MEXICO: THE NEW CHINA

IBG Presentation 10.14.2014

GROUP 50®

Align + Integrate + Optimize = Execute

What Is Going On?

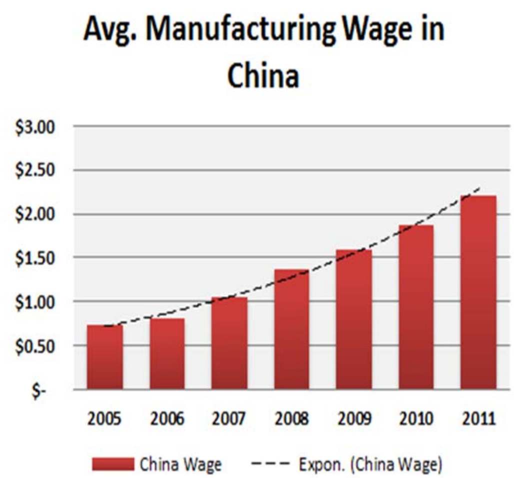
- Forget everything you knew about Mexico 10 years ago:
  - ✓ Economics
  - ✓ China is looking inward, they don't need us as much anymore
  - ✓ Mexico has signed free trade agreements with 44 countries vs. 20 in the US and 12 in China
  - ✓ Cycle time requirements from customers
  - ✓ Mexico has a much more progressive economic agenda
  - ✓ Total Cost of Ownership

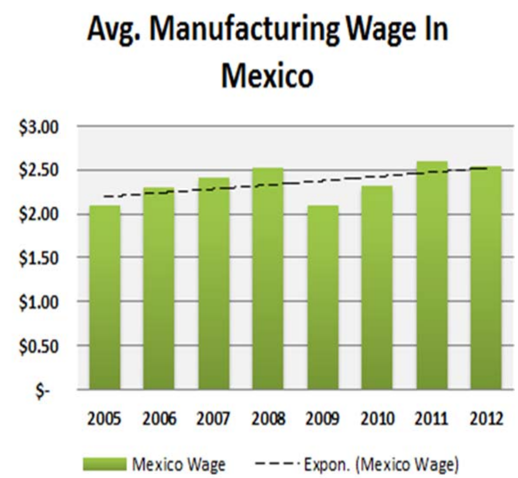
Total Cost of Ownership

- Companies who only look at the per unit cost are missing the picture of China vs. Mexico

  ✓ Labor

Labor is near parity between the two countries





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Total Cost of Ownership

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  ✓ Productivity

Mexico's productivity has offset it's wage inflation. Not the case in China (2/3)

Total Cost of Ownership

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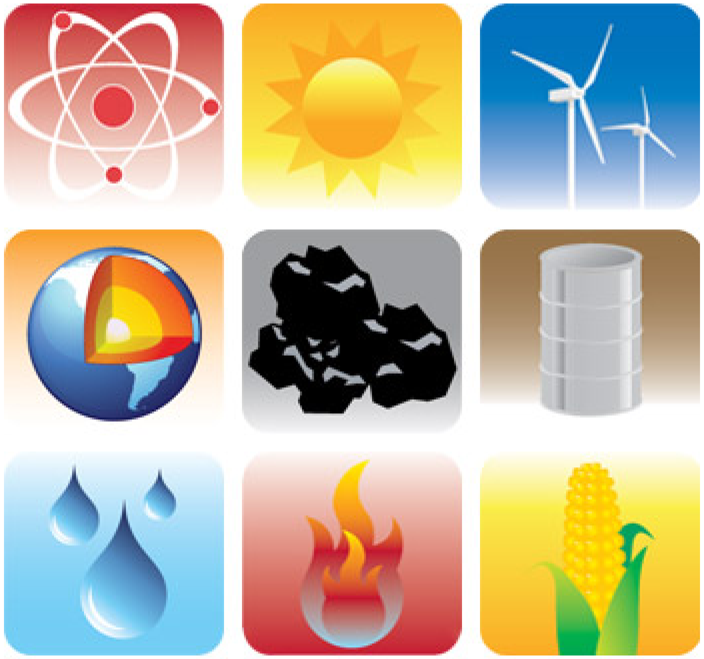
✓ Energy

Natural gas and electricity have decreased 37% in NA with little change in China



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✓ Transportation

Transportation is reduced 65% when produced near consumption

Total Cost of Ownership

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✓ Cost of Capital

The cost of capital for inventory and pipeline negatively impacts P&L's

Total Cost of Ownership

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✓ Currency

Over the last 10 year the Peso is down 12% while the Yuan is up 25% - a 37% swing

Total Cost of Ownership

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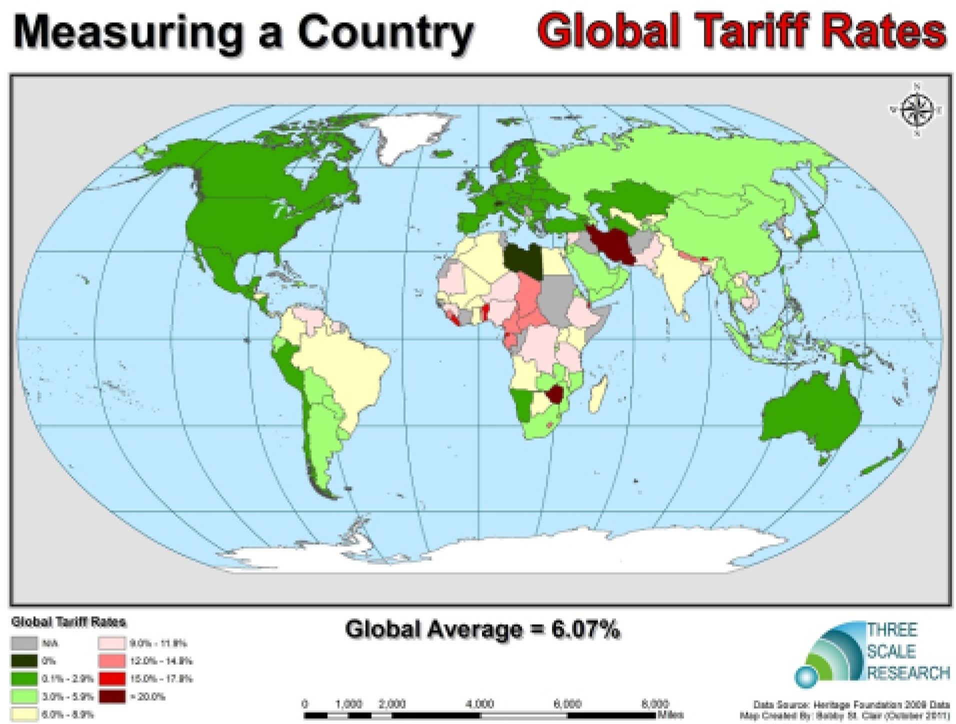
✓ Tariffs/Policy

China has much more restrictive policies than Mexico



Major Differences Between China and Mexico

- Mexico is at wage parity with China when adjusted for productivity
  - ✓ Productivity in Mexico has offset wage inflation while that hasn't happened in China
  - ✓ Wage inflation will continue in the high teens for the foreseeable future in China
- China was rated as the worst IP offender in a 2008 Trade report
- Transportation cost and lead times
  - ✓ Negative differentiator in the market place
  - ✓ More costly to support demand near points of consumption
- Language and time zones make it difficult to work as a team
- The US and Mexico are enjoying significantly reduced energy costs that are expected to continue for decades
- Mexico is our neighbor and 17% of our population is Hispanic vs. 4.8% Chinese
- China's poor environmental record: Risk, Cost, Perception
- Human Rights reputation
- Our free trade agreements and open economic policies provide much more freedom in how we produce goods

Taking Advantage

- There are 4 primary ways to do business with Mexico
  - ✓ Contract Manufacturing: Every state in Mexico has an aggressive economic development Council
  - ✓ Maquiladora: Being along the border has a lot of advantages and specialty treatment
  - ✓ Owning your own Operations elsewhere in Mexico: There are areas of expertise in Mexico that favor various industries
  - ✓ Sheltered Workshop: A Mexican company that does all the work for you in Mexico. Can be up and operational in 45 days. Very cost effective.

The Issues That Favor Mexico vs. China

- **Objective**

✓ Wage Inflation	✓ Freight Costs	✓ Energy
✓ Cycle Time	✓ Travel	✓ Overhead Support
✓ Overhead	✓ Tariffs	✓ Currency

- **Subjective**

✓ Environment	✓ Time Zones	✓ Languages Barriers
✓ Speed	✓ Travel Time	✓ IP Protection
✓ Country Risk	✓ Ease of Starting	✓ Education
✓ Human Rights		

- **Risk**

✓ Geo-Political	✓ Social	✓ Regulatory
✓ Labor Law	✓ Transport	✓ Currency

A Case Study: A company with $60M/yr. in sales

- Reduced Mfg. Cost from U.S. to Mexico $1.0M/year, the same as China
- Lead times: Down 75%
- Shipping costs reduced 60% vs. China
- Owners much more comfortable with Mexico vs. China
- Eliminating 25% profit from contract manufacturer
- Lead time for introducing new products down 75%
- Working capital reduced 30%

Conclusions

- A recent BCG study of direct costs when compared to the US,
  China 95.6 Mexico 91.5

- When you add transportation and average tariffs for Chinese goods coming into the United States, the numbers are more like:
  China 95.6 Mexico 88.5

❖ These benchmarks don't apply to every industry or product type, but they are compelling enough to:

- ✓ Re-look at a company's supply chain strategy
- ✓ Do a total cost "make vs. buy", including direct and indirect costs
- ✓ Understand how "near-shoring" will impact market position
- ✓ Look at the risk factors between Mexico and China

About the Author

Jim Gitney, the CEO of Group50® Consulting, has over 30 years operational experience in companies ranging from start-ups to Fortune 50. He brings a best practices view of how to effectively execute strategy in many industries and cultures. Jim has served as a Chairman, Board Member, CEO and worked many C-Level executive and operational roles.

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