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Mexican Automobile Industry Experiencing Strong Growth

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While the overall Mexican economy has stagnated, in part because of a slump in global oil prices (SourceMex, Feb. 4, 2015), the automobile sector is showing signs of unprecedented growth levels that have vaulted Mexico to seventh place among the world's automobile manufacturers as of the end of 2014. With auto sales slowing down in India and South Korea, Mexico has the chance of surpassing the two competitors in the next five years, industry sources said.

Mexico has also become a global leader in auto-parts production, ranking fifth among all producing nations. Mexican plants produce about 33% of the auto parts sold in the US market, said the Secretaría de Economía (SE).

The rapid growth rate of the Mexican automobile industry was reflected in the statistics for 2014. The Asociación Mexicana de la Industria Automotriz (AMIA) said that auto-assembly plants in Mexico produced more than 3.2 million vehicles last year, almost 10% above the output recorded in 2013. Spain, with an increase of 11%, was the only country to surpass Mexico in the growth of its auto production last year. Mexico accounted for 3.7% of the global production of cars and light trucks last year, said AMIA.

More than 80% of the motor vehicles produced at the Mexican plants last year were exported, primarily to the US and Canadian markets. Four out of every five vehicles of Mexico's total exports of 2.6 million last year were shipped north of the border, said AMIA.

With new plants coming online and existing factories expanding production, AMIA projects that Mexico is on pace to manufacture as many as 3.5 million cars and light trucks this year and possibly as many as 5 million units by the end of the decade.

Guanajuato state attracts new investments

The growth in the Mexican auto industry is driven by a huge increase in investment. In the past four years, foreign automobile companies have spent about US$12 billion in new operations in Mexico. Companies from Asia, Europe, and the US have recently established new operations or expanded existing automobile and auto-parts plants in Mexico, including Mazda, Honda, Toyota, Kia Motors, Volkswagen, Audi, Nissan-Daimler, BMW, Ford, and General Motors.

Furthermore, foreign investment in the sector is projected to increase a further 70% in the next six years, which could move Mexico further up the ladder in manufacture and exports of automobiles by 2020. "This is a clear sign of Mexico's potential in the auto sector," said AMIA president Eduardo Solís, who projected exports could increase to 4 million units by the end of the decade from the 2.64 million units sold in 2014. Exports in 2014 rose by 9% from 2013.

"Our exports are already close to those of South Korea, which is the third-largest exporter in the world," added Solís. "We are currently the fourth-largest exporter, and the largest in Latin America."

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Some auto manufacturers have moved their operations to Mexico from the US and Canada, and a preferred destination appears to be the region known as El Bajío in central Mexico, including the states of Guanajuato, Querétaro, Aguascalientes, and Jalisco. Most recent investment, however, has gone to Guanajuato. Earlier this year, Toyota announced plans to move assembly of its popular Corolla model from Cambridge, Ontario, in Canada to a new plant in Celaya. Honda also opened a plant in Celaya last year, manufacturing the Fit subcompact and HR-V crossover.

In mid-April, Ford announced plans to construct a transmission plant in Irapuato, also in Guanajuato state, adjacent to the existing facilities of its German partner Getrag. The US automaker is also planning to construct a new engine facility within its engine plant in the northern state of Chihuahua.

The trend includes some of the smaller parts manufacturers that have become a source of automobile components for the big automakers. At present, Michigan-based parts giant Delphi is one of Mexico's largest private employers, with more than 50 plants and 50,000 employees.

Low labor costs benefit Mexico

Low labor costs and the absence of tariffs are the major incentives for foreign manufacturers to move to Mexico. A worker at an auto plant in Mexico receives the equivalent of US$8 an hour, including wages and benefits. In contrast, autoworkers employed by General Motors in the US receive US$58 an hour. The lowest US hourly wage is US$38 per hour at the Volkswagen's factory in Tennessee, according to the Center for Automotive Research, an industry research group in Ann Arbor, Michigan.

"Mexican auto factories and Mexican manufacturing offer First World productivity and quality at Third World wages," Harley Shaiken, an expert at the University of California at Berkeley who has tracked Mexico's auto industry for decades, said in an interview with The Washington Post. "That is an unusual combination, and right now it is a defining combination."

The transfer of plants to Mexico has been an issue for US unions since at least the 1980s (SourceMex, March 6, 1991, and June 5, 1991), but the migration was made easier by clauses in the North American Free Trade Agreement (NAFTA) in 1994. One of the biggest impacts of NAFTA, however, has been to boost investments by auto manufacturers from Asian and European countries in Mexico to manufacture vehicles for exports to the US market (SourceMex, March 23, 1994, Sept. 27, 2006, and Aug. 15, 2007).

The migration of plants and the decision of automakers to start new operations in Mexico instead of the US has a direct impact on the United Auto Workers (UAW) union and many of its 1 million active and retired members. The shift means that new jobs that could have provided a source of employment in the US instead went to Mexico.

The number of jobs in the auto sector in Mexico has increased by 38% since 2008 to reach 675,000 in 2014, according to government and industry statistics. During the same period, employment in the US auto sector increased by about 15% to slightly more than 900,000 workers. "American manufacturing workers could have had good-paying jobs that respect basic human dignity," UAW President Dennis Williams said.

The small increase in the number of workers employed in the US auto industry means that a share of the investments of the global auto industry in North America are also targeted at the US.

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According to US government statistics, the auto industry invested about US$46 billion to improving and expanding US factories between 2010 and 2014, and employment in auto plants increased by 37% during the same period.

Strong US dollar a contributing factor

Some experts point out that a strong US dollar has added incentives for auto manufacturers to invest in Mexico rather than the US. "The decline in the value of the peso versus the dollar has become an advantage for the assembly plants in Mexico," said the daily business newspaper El Financiero. "The reason is because the value of their exports has increased while the cost of operation is still valued in pesos."

The Banco de México (central bank) says the value of exports by the Mexican auto industry increased by 11% last year relative to 2013.

Automobile manufacturers also increased exports from US plants despite a strong dollar. The US International Trade Administration said US auto exports amounted to a total of 2.1 million vehicles, worth about US$57.5 billion, in 2014. However, there is concern that a strong dollar could become an obstacle. "The US dollar will rain on our exports," said Sean McAlinden, chief economist for the Center for Automotive Research in Ann Arbor, Michigan.

Mexico reaches new quota agreements with Brazil, Argentina

Mexico’s improved standing among automobile manufacturers in Latin America has come at the expense of Brazil. In 2014, Mexico surpassed Brazil as the seventh-largest automobile producer, with the South American country suffering a second-consecutive year of production declines. Mexican production of 3.2 million vehicles compared with the 3.1 million produced in Brazil last year.

The biggest difference between the two countries is that a vast majority of the vehicles produced in Mexico are intended for the export market, while 85% of the Brazilian output is intended for the domestic market. With a slump in domestic sales, the Brazilian government negotiated an agreement with Mexico to continue a quota system negotiated in 2012 to protect the Brazilian auto industry (SourceMex, Feb. 15, 2012, and March 21, 2012).

The agreement, which was to expire in 2015, would have restored free trade in motor vehicles between the two countries. Instead, the two countries negotiated new terms of the quota system. Under the new agreement, Brazil and Mexico will permit US$1.56 billion of duty-free vehicle imports for the first year of the agreement. That amount will rise 3% each year until the agreement expires, in 2019, when the countries return to a free-trade system.

Mexico this year also negotiated a new four-year agreement on automobiles and parts with Argentina, following the expiration of an accord negotiated in 2012 to ease trade tensions between the two countries (SourceMex, July 18, 2012). Argentina is facing a similar situation as Brazil, with its auto production declining about 22% in 2014. The four-year agreement allows for gradual increases in tariff-free trade on an annual basis, going from US$575 million in the first year to eventually reach US$640 million in the fourth year. Trade exceeding the 12-month limits will be limited to 1-to-1 import-export transactions in order to remain tariff free, a source told Reuters.

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