clients' Experiences

A Client New to Mexico

- China-based Bluestar Technology: part of Hong Kong Stock Exchange-listed BSM Group
- Key Asian tooling, injection mold and parts provider
- Provider to: automotive, medical, industrial sectors; OEMs and Tier Ones
- Duration in Mexico: A few months
- Mexico operations: Fresnillo, Zacatecas

Why Mexico?

- Customer proximity is key in plastics processing
  - Shoot and Ship
  - Inventory
  - JIT delivery
  - Transport
  - …Mexico is a huge advantage for all

- Needed to ship internally within Mexico
- Heavy customer demand beyond moldmaking
- Responsive teams
- Expects to be at full capacity within 16 months

Tips for Success in Mexico

- Diversify
  - Assembly and processing alone aren't enough, as Mexico market is maturing and processes are becoming more sophisticated
- Leverage customer demand
  - Engineering, mold-making, maintenance, repair
  - Bluestar will offer machine shop in Mexico
  - In future will manufacture molds locally
  - "We will make more in mold repair than in injection molding"
- Must be vertically integrated
- Offer additional services

Thank You

Doug Donahue
Principal & VP of Development
Entrada Group
Tel: +1 210 828 8300
ddonahue@entradagroup.com

Entrada Group
Mexico, Delivered

Plastics News Executive Forum
March 5-7 2018