

# Much more than just cheap labor

## Solange Monteiro

EXPANDING ITS INCLUSION in global value chains is also a task for Mexico, which since it signed the North American Free Trade Agreement (NAFTA) in 1994 has recorded a surge in the activity of maquilas—companies that import components to assemble products for export, taking advantage of low labor costs — and now seeks to increase the value it adds to participation in this global supply chain.

“We seek not only a formal change but more efficient coordination between maquiladoras and the national economy, and greater integration of Mexican industry into the production processes,” says Celso Garrido, head of business area finance and innovation, Metropolitan Autonomous University of Azcapotzalco, Mexico City.

Concern over the issue is reflected in the Program of Innovative Development of the government of Enrique Peña Nieto. It expects to increase domestic inputs in the manufacturing sector, the maquilas, and export services from 30% in 2013 to 36% in

2018. For example, the automotive sector has attracted new manufacturers—six in the last four years, among them Audi, Mazda, and Honda—which are taking advantage of Mexico’s auto parts industrial base. In the first half of 2014 Mexico’s car production surpassed Brazil’s.

Another example is the software development hub in Jalisco state, with annual sales of about US\$1.5 billion, supported by a federal program to build up the exports of this industry. Among its beneficiaries are IBM, HP, and Oracle. Perhaps the most prominent business to join in recently is the Canadian company Bombardier, which has announced it is opening a new center for advanced engineering in Querétaro. It will be joining an aerospace cluster that since 2006 has been manufacturing parts, such as wings and fuselage of the Learjet 85, in Querétaro.

Garrido explains that these changes are related to two factors: the evolution of the global value chain itself, now with very competitive companies that can relocate operations globally; and more recently with the growing participation of Asian

companies, particularly South Korean and Chinese. The US Census Bureau has reported, for example, that in 2001 Mexico and China both imported virtually the same amount of manufactured imports



from the United States, about 12%; by 2010, China had more than doubled its US imports to 27.3%, while Mexico was still at 12.4%.

Garrido also emphasizes the importance of diversification. Costa Rica offers a current example of the risks inherent in dependence on just a few companies. In April, Intel Company announced that it was relocating its Costa Rican manufacturing operations to Asia. Intel, which had operated in Costa Rica since 1997, represented 20% of national exports. "In 1998, total exports of integrated circuits and microcomponents was US\$440 million; it had jumped to US\$2.37 billion in 2013, an increase of 439%," says Monica Segnini, president of the Chamber of Exporters of Costa Rica. The country is now trying to attract new foreign investors based on the conditions that attracted Intel Company in the first place, such as legal security, skilled labor, and proximity to key markets. Segnini also points out that "Intel also boosted creation of small national companies in technology and machinery that have become providers to other high-tech companies."

According to the Costa Rican Coalition for Development Initiatives, about 250 multinational companies have operations in the country, mostly dedicated to medical technology, film industry, electrical and electronic components, electromechanics, and services. Exports of electrical and electronics and medical and precision equipment totaled US\$4.8 billion in 2013, 41.62% of total exports. Segnini thinks that "The medical industry is one of the niches with potential to occupy the space left by Intel."

### Global competition

National content of Mexican and Chinese exports by market (%)



Source: US International Trade Commission, April 2011.

In Mexico, more than diversification its productive sectors the big challenge is to lessen dependence on the US market, even though that dominance is to some extent inevitable. In 2009, shortly after the subprime collapse, Mexico's GDP fell by 4.7%—of which 3.3% was related to exports. "Another negative effect we have to consider is that the improved participation in global value chains occurred at the expense of the domestic market and traditional and mature industries with low productivity geared to domestic demand, such as food and textiles," says Garrido. "Today, we have a dual economy: a modern sector globally inserted, but at the same time a domestic economy formed by small and medium enterprises disconnected from this process. This is reflected in the quality of our growth. We have to promote domestic businesses so they, too, reach a high level of competitiveness." ▾