Doing Business in Mexico

A practical guide on how to break into the market

Frank Unger
and Roger Frankel

AUSTRALIA
FOREIGN AFFAIRS AND TRADE

COALAR
council on australia latin america relations

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An initiative of the
Council on Australia Latin America Relations
with the support of the
Australian Department of Foreign Affairs and Trade.

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Disclaimer and Acknowledgements

Special thanks for their contribution to this publication to: David Aarons, Jose Blanco, Paul Bradley, Luigi di Palma, Rob Emerson, Libby Harold, Steve Holt, Justin Macdonnell, Graeme Monkhouse, Ivan Rivera, Jorge Sanchez, Bernard Wheelahan, AmCham Mexico, ACANZMEX, Austrade, the Australian Embassy in Mexico City, the Economic Analytical Unit and other DFAT contributors.

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Production by DPI – Design Print Integration, Melbourne
Design and typeset by Patricia Tsiatsias, Melbourne

ISBN 0-642-50241-2

Foreword by Mark Vaile

I have been delighted to see how many Australian firms are making inroads into Latin American markets. Each time I visit the region I hear success stories of innovative Australian companies securing new markets and taking our export and investment base in new directions. Australia's future economic success depends on our ability to capture new commercial opportunities and find new trading partners all over the world.

Latin America has considerable untapped potential for Australian trade and investment growth in the coming decades. That potential is most evident in Mexico. Australian exporters and investors have already moved to establish a firm foothold in the Mexican market. This is raising Australia's commercial profile in what is a rapidly modernizing country.

While current Australian exports to Mexico include many of our traditional items, such as meat, live animals and coal, Australian technology exporters are moving to the forefront. For example, with the Bank of Mexico's launch of the 20 peso polymer note in September 2002, the Mexican people will now share in the benefits of the Australian-made polymer bank note technology that we are exporting around the world.

To take full advantage of emerging opportunities in Latin America, the Australian Government continues to work closely with the Australian business community to promote understanding of the region's potential and to support the efforts of individual firms that already are looking to make their mark. Through our network of Embassies, Consulates and Austrade offices in the region, the Australian Government continues to promote Australian trade and investment interests and push for better market access.

Moreover, and in support of these efforts, the Minister for Foreign Affairs and I announced in March 2001 that we would create the Council on Australia Latin America Relations (COALAR). Through its dynamic Chair, Mr Bernard Wheelahan, and its executive committee, which includes a number of prominent Australian business people, COALAR is strategically engaged in enhancing Australia's relations with Latin America. As part of its approach, the Council is leading the way in identifying new opportunities in Latin America for Australian firms and in assisting to better coordinate Australia's broader regional efforts. COALAR's decision to commission and fund the production of this book, *Doing Business in Mexico*, the third in a series of publications about business opportunities in Latin America, is just one of the tangible contributions it has already made.

The focus on Mexico is timely. In 2001, Mexico became Latin America's largest economy. It enjoys a level of stability and commercial opportunity unparalleled within the region's major economies. Having discarded its more inward-looking economic past, Mexico has made considerable efforts to reform its economy and open it to the world. At the forefront of these efforts has been Mexico's negotiation of a web of free and preferential trading arrangements, most notably NAFTA and the EU-Mexico Free Trade Agreement. Mexico's close relationship with the United States is also important to the opportunities to be found there. Mexico is an increasingly active and constructive player on the international stage as well, as evidenced by its hosting in 2002 of APEC and the UN Financing for Development meeting, to be followed in 2003 by the WTO Fifth Ministerial Conference.

Mexico is Australia's largest trading partner in Latin America, with the value of our two-way trade now exceeding A$1 billion. The potential for Australian exporters and investors has been clearly evident during my two visits to Mexico in October 2001 and May 2002. During the most recent of these visits I welcomed the participation of several of Australia's leading energy companies in a business mission that explored opportunities in Mexico's burgeoning energy sector. In the same visit I was also able to secure the removal of a three per cent tariff on a number of export items that had acted as a barrier to existing and potential new Australian exporters. Other advancements in our healthy and productive relationship with Mexico have included the recently concluded Australia-Mexico Double Taxation Agreement and a Memorandum of Understanding on Mining Cooperation.

The time is right for many Australian exporters and investors to take a first-hand look at emerging opportunities in Mexico. I commend *Doing Business in Mexico* to all Australian businesses interested in Mexico as a readable, informative and invaluable tool that can help them analyse these opportunities and work toward entering the Mexican market.

Mark Vaile, Minister for Trade

Introduction by the Chair of the Council on Australia Latin America Relations, Bernard Wheelahan

On behalf of the Council on Australia Latin America Relations (COALAR) I am delighted to see publication of *Doing Business in Mexico*. Latin America is a region of dynamic, sophisticated and open markets, which the Council believes have tremendous untapped potential for astute Australian businesses. This potential is highly apparent in Mexico, which currently is enjoying a reform-driven, NAFTA-energised economic resurgence.

Doing Business in Mexico contains a wealth of information for any Australian company interested in the vast Mexican market – from indications of the range of opportunities available to suggestions on how best to structure an entry into the market and how to deal with cultural differences. It also includes an invaluable list of contacts for seeking further information on the issues raised in the publication. From personal experience, I would also highly recommend that prospective businesses establish early contact with, and seek guidance from, the knowledgeable Australian Embassy and Austrade staff in Mexico City as well as Canberra-based officers in Austrade and the Department of Foreign Affairs and Trade.

In producing *Doing Business in Mexico* we have deliberately sought authors who are not only expert in the area, but who also write in an engaging and accessible style able to capture the interest – and serve the purposes – of a wide range of readers. We have placed a premium on accuracy of information and on presenting information which should be particularly useful for businesses seeking to access the Mexican market.

I would like to say something more about COALAR. The Council was established in 2001 by the Minister for Foreign Affairs, Alexander Downer, and the Minister for Trade, Mark Vaile, on the basis of recommendations by the Federal Parliament's Joint Standing Committee on Foreign Affairs, Defence and Trade. All recognized that – once created – COALAR could, through promotional and coordinating activity, act as a catalyst to open up major untapped potential for more productive and mutually advantageous relations between Australia and Latin America.

In its first year, COALAR has taken a strongly commercial approach to its task, focusing particularly on ways to apprise more Australian businesses of the abundant opportunities throughout Latin American. Beyond *Doing Business in Mexico*, Council initiatives continue to include assisting and encouraging business missions to the region, increasing balanced media coverage in Australia of Latin America, and dissemination in Latin America in Spanish and Portuguese of information on Australian capabilities in specific business sectors. At the time of this publication, the Council is just hitting its stride. You can expect to hear more from us – and of our activities – in the near future.

In the meantime I strongly commend to you *Doing Business in Mexico*. On behalf of the Council, I very much hope that, armed with *Doing Business in Mexico*, increasing numbers of Australian companies will be enthused and inspired to seek out new opportunities in what is a fascinating and increasingly prosperous country.

The promised riches of the Mexican piñata await!

Bernard Wheelahan

Bernard Wheelahan, Chair


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Contents

A Piñata

Blindfolded, the child swings a stick through the air at an object it cannot see, but knows is there. Repeated swings are greeted with the laughter, chanting and heckling of the other children milling and skipping around at a safe distance. The eyes behind the blindfold are shut even tighter as the child makes a final monumental effort, crashing the stick into a large, colourful and hollow paper-maché star with seven points, suspended from the ceiling. The cheers and the shower of sweets, peanuts and toys from the centre of the star is the signal all have been waiting for, and as the bandana is pulled from over eager eyes, all scramble for their share of the rich spray of delicacies.

In the days leading up to Christmas, visitors to Mexico will frequently be able to see this traditional and lively game of breaking the *piñata* (*pin-yah-ta*). Like many aspects of Mexican culture, it mixes elements from Europe with those of indigenous Indian origin. Brought to North America by 16th Century Spanish missionaries to attract local converts to their ceremonies, the *piñata*, originally fashioned from fragile clay pottery, resembled both Aztec and Mayan devices. The Aztecs had a richly decorated clay pot atop a pole filled with small treasures, which, when broken by a club, showered the ground with offerings to Huitzilopochtli, the god of war. The Mayans added the blindfold to the game suspending the clay pot by a string.

Combined, these serve as an allegory for those who approach Mexico with a view to doing business: blindfolded, the visitor leaps about trying to crack the Mexican market, while others variously encourage, heckle and laugh. After many fresh-air swings the visitor finally connects and the Mexican *piñata* disgorges its treasures.

So, what sort of a *piñata* is Mexico for Australian business: what is within, what stick should be used, who can lift a corner of the blindfold, and to what kinds of noises is it worth listening?

In the world picture, Mexico is an important place. It is home to 100 million people. It covers roughly the same area as the UK, Germany, France, Benelux, Switzerland, Spain and Portugal put together, it is slightly larger than Indonesia and larger than all the other ASEAN nations together. In Australia it would cover more than Queensland and still be able to accommodate Victoria. The International Monetary Fund (IMF) ranked world economies according to their 2001 gross domestic product in US dollars and by this measure Mexico is the world's 9th largest economy, ranked ahead of Spain, Brazil, India and South Korea (10th to 13th) and behind France, China, Italy and Canada (5th to 8th). Australia was the 15th largest economy.

Mexico is developing rapidly in economic, political and social terms. In its dramatic shift from an inward-looking economy, Mexico is increasingly connecting itself, through the device of free trade agreements, with the other country groupings important to its integration into the global economy. Since joining the US and Canada in the North American Free Trade Agreement (NAFTA) in 1994, Mexico has, after its 1994-95 crisis, acquired an economic dynamism that is reminiscent of East Asia's developing nations in their heyday. In the space of five years since 1996 the country's gross domestic product has doubled[1] to make it Latin

1 DFAT, Mexico Fact Sheet

America's largest economy. Mexico's economy has eclipsed Brazil's by 23 per cent and grown to 2.3 times that of Argentina.

While Latin American countries feature prominently as Mexico's free trade partners (Chile since 1992 and Bolivia, Costa Rica, Colombia and Venezuela since 1995 and Nicaragua since 1998) and have been joined by Israel in 2000, the agreement with the European Union in 2000 makes it the only country in the world tied to the world's two largest economic groupings, on either side of the North Atlantic Ocean. In 2001 similar treaties were made with the European Free Trade Association (EFTA) countries and with Guatemala, Honduras and El Salvador. No surprise, then, that Mexico is now the major trading nation in Latin America, exporting more value than all other Latin American countries put together. Mexico is now looking to its participation in the Free Trade Area of the Americas (FTAA), which has the potential to become the largest free trade grouping in the world.

Confidence in the further upward movement of economic growth is reflected in the fact that although direct investment flows around the world in 2001 slumped by 40 per cent (the first fall in 10 years and the biggest fall in 30 years) some select emerging markets showed an increase: the leading ones amongst these were China and … Mexico.

Mexico offers Australian business some solid economic fundamentals, a dramatically improved foreign investment climate and a legal environment a long way from the unpredictable and corrupt practices of the past.

A good indicator of a country's increasing stability, and hence the decreasing level of risk in doing business there, is the extent to which it is able to cope politically with an election that changes government after 70 years of rule by a dominant party. In this developmental aspect Mexico has shown a maturity which bodes well for its economic and political future. Importantly, this progression also makes Mexico a market of significant, compelling and enduring interest to business as its substantial population partakes of the fruits of international economic integration and the nation fulfils its promise as a regional economic locomotive.

While Mexico displays all the characteristics of the kind of market in which Australian businesses feel most at home, it still ranks behind Finland, Spain and Belgium/Luxembourg as a trading partner for Australia. Although Mexico has begun to attract greater Australian commercial interest, it remains a *piñata* waiting to be tapped with vigour.

This publication provides a description of the *piñata*, its shape and size, its context and contents, the rules of the game, some tips on how to interact with the players, how to swing the stick and how to pick up the rewards. It moves from the general themes of Mexico's physical assets, its people and their economic activities, the political and economic policy settings and the interaction with other countries to the business culture, the opportunities to be found in specific industry sectors and contact points for further information. *Vamos adelante …*

PART ONE Understanding Mexico

Shadows of the Past

It is difficult to jump over one's own shadow. Mexico has a long shadow of recorded history, a period of over 3,200 years of cultural, economic and political development since the Olmecs established themselves where today we find the states of Veracruz and Tabasco. Throughout that time the country has had political and economic systems which were centrally controlled by a procession of a few powerful, privileged groups. One of these was the Spanish conquistador Hernan Cortes, who in 1519 with 600 men, 20 horses and 10 field pieces conquered Mexico's Aztec Empire. While the feat was astounding in its audacity, good fortune and deviousness, it was also the first of many foreign interventions which exploited the local population for the enrichment of foreign powers. From today's perspective some of the twists and turns of Mexican history border on the bizarre. How could, for instance, a Mesoamerican country have an Austrian Arch-Duke proclaimed its Emperor at the instigation of the French, years after it became an independent nation in 1821?[2] Or how could it happen, that Mexico lost half of its original area to a friendly neighbour?[3]

"Tijuana sits near Newcastle and Yucatan is in the Kimberley..."

2 Emperor Maximilian I of Mexico, formerly Arch-Duke Maximilian of Austria, brother to Emperor Franz-Joseph of Austria.

3 Texas gained independence from Mexico in 1836. As a result of the American-Mexican War Arizona, California, Colorado, New Mexico, Nevada, Utah, and Wyoming became part of the United States in 1848. The Gadsden Purchase in 1853 "clarified" the New Mexico border and gave parts of southern Arizona and a slice of southwestern New Mexico to the United States.

The answers are in the pages of history books, but it is that same history that determined Mexico's economic and social development, its attitude to foreigners and the prevailing traditions and social norms and, as a consequence, the ways business is done. Understanding these is essential to successfully doing business in Mexico.

Mexico is a large, diverse and complex country. Understanding this is central to business success.

Earth, Water and Air

If one were to place Tijuana in the north-west tip of Mexico onto the corresponding latitude in Australia, it would sit comfortably near Newcastle in NSW. Moving towards the equator, that would put the southernmost reaches of Mexico on the northern coast of the Kimberley, the Yucatan Peninsula into the Great Sandy Desert, the border town of Matamoros and the Rio Grande's entry into the Gulf of Mexico near Alice Springs, and Mexico City into the Never-Never of the Barkly Tablelands near the Gulf of Carpentaria.

Tapering from 3,326 kilometres along the US border to about 200 km at the Tehuantepec Isthmus about 500 km southeast of Mexico City, the country flares out again into the Yucatan Peninsula and its borders with Belize and Guatemala. With a coastline 9,330 km long facing the Pacific Ocean (including the tongue of the Gulf of California) and the Gulf of Mexico, there are no great rivers cutting across the country's high plateaus. There are deserts, high and rough mountains, mostly small and low coastal plains with small rivers, and sub-tropical and tropical forests. Only about 12 per cent of the land is arable, including over 60,000 sq. km under irrigation, while 39 per cent are permanent pastures and 26 per cent are covered by forests and woodlands that include ebony, mahogany, rosewood, walnut and pines. Deserts and cities make up 22 per cent.

Mexico is not only a large place, it is also high. The average altitude in the country is just over one km high. Mexico City sits at 2,240 metres – about 10 metres higher than the tip of Mt. Kosciusko. The highest point in Mexico is the 5,700 metre Pico de Orizaba, and southeast of Mexico City are the volcanoes tonguebreakingly named Ixtacihuatl and Popocatepetl, both more than 5,200 metres high.

With the variety of landscapes comes a great variation of climates. When nature turns ugly, there are active volcanoes and earthquakes in central and southern Mexico, cyclones along the Gulf of Mexico coastline and tsunamis from the Pacific Ocean. And where nature has not made a mess, human activity has: in the north of the country fresh water resources are scarce and polluted, while in the centre and southeast they are of poor quality and difficult to reach. Raw sewage and industrial pollution have affected rivers in the country's urban areas, the air pollution in Mexico City is legendary and the cities along the US border appear to be trying hard to catch up. The other impacts of civilisation are also felt: deforestation, erosion and desertification. Membership of NAFTA has brought with it closer scrutiny of activities detrimental to the environment – the formation of the Commission for Environmental Cooperation, in which the three NAFTA members tackle environmental issues of mutual concern, is one such mechanism.

The 14th largest country in the world inevitably has a rich geology. Some of this potential has been tapped: Mexico leads the world in the production of silver, fluorite, sodium sulphate and celestite and extracts a wide range of other treasures.

In the Western Hemisphere, Mexico ranks second behind Venezuela in proven reserves of crude oil. Natural gas is also abundant. These reserves have had a major economic and political impact on Mexican sovereignty and independence and their exploitation remains a prime national task with complex political overtones.

People

Of Mexico's estimated 103,407,000[4] inhabitants about one third is under 14 years of age and this is in spite of an annual population growth rate that has slipped from three per cent in the early 1970's to just 1.5 per cent. In addition, the average **life expectancy** in Mexico has climbed to 71.8 years (68.7 for men, 74.9 for women)[5] and infant mortality has been reduced. What this will do for Mexico's consumer demographics in future years is not hard to imagine.

A quarter of the population lives in the greater Mexico City area. At the other extreme, 96 per cent of Mexican towns and villages have less than 1,000 inhabitants. The large urban centres display all the characteristics of modern global cities, but village life brings with it extreme poverty to seven from ten of their inhabitants.

The majority (60 per cent) of **Mexico's inhabitants** is mestizo, or Spanish-Amerindian, another 30 per cent are Amerindian or predominantly Amerindian and nine per cent are described as European. Within the second group, making up about six per cent of the population, are pure-blooded descendants of indigenous groups such as the Náhuatl, Maya, Zapotec and Mixtec, each with their own widely varied and distinguishing cultural characteristics, including languages. About one in 10 Mexicans see themselves as indigenous and as such may have a different set of economic values which determine that, for instance, assets (especially land) are non-tradable sources of identity, community benefit is a higher value than individual profit, traditional leadership groups are trusted more than the official legal system, social organisation is based on prestige and civic duty, and the language is not Spanish.

The point of all this demographic information is to highlight that Mexico contains within it the features of a developed as well as those of a developing country. The extremes and diversity are evident.

In **education**, these extremes are visible in the illiteracy of 10.4 per cent of the population aged over 15 years and in the availability of world-class universities in the wealthy triangle of Guadalajara, Monterrey and Mexico City. Only just over 70 per cent of the population aged over 15 years have completed primary schooling and less than half of the over 15's have completed secondary schooling. The proportion of students in higher education to total population is about one half of that in Australia; but that still adds up to 1.86 million students (vs. 0.67 million in Australia). Education spending hovers at about five per cent of GDP (just below Australia's 5.3 per cent).

In **health**, Mexico has been able to make considerable progress. Cases of whooping cough, TB and polio have been reduced with universal vaccination programs, and malnutrition has been tackled through food support programs such as subsidised milk for over four million

4 Estimated at July 2002
5 CIA – The World Factbook – Mexico

children, breakfasts for three million kids and free bread (tortilla) rations to 1.2 million needy families. In remote areas of the country malnutrition remains a serious health issue.

Why do we need to know all this? These facts contribute to understanding the nature of the Mexican labour force, the **Mexican consumer** and the diversity within the nation. The exact characteristics of each socio-economic group within Mexico's population have been plotted by the members of AMAI, the Mexican Association of Marketing and Public Opinion Research Agencies[6]. Currently there are six urban groupings of interest to business[7], which are periodically revised and updated. A compressed version looks something like this:

A/B – the population segments with the highest standard of living. In the greater Mexico City area they comprise about 9% of all households. In other urban areas they make up about 6% of households. Of families belonging to grouping A/B, 80% own their own home, all have television sets, 71% have cable television, 68% have personal computers, 62% have cellular phones, 98% have a car and 53% have domestic help.

C+ and C – includes families with upper middle class and middle class living standards. In Greater Mexico City they make up about 31% of households, while in other urban areas they make up about 35% of households. In these two groupings 74% own their home, 99% have television, 32% have cable TV, 24% a PC, 34% a mobile, 83% a car and 14% have domestic help.

Mexico has a sizable and sophisticated middle class with a taste for consumer goods, lifestyle products and better education.

D+ and D – the better-off of the lower class, making up 48% of all households in all urban areas.

E – the lowest segment of the population. They make up 12% and about 11% respectively of households in Greater Mexico City and other urban areas. In groupings D+, D and E, 32% own their home, 95% have television, 9% have cable TV, 3% a PC, 9% a mobile, 17% a car and 2% have domestic help[8].

It needs to be made clear, however, that over a quarter of Mexico's population is poor by the country's own consumption measures, living on the equivalent of less than the purchasing power of four Australian dollars a day. The World Bank numbers the poor in Mexico at 45 million, with deep and widespread inequality between regions, ethnic groups and genders. At the other end of the scale, the dozen richest people in Mexico tip the scales at a combined net worth equivalent to 41 billion Australian dollars (see box). The top ten per cent of the population consumes and earns almost 57 per cent of the county's total. The lowest ten per cent has to make do with four per cent[9].

6 Asociación Mexicana de Agencias de Investigación de Mercado y Opinión Pública.
7 National sample census of households in 2000 by ACNielsen Co in cities with a population of more than 50,000.
8 AMAI and AmCham data.
9 From World Bank Country Assistance Strategy, April 2002.

MEXICO'S BILLIONAIRES

1 **Carlos Slim Helu** (net worth US$7.9 billion): Latin America's richest man, involved in technology, telecommunications, retailing and financial services. Controls Telmex.

2 **Lorenzo Zambrano** (net worth US$2.1 billion): Turned family cement business into world's 3rd largest.

3 **Eugenio Garza Laguera** and Family (net worth US$2 billion): Heads Fomento Económico Mexicano (Femsa), a century-old brewery and bottling company. Also part-owner of Mexico's second largest bank.

4 **Emilio Azcarraga Jean** (net worth US$1.5 billion): Heads Grupo Televisa, the world's leading Spanish language media group, recently expanded into Internet services.

5 **Ricardo Martín Bringas** and Family (net worth US$1.5 billion): Heads the big Mexican supermarket chain, Soriana.

6 **Isaac Saba Raffoul** and Family (net worth US$1.4 billion): Investments in polyester. Owns Xtra Immeubles holding company and has control of pharmaceutical distributor Grupo Casa Autrey.

7 **Ricardo Salinas Pliego** and Family (net worth US$1.4 billion): broadcasting, telephony, electronics, and furniture. Controls TV Azteca, Mexico's No.2 broadcaster, and retail chain Grupo Elektra.

8 **Alberto Bailleres** and Family (net worth US$1.2 billion): Chairman of metals, mining, and chemicals conglomerate Industrias Peñoles.

9 **Alfonso Romo Garza** (net worth US$1.2 billion): CEO of the world's largest seed distributor, Savia, and owner of Mexico's largest insurance company. Through his venture capital group, Pulsar Venture Group, invests in Internet infrastructure, including software development for small businesses.

10 **German Larrea Mota-Velasco** (US$1.1 billion): Controls Grupo México, which recently became the third largest copper producer in the world.

11 **Carlos Peralta** (US$1.1 billion): Main shareholder in Grupo Iusacell, Mexico's independent wireless telecommunications company.

12 **Maria Asunción Aramburuzabala** and Family (net worth US$1 billion): Vice Chairman of Grupo Modelo, Mexico's largest brewery.

Source: Forbes World's Richest 2000.

Infrastructure

Mexico has slightly less than the length of **roads** of New South Wales and Victoria combined: 332,000 kms. The difference is that while half the Australian states' total is paved, the Mexican mileage is one-third hard-topped. Of Mexico's 111,000 kms of paved roads 6,335 are expressways and together with the 221,000 km of unpaved roads these accommodate 15 million vehicles[10]. Early in the Mexican economic reform process under the Salinas government private companies were sold rights to operate toll roads. These did

10 As compared to 6.7 million vehicles registered in NSW and Victoria.

not achieve adequate volumes of traffic and after the economic crisis of 1994 the government had to bail out the toll-road operators and re-nationalise the highways. New initiatives in private road infrastructure development can be expected.

The condition of Mexico's infrastructure reflects a developing country in transition. Repairing and strengthening it is a Mexican priority and a business opportunity.

81 per cent of Mexico's 27,000 kms of **railways** are in private hands, the original state-owned railways Ferronales having been split into five regional companies and the management of the three largest handed over on 50-year concessions in 1997-8. In the five years from 2000 more than US$13 billion are due to be spent on facility and track improvements and another US$5 billion on long-term lease-financing of hauling and traction equipment. Mexican railways move over 85 million tonnes of freight.

As can be expected from a country with 9,330 kilometres of coastline, Mexico has many **ports**: 108 at last count[11], covering 190 square kilometres of port facilities. The biggest and most important of these number 26 and here, too, privatisation has moved apace. By 1998-99 the administration of most ports had been awarded by concession to private companies called Integral Port Administrations, which are permitted to be up to 49 per cent foreign owned (port service providers can be fully foreign owned). They are home to a total of some 1,000,000 dead weight tonnes of Mexican shipping (a little less than one third of Australia's total). Mexico moves 80 per cent of its foreign trade and one third of its domestic freight through these ports, making a grand total of nearly 250 million tonnes per year.

There is some disagreement about the number of **airports** in Mexico. Government sources make it 55 international and 29 domestic airports. Bancomext and The Economist listed 35 international airports for privatisation, while the CIA, who may see airports where others do not, has found 1,848 of them all over Mexico, including 238 with paved runways and 1,610 unpaved, as well as two heliports. They are probably all right. Privatisation of airports commenced in earnest in 1998 when 35 airports covering 97 per cent of total passenger numbers were split into three groups, which were auctioned to joint Mexican/foreign consortia. Mexico continues to debate the location for building a new international airport for Mexico City.

An early candidate for privatisation was Teléfonos de Mexico (Telmex), the **telecommunications** monopoly, which since its privatisation in 1990 has doubled telephone lines in density per population to 12.5 million lines. By 1996 long-distance calls were opened to competition as were local calls by end 2000, all overseen by the regulatory agency COFETEL. Considerable activity continues in this sector, with over 20 million mobile telephones connected in 2001 and a fluctuating number of telecommunications service providers operating in the market.

Economic Activity

Mexico's **agriculture** is historically inefficient because of the size of landholdings and the lack of capital. Since the constitutional reforms of 1992, occupants of the *ejidos* (sub-divided plots of communally-owned land) have full property rights over a total of nine million plots of land covering half of Mexico's surface. The reforms have given farmers the

11 From Mexican government information sources.

capacity to buy, sell or rent land, hire labour and go into cooperative ventures with third parties, including domestic and foreign investors.

The modernisation of the agricultural sector is underway, and is most evident, paradoxically, in the driest part of the country. The larger northern farms have benefited from proximity to the US markets and irrigation schemes built over 35 years ago, but the smaller holdings in central and southern Mexico still have a way to go. In these areas there is an overlay of indigenous attitudes to land which operate differently from those implicit in structural reform.

Agriculture employs about a quarter of Mexico's workforce and accounts for one-twentieth of its gross domestic product. Government support for agricultural production, with annual cash payments to producers of staple goods, occurs through a program called *Procampo*, the *Programa de Apoyos Directos al Campo*.

Most important for domestic consumption are maize, sorghum, wheat and beans and contributing to exports are vegetables, fruit, coffee, sugar, and cotton. Barley, rice and soybeans are produced in smaller quantities. Livestock accounts for one third of agricultural output, with meat production totaling more than four million tonnes, mainly beef, pork and poultry, almost 50 per cent more than Australia produces. In milk production Mexico and Australia are running neck-and-neck at between 9 and 10 billion litres.

Another part of the primary production sector, **forestry**, is in difficulty. According to the findings of the Mexican Environmental Protection Office, exploitation and severe fires a few years ago have far outstripped investment and development. A new forestry commission is to push for sustainability, particularly in the 23 states where the alarm bells are ringing loudest.

Mexicans are not big fish eaters. At about 11 kilograms of fish consumed per head of population a year, there is a lot of enthusiasm about the upside potential for **fisheries**. Hovering between 1.3 and 1.6 million tonnes annual catch of mostly tuna, prawns, sardines and squid, there is a good export market for the product, but as in most other parts of the Mexican economy, fresh investment in boats and the privatised ports is necessary. Aquaculture is being encouraged, and legislation permits foreign investors to own 100 per cent of a Mexican company involved in this activity, unlike fisheries, where the limit is 49 per cent.

Tight government control over access to mineral resources has meant that the Mexican **mining** industry has not met the full potential represented by the abundance of resources. At just over one per cent of GDP, its contribution to the economy has some upside, hinging on increased investment, the application of new technologies and the legal framework required to make the sector attractive for investment and to international mining companies. Some significant reforms have been made, particularly in respect to limits on concessional land, the period covered by mining and exploration concessions and enabling 100 per cent foreign ownership of Mexican mining companies.

26 tonnes of gold were produced in 2000 from high-grade deposits in the states of Sonora, Durango and Guanajuato, and the largest unexploited gold and silver reserves are thought to be in Chihuahua state. Mexico is the world's largest silver producer with an annual 2.5 million kg output, or about 17 per cent of the world's total, coming mostly from mines in the states of Zacatecas, Chihuahua, Durango and Guanajuato. 357 thousand tonnes of zinc and 156 thousand tonnes of lead, as well as 376 thousand tonnes of copper round off the major mining hits.

Most important for their economic impact have been the huge oil and gas resources of Campeche Bay in the Gulf of Mexico and the states of Veracruz, Chiapas and Tabasco, which have placed Mexico ninth for crude oil and 21st for natural gas in the 2001 table of countries with the world's proven reserves. In 2000 crude oil production ran at 3,012 million barrels a day (one heavy and two lighter varieties) and the production rate of natural gas was 4,679 million cubic feet per day, about 50 per cent higher than Australia[12]. Although declining due to decreasing exploration, Mexico's production and export of oil continues to be of vital significance: it earned almost US$13 billion in 2001 (almost US$16 billion in 2000) as an export and contributed one third of the government's budget, through the government-owned monopoly *Petroleos Mexicanos* or Pemex.

Pemex is the world's sixth largest oil company, controlling virtually the entire oil and gas sector in Mexico: exploration, extraction, refining, petrochemicals, transport, storage and distribution. This exclusivity is guaranteed by Mexico's constitution and reflects the nationalist sensitivities of earlier decades. There is, however, an intention and a necessity to open as much of this sector to private and foreign investment as possible, although this is unlikely to happen at too fast a pace. The levels of investment required to make necessary improvements to the oil industry are of such a large magnitude, that even with dramatically increased investment funds available to Pemex (US$14.7 billion in 2002) it will be difficult to catch up on decades of under-spending. While privatisation of Pemex is off the agenda, modernisation and efficiency gains are on (for opportunities see Energy and Resources, page 56).

Needless to say, oil plays a major part in the supply of **electricity** to the homes and factories of Mexico, although it varies between the regions: 100 per cent on the Yucatan Peninsula to 15 per cent in the Northeast. On average, 50 per cent of electricity generated uses oil as fuel, 11 per cent is gas-fired, five per cent comes from Mexico's sole nuclear power station and 3.5 per cent is renewable in origin, with a further 11 per cent coming from coal-fired power stations. US-based Mission Energy is Mexico's largest coal producer, but the coal is more suitable for use in steel-making due to its high ash content. Increasing amounts are expected to be imported, mostly from the US, Canada and Colombia, but also from Australia.

Manufacturing has been the outstanding performer in Mexico's economy.

Since recovering from the debt crisis of the early 1980's and accelerating with the implementation of NAFTA, there has been a shift in industrial development from import substitution towards export orientation. While it is a familiar pattern in Asian nations and East European industries, Mexico has one big advantage: the world's largest and richest market is a neighbour, made uniquely accessible through a free trade agreement. When relatively low wages are added to the equation, the result is that in the early part of the new millennium manufacturing exports have a share of 88 per cent of total exports and intermediate goods make up 77 per cent of imports. Transforming these imports into exports employs millions and creates over one fifth of GDP.

The form of manufacturing of most interest to foreign companies with their eyes on the US market is something called a ***maquiladora***. This is in-bond assembly of imported intermediate goods for re-export. Making up a large portion of Mexican manufacturing,

12 From the Pemex website, www.pemex.gob.mx, and Australian Bureau of Statistics, Year Book Australia.

about 3,500 *maquiladora* plants are dotted mostly along the US border and in major conurbations. They assemble motor vehicles, textile, clothing and footwear products, electronic and electrical items, furniture, chemicals, food-related products, tools and machinery, toys and sports equipment and supply a variety of related services. There are special rules governing the establishment and operation of *maquiladora* enterprises, but they have been remarkably successful, even though they are more susceptible to US economic cycles (for further details see page 43).

The manufacturers oriented towards the domestic market have had problems of their own: they have had to compete, with lessening protection, against strong import competition for the attention of increasingly sophisticated Mexican consumers. Mexican manufacturers are gradually moving from being low-tech and uncompetitive towards modernisation, adopting ISO certification in increasing numbers, and the proportion of locally produced input materials is increasing from a very low base (in the manufacture of electrical, electronic, chemical and textile products as little as 2-3 per cent is locally sourced). The centres for manufacturing are Mexico City and environs and the states of Nuevo Leon, Baja California Norte, Chihuahua, Jalisco, Guanajuato, Coahuila, Puebla and Tamaulipas.

The **construction** sector has had a tough time since the 1995 slump when it contracted by almost one quarter by value and 45 per cent by employment. By 1999-2000 it had clawed its way back to earlier value levels, but still only employs about a quarter of a million people. Part of the problem was that the larger companies were hit by the fallout from the failed toll-highway privatisation. In the year to early 2002, construction output rose 9.1 per cent[13].

As in most economies, the **services** sector contributes the lion's share to GDP, almost 70 per cent in Mexico's case, and there have been major changes here too. In **retail** trade, foreign chains have moved in and forced Mexican companies to lift their game through modernisation. This has expanded into the smaller regional centres, improving services there, while major shopping centres are becoming part of the landscape. These large and modern outlets are, however, still less than half the retail story in terms of sales: most of the business is still done by small, family-run businesses without the huge range of goods offered by the discount and hypermarket chains.

The full range of **transport and logistics** services is available in Mexico, including full trucking, LTL (less-than-truckload), air cargo, couriers, brokers, warehousing, outsourced logistics providers and logistics information technology[14]. Estimates put the contribution of this sector at about 10 to 12 per cent of GDP. The needs of foreign companies, particularly those of *maquiladoras*, have changed the face of this industry.

Tourism makes a large and growing contribution to the Mexican economy: it earned over US$8.4 billion in 2001 and directly employed six per cent of the workforce, capturing 3-4 per cent of worldwide tourism. What has helped the industry progress is a good promotional effort and the relaxation of investment rules, which has brought in foreign investors and more private sector interest in hotels, resorts and the associated capacity building. Not surprisingly, US tourists make up more than 80 per cent of the total.

13 Carlos Gamez (published by Bloomberg on 11 June 2002)
14 Getting to the Market, The Guide to Mexico for Business, American Chamber of Commerce of Mexico.

Liberalisation of the economy cannot happen without liberalisation of the **financial services** sector: one needs the other. In 1982 all banks in Mexico had been nationalised, a process reversed in 1991-2, when the government privatised 18 banks in which it held majority ownership. New domestic banks were then permitted and with NAFTA accession, licenses were granted to foreign banks from the US and Canada in 1994. By the start of 1999, all limits on the foreign ownership of banks had been removed and today Spanish, US and Canadian capital controls 89 per cent of Mexican banks.

The banks had a tough time in the mid 90's, particularly when recession pushed bad loans to one-fifth of total loans in 1996. Seven different programs of assistance to banks were introduced, including capitalisation and debt-relief programs and efforts to sell off debt and troubled financial institutions. Mexico's financial market has now achieved a high level of consolidation: the six largest domestic banks now account for over 85 per cent of total assets, with the largest three controlling two thirds of all assets.

Mexico also has five development banks active in specific contexts: small and medium business, foreign trade, public works and services, the sugar industry and for rural development. By far the most important of these are Nafin (small and medium business) and Bancomext (foreign trade).

The Mexican stock exchange (BMV) began with the trading of mining stocks in 1850 and currently has a market capitalisation of US$154 billion, about 40 per cent of the Australian Stock Exchange with about 200 firms listed. The *Bolsa Mexicana de Valores* has been open to foreign traders for over a decade.

The Political and Economic Settings

The Mexican constitution, re-written in 1917 to update one originally adopted in 1857, set some of the basic themes for 20th Century preoccupations. It gave public interest primacy over private property rights and specifically provided for land reform. It severely limited the power and influence of the clergy and highlighted the rights of workers. It also established the federal system of government with its 31 states and one Federal District, and saw to the separation of the powers of government into its three components of executive, legislature and judiciary. Before the political reforms of the Nineties the power of the executive had been significantly stronger than the other two elements, but there has been a clear development towards more independence for the courts and more say in politics for the two houses of parliament.

The presidential elections in July 2000 represented a turning point in Mexico's recent history. In what has been described as the country's most open and democratic election, Vicente Fox Quesada and the Partido Acción Nacional (PAN), in alliance with the Greens party[15], ended seven decades of domination of Mexico's political life by the Partido Revolucionario Institucional (PRI). There was also another qualitative change, in that no single party has an absolute majority in either of the parliament's chambers, the Chamber of Deputies or the Senate, and that decision-making was being driven even more by a wider range of interests requiring more compromise and cooperation.

15 Partido Verde Ecologista de México (PVEM)

Mexico has reached a level of political maturity and economic stability that makes it a more attractive place to do business than in the days of the de facto one-party state and an economic fragility that turned every problem into a crisis.

These things did not happen overnight. The election result was a reflection of the changes that had been occurring in Mexico for a much longer period of time. Inadequate policy settings in the 1970s led to an economic crisis in 1982 as a result of unmanageable foreign debt, and governments, starting with the one headed by Miguel de la Madrid (82-88), had to bite into the sour apple of structural reform. Economic reform gathered momentum as well as opposition under President Carlos Salinas de Gortari (88-94). Social unrest in 1994[16] showed that economic reform by itself was not enough. Salinas pushed electoral reform to make the process less liable to manipulation and more inclusive of dissent. His government also continued the opening of the economy through membership of international fora and signature of the North American Free-Trade Agreement (NAFTA), thus setting the points for unprecedented economic change. By 1996, during the presidency of Ernesto Zedillo Ponce de León (1994-2000), all four major political parties had agreed on new election rules and approved the required constitutional changes.

One measure of the modernising changes wrought during the de la Madrid and Salinas presidencies was the reduction of the number of state-owned enterprises. From 1,155 companies in 1982 the state's direct hand in the economy was reduced to 412 enterprises in 1988 and further to 215 by 1994. This kind of structural reform was one of the ingredients to Mexico's remarkable metamorphosis, and needed to be administered along with many other changes. A reduction of government borrowings was engineered through tighter controls on government spending. An "accord" between government, labour and business (called the "*pacto*" in Mexico) saw inflation reduced from 52 per cent in 1988 to seven per cent in 1994. This had an added benefit of pushing down interest rates, further reducing cost levels, kicked along by the liberalisation of the financial markets: 18 government-owned commercial banks were privatised, new private banks were allowed to open and US and Canadian banks allowed entry. Exchange controls were abolished and the Banco de México (Reserve Bank) was given partial independence.

The tricky bit was the word "partial". Old habits die hard, and the government retained control of the exchange rate and kept the currency high. By 1994 the Mexican peso had become overvalued when taking into account the effects of trade liberalisation and its associated economic growth. Trade and current-account deficits grew to worrying levels without the corrections a floating currency would have provided.

In late 1994 when he took office, President Zedillo was faced with a familiar cyclical pattern at the beginning of a new administration: spiraling debt, empty coffers and an overvalued peso. His response was equally predictable: blame the predecessor, devalue the peso, introduce tough economic measures and get some help from the international financial community to get the country back on track. Within a few hours of the decision to devalue the currency, billions of US dollars fled the country.

16 The uprising in Chiapas by the Zapatistas (Ejercito Zapatista de Liberacion Nacional or EZLN)

The resulting crisis was overcome by another "*pacto*" and an undertaking to float the peso, which convinced the US Treasury, the IMF and the Bank of International Settlements to refinance Mexico's short-term debt. Progress was made on inflation and the economy grew by more than anticipated: at an average of five per cent every year since the crisis, even hitting 6.9 per cent in 2000. In that year real wages and salaries went up for the first time since 1994, but still remained 25 per cent below pre-94 levels.

The US economic slowdown of 2001 inevitably affected Mexico, reducing the 6.6 per cent GDP growth rate in 2000 to an almost stationery minus 0.3 per cent in 2001. Most of the impact was in industrial production and new investments, where declines of 3.4 and 5.9 per cent were felt. The Mexican consumer, however, had his foot firmly on the accelerator pedal. Unused to a strong and stable currency and twitching from conditioning of the past, the mood of "… if you don't get it or do it now, you won't be able to at all once the peso devalues…" saw consumer spending rise five per cent and consumer imports by 10 to 15 per cent.

Perhaps more important for the Mexican economic performance is the high investor confidence in the country, evidenced by the huge inflow of capital. Over a seven-year period more than US$10 billion a year of foreign direct investment, much of it in the automotive sector, has demonstrated that confidence. The upgrade of Mexican government debt to investment grade by ratings agencies also reflects that confidence.

There are some novel perceptions to accept: inflation has settled below five per cent, the peso is stable, investor confidence is high, the economy has a global orientation and the middle class is rapidly growing. These are not unusual achievements in the Asia-Pacific hemisphere and while the reform process is far from complete, the central lesson from Mexico's economic setting is there to be learned: although the country looks, feels, tastes and sounds Latin American, every passing day makes it more North American and global.

The External Sector, NAFTA and the Influence of the US Market

Complementing the political and economic changes at home are those concerning Mexico's relationship with the rest of the world. For most of the last two centuries the US has been the predominant foreign influence in Mexico. Since the completion of NAFTA there has been particularly close cooperation and when Mexico experienced financial difficulties towards the end of 1994, the Clinton administration provided 20 billion dollars from the US Treasury to prevent a worse situation. As with most neighbours, there have been difficult issues involving cross-border illegal and criminal activities, foreign policy differences on Cuba and arguments over water in times of drought, but levels of cooperation have continued improving.

Mexico has sought to counter-balance its reliance on the US with a greater emphasis on integration into the global economy. In 1986 Mexico joined what was then called the General Agreement on Tariffs and Trade (GATT), became a member of the Asia-Pacific Economic Co-operation (APEC) forum in 1993, the Organization for Economic Cooperation and Development (OECD) in 1994 and completed a string of free trade agreements that tie Mexico into its own region and into the world's major trading blocks.

"Through its network of Free Trade Agreements, Mexico has preferential access to 860 million consumers in 32 countries covering 60 per cent of the world's GDP".

This is an impressive line that comes up near the beginning of presentations by the Mexican Council for Foreign Trade (COMCE). In the year 2001 Mexico's total trade with the rest of the world was US$326 billion, of which US$158 billion were exports and US$168 billion came as imports. And that, as the Council proudly declares, makes Mexico the seventh largest trading economy in the world and first in Latin America. That makes its exports bigger than Turkey, the Czech Republic, Poland and India combined, and Mexico a bigger import market than all Eastern European countries combined.

Mexico's trade growth in the decade to 2000 is matched only by that of China: both registered an annual average growth rate of above 15 per cent. In the process of quadrupling its exports, Mexico has built up its trading position in the US to become its neighbour's second largest trading partner after Canada, ahead of Japan and the UK and Germany combined, passing 11 per cent of total US imports for the first time in 2000.

What has gone hand-in-hand with this growth in trade is the rapid increase in foreign direct investment. In the years from 1994 to 2001 almost US$100 billion flowed into Mexico, two thirds of it into the *maquiladora*, about 14 per cent into financial services, almost 12 per cent into trade and the rest into energy, infrastructure, mining, agriculture and tourism. Between 1994 and 2000 the sources for foreign direct investment were 63.4 per cent from the US, 19.2 per cent from the European Union, 5.8 per cent from the Asia-Pacific area and 11.6 per cent from all other sources. Of the total of investment funds from the Asia-Pacific some 92.4 per cent are tied up in manufacturing, and it does not take much to work out why this is so.

NAFTA currently allows for 84 per cent of Mexico's non-oil exports to enter the US free of duties and quotas. In return, 40 per cent of US and Canadian export goods have the same free access to Mexico. Almost 90 per cent of these imports are intermediate goods (not made or sold in the Mexican market) or capital goods such as machinery and high technology equipment and systems.

Due to these benefits, NAFTA enjoys more support in the traditionally inward-looking and protectionist Mexico than it does in the US. In fact, the Mexican economy is the prime beneficiary, both in terms of exports and of investment flows. As a result, Mexican exports to the US have grown dramatically making up a dominant 89 per cent of Mexico's total exports in 2001. The next most important destination for Mexican products is the EU, taking 3.5 per cent of the total with the other NAFTA partner, Canada, in third spot with another two per cent. The situation is more diverse in Mexico's imports, but not by much . The US provides 80 per cent of Mexico's imports, with the No.2 spot held by Japan on 4.5 per cent followed by Germany on 3.6 per cent and Canada on 2.5 per cent.

In that context, when the US places a ban on Mexican tomatoes or embargos Mexican tuna or makes life difficult for Mexican truckers delivering product into the US market, then this quickly becomes a big issue for Mexican business; more so than concerns about the effects of rapid industrialisation on the country's ecology or of increasing cultural influence from the north.

The same economic dependence is evident in the flow of foreign direct investment into Mexico. The US dominates the inflow. In 2001 it furnished some 82 per cent of the year's total.

FOREIGN DIRECT INVESTMENT IN MEXICO – 2001

	Total Direct Investments	
Source country	**US$ million**	**Per cent**
USA	19,115.9	82.5
The Netherlands	2,251.9	9.7
Canada	803.5	3.5
France	246.7	1.1
Spain	156.5	0.7
Japan	151.4	0.7
Luxembourg	122.5	0.5
Switzerland	100.9	0.4
Others	219.1	0.9
Total	**23,168.4**	**100.0**

APEC is receiving more attention by Mexican policy makers. The Americas side of APEC is home ground for Mexico; it is the Asian side where new connections are being sought. The trade and investment imbalance Mexico faces is not only in the difference between the ingoing and outgoing flow, but also in the direction of that flow. The relationship with the full arc of western Pacific countries, from Australia and New Zealand through South-East Asia, East Asia and North Asia, is comparatively inconsequential for all involved. It resembles, as does the Latin American-East Asian relationship generally, an empty space waiting to be filled.

In its free trade agreement with the EU, which has been in force since 2000, Mexico benefits from a more gradual adjustment period. At its start, just over 58 per cent by value of Mexican exports to the EU and only 27.6 per cent of EU exports to Mexico entered duty-free, but all tariffs are expected to be eliminated over a ten year period. Of course there are exceptions, and it will come as no surprise to Australians that these are from the sensitive agricultural sector: some crops, meat, sugar and dairy products.

Mexico's merchandise trade deficit in 2001 and 2002 was between US$8 and 10 billion, and the reasons for this have been the nexus between imported intermediate products and processed exports and the demand for imported products by Mexico's consumers. What doubles the current account deficit are net interest payments, but it is debt that is well regarded in international markets, as it is clear that Mexico has largely decoupled from other Latin American economies.

The Role of the Regions

Regardless of all the finest broad-brush presentations about a particular country, in the final analysis business is done between people in a particular place and time. Just as the choice of business partners is a central issue in doing business anywhere, so is the place where the business is done, particularly when that business involves an investment. In an arrangement familiar to Australians, Mexico is subdivided into states (page 18), each with their own governments and their own economic, geographic, social and financial strengths and weaknesses. It is also categorised into regions.

A closer look at Mexico's 31 states and one federal territory is worth the effort, to see that Mexico contains great variations in socio-economic characteristics and business cultures.

Centred around Monterrey, the Northern Region is known for its heavy industry and its straight-talking, direct, hard-working, thrifty and decisive people.

The centre for the Western Central Region is Guadalajara where the family-run small and medium-sized business predominates. In recent years multinational companies have set up their subsidiaries in the region, adding further dynamism to the economy as well as less traditional forms of management to the local easy-going style.

The Southern Region, including the Yucatan Peninsula and the areas south of Mexico City to the borders of Guatemala, is the least developed part of Mexico although big efforts have been made to increase and diversify industries there (see Plan Puebla-Panama). Paternalistic and autocratic management styles still predominate.

The most sophisticated part of the country, Mexico City and its metropolitan area, is on a par with the world's major conurbations, strongly influenced by an internationally integrated business environment. This is Mexico's answer to New York, Tokyo, London and Shanghai. It accounts for almost a quarter of the country's GDP and more than a fifth of its manufactured value-added.

All along the border with the US one can observe how the old and new in Mexican society mingle: the proximity of the US and the foreign influence on business and management styles is pervasive, often creating a nationalistic reaction.

Each state has a promotional arm with the purpose of drawing business connections into their state. They provide personal assistance in any exploratory efforts, giving access to their data bases on investment opportunities and government programs, discussing investment incentives and capacity building programs, and generally making up some of the cheer squad while the *piñata* is being assailed.

Over the last decade, government decision-making has been progressively devolved towards state and municipal governments in a decentralisation process called *federalismo*. This trend was boosted by the transfer of major budget lines to these levels of government in 1997 and even further after the 2000 election of President Fox, who, as a former state governor, made *federalismo* a priority. This is no easy task, as it will in essence require the federal government to contract with 32 first-tier and 2,400 second-tier sub-national governments.

Industrial Parks

The provision of modern infrastructure in designated industrial parks throughout the country is one of the ways Mexico has promoted investment and modernised its economy. The Mexican Bank of Foreign Trade (Bancomext) lists some 171 such parks[17] located in 83 cities in 26 states and Mexico City, covering an overall total of 27,500 hectares, of which 42 per cent is vacant. The American Chamber of Commerce of Mexico assessed nearly 300 parks as ideal for light industries such as automotive parts, electrical and electronic components, textiles, metal machinery products, plastics, chemicals and so on. The average size of a park is 160 hectares (with 67 ha. available), accommodating 3,120 companies with 585,000 employees at an average of 187 per company. Two-thirds of these companies are Mexican, with the remainder foreign-owned and a small number (three per cent) in mixed ownership. The Bancomext research contains a wealth of information, including on the transport infrastructure, comparative analyses of production costs, communications costs and rates, and details on location, contacts and everything else the budding entrepreneur could possibly desire. Most importantly, it has information on the preponderance of specific industries by park and state. The tip is to choose a park where the chances of creating or joining a cluster of related or complementary companies in common industries are high.

The Mexican Bureaucracy

The speed and the transparency of decision-making at the federal level in Mexican government have improved immeasurably, and there are prescribed maximum time limits on administrative processes. In the years to 2000 alone, the impressively named *Comisión Federal de Mejora Regulatoria (COFEMER)*, or Federal Regulatory Improvement Commission, removed almost half of the information, registration and permit requirements imposed on businesses by 11 federal government ministries. It also simplified 90 per cent of those remaining. According to COFEMER these business formalities had been obsolete, unnecessary or even just too detailed to be of much use to anyone. To make all current processes more transparent, COFEMER is collecting all enforceable business formalities in one central spot: the Federal Registry of Business Formalities, which will also be made available on-line on the internet in the language spoken by 450 million people: Spanish.

17 The Mexican Bank of Foreign Trade (Bancomext), *Industrial costs in Mexico 2000, A Guide for Foreign Investors, 2000*.

The same basic rule applies to business activities in Mexico as it does in any market: local lawyers, accountants and other advisers, who have an intimate knowledge of the local bureaucracy and who have experience in the needs of business, are just as indispensable as they are at home.

This applies doubly at the level of state and municipal government, where most difficulties in regard to red tape and corruption are likely to occur. Government at this level controls many business formalities, including licensing, zoning and environmental regulations. Deregulation has also been encouraged here, but the response has not been uniform: in a setting not unfamiliar to Australian business, the federal system places many aspects of business regulation in the hands of state administrations.

At the federal level there are a number of ministries which are of central importance to foreign business in Mexico.

Ministry of Agriculture, Livestock, Rural Development, Fisheries and Food – ***Secretaría de Agricultura, Ganadería, Desarrollo Rural, Pesca y Alimentación* **(SAGARPA): issues import authorisations for agricultural products and products used in agriculture.

Ministry of the Economy – *Secretaría de Economía (SE), formerly the Ministry of Commerce and Industrial Development* **(SECOFI)**: issues import permits and is a central source of information on all aspects of business and investment. Within this Ministry is also the **General Directorate of Standards** which sets and administers the Mandatory Mexican Standards (NOMS), and

Federal Regulatory Improvement Commission (COFEMER), which includes the Federal Registry of Business Formalities, and links to individual state regulatory agencies.

Ministry of the Environment and Natural Resources – *Secretaría del Medio Ambiente y Recursos Naturales* **(SEMARNAT)**: issues import authorisation for products used in industries within its areas of responsibility.

Ministry of Finance – *Secretaría de Hacienda y Crédito Público* **(SHCP)**: issues the taxpayer registration number which is mandatory for all businesses and resident individuals.

Ministry of Foreign Relations – *Secretaría de Relaciones Exteriores* **(SRE)**: approves company names and issues incorporation permits.

Ministry of Health – *Secretaría de Salud* **(SS)**: issues import authorisations for medical products, pharmaceuticals and hospital/medical equipment.

In the following chapter, Operating in the Market, there are some strategies for dealing with the bureaucracy.

The Australia – Mexico Relationship

The Mexican-Australian commercial relationship took off sometime during 1997. After bouncing along unspectacularly for many years at approximately A$300 million, bilateral trade now stands at around the A$1billion mark. It ranks Mexico 34th as an export market for Australia and 30th as a supplier. Interestingly, in an analysis of merchandise trade Australia displays a developing country profile (coal, live animals, meat, dairy and wool account for close to 70 per cent of Australian exports), while Mexico's exports to Australia are those typical of a developed economy (pharmaceuticals, fertilizers, computer parts and equipment, automotive products, telecommunications equipment, photographic supplies and other manufactured goods represent over 70 per cent). While the balance of merchandise trade has consistently been in Mexico's favour, the deficit in 2001–2002 was substantially less due to the strong performance of traditional Australian exports. In October 2002 the exchange rate was A$1 = Pesos 5.53.

Foreign investment flows are not significant. According to the Economic Analytical Unit (EAU) of the Department of Foreign Affairs and Trade[18], Australian direct investment in Mexico represented only 0.06 per cent of Mexico's FDI inflows between 1994 and 2000, at US$39 million. Mexican investment in Australia is negligible. The EAU study numbered Australian companies registered in Mexico at 59, citing the Mexican Ministry of Trade and Industrial Development. Of those able to be identified, there was a heavy concentration in mining and manufacturing.

Neither country features prominently on the other's horizon. Latin America has not been a priority region for Australian trade, aid or investment. Just over 1 per cent of our total trade takes place with Latin America and only 0.06 per cent of our aid is spent in Latin American countries. The truth is, if we have seen each other at all, we have seen each other as exotic and distant tourist destinations and as rivals on world markets, and there is a process of discovery as both countries look beyond respective traditional horizons and further match each country's needs with the other's competitive advantages.

Relative size, and the strength with which NAFTA arrangements endow Mexico, suggest that the balance of advantage from a more dynamic relationship should be towards Australia, provided Australian companies can approach the Mexican market in a strategic way, transcending the pursuit of easy profit from one-off trade deals. Their own proximity to the US market, favourable trading arrangements in place with the European Union, the very size of its domestic economy make Australia, for Mexicans, a small and distant market. Mexicans are often surprised to discover that the size of the two economies is similar. The initiative to energise the relationship rests squarely with Australia, with a dual purpose: first, to challenge US dominance in areas where Australia is able to supply Mexican demand competitively; secondly, to enhance access to the North American market where it is feasible for Australia to establish manufacturing operations under NAFTA arrangements taking advantage of Mexico's privileged position and cost structure.

Some Australian companies have embarked on the process which will enable such advantages to be harvested and which must precede business success anywhere: learn and understand the market, establish and develop relationships of trust, find the common ground and the needs Australia can supply competitively. Those companies have

18 In its 2001 report on Investing in Latin American Growth.

understood that doing business in and with Mexico is not dissimilar to doing business elsewhere, and in many respects can be easier. The culture is amenable to enterprise; participation in NAFTA has brought about changes in the Mexican business and corporate governance to render it more akin to what we are familiar with; English is reasonably widespread in business circles. In brief, Australians who have made the journey have found a different and challenging business environment, but not one that is alien or forbidding. This practical guide to the Mexican market seeks to ease the journey of Australian companies willing to look beyond the horizon, to Mexico.

Bilateral agreements that have relevance to certain sectors of the Australian economy include:

- Trade and Investment Agreement – effective since 3 April 1997;
- Agreement on Scientific and Technological Cooperation – effective since 4 March 1982;
- Memorandum of Understanding on Breeder Cattle – signed May 1997;
- Memorandum of Understanding on Mining Cooperation – signed July 2002;
- Double Taxation Agreement – signed September 2002.

Under negotiation are:

- Investment Promotion and Protection Agreement[19];
- Memorandum of Understanding on Energy Cooperation;
- Agreement on Energy Cooperation.

Other agreements are:

- Treaty on Extradition – in force since 27 March 1991;
- Treaty on Mutual Legal Assistance in Criminal Matters – in force since 3 June 1992;
- Agreement on Cooperation in Peaceful Uses of Nuclear Energy and Transfer of Nuclear Material – in force since 17 July 1992.

19 Australia is currently involved in negotiations with Mexico on an Investment Promotion and Protection Agreement (IPPA). This is due to be concluded in October 2002. The IPPA will facilitate bilateral investment by providing a clear set of obligations on the promotion and protection of investments.

PART TWO Operating in the Market

Cultural Issues: Life and Business

Understanding Mexico's unique business culture, laws and sensitivities takes time. Doing business in Mexico is different – not more difficult – and what is different and most challenging relates to intangible qualities of character and the backdrop of culture.

Mexico's **cultural heritage** is a rich and diverse mixture of native American, Spanish and North American influences, with wide regional variations. Fierce regional loyalties prevail, with strong *mestizo* influences created from descendants of the native Aztec, Maya and Toltec civilisations mingling with the Spanish. To better understand the culture, there is no substitute for travelling widely in the country.

Language provides access to the culture, and any effort to learn the language will be rewarded not only with better understanding, but also by Mexican partners appreciating the effort. While it is useful for travelling, it is almost essential to make the most of living and doing business in Mexico.

Loyalties – Mexicans are intensely nationalist and emotionally attached to their home town or region. It would be a mistake to assume that the capability to do business in other parts of Latin America translates directly into success in Mexico.

Foreigners have been the cause of a lot of trouble in Mexico's past and therefore the attitude towards them is mixed. However, as Mexico has become more open, there is great interest in what foreigners have to offer.

Personal relationships are vital. They often determine the choices made in business, rather than the more advantageous deal or the better-quality product or service.

While this is changing, the intent behind it is worth remembering. Mutual trust and respect grow with time and are more valuable than a passing opportunity. Business is strictly done between friends, and fortunately Mexicans are a gregarious and friendly lot, so it does not take long to make friends and to build up *confianza* – mutual trust. Starting with business breakfasts and luncheons, the process of getting to know each other will move to evening outings and to meals with the family.

Respect for a person, and the sensitivity needed to assess quickly how that person's authority or status could be affected by a particular course of action, is central to business relationships. Even an obviously unintended or presumably insignificant slight can have unwanted and lasting consequences. **Status** is integral to respect, so the kinds of clothes worn and cars driven are seen as a sign of status and contribute to respect. The proper title or form of address is of great importance. Mexicans tend to address each other by their professional title: *Licenciado* (holder of a university degree, or lawyer); *Ingeniero* (engineer); *Arquitecto* (architect); *Doctor* (Ph.D. or medical doctor). When in doubt, call a business colleague *Licenciado*, or *Licenciada* for a woman.

Like other Spanish-speaking peoples, Mexicans use two surnames (e.g. Vicente Fox Quesada: 'Fox' is his father's surname; 'Quesada' is his mother's). They are often addressed by the 'first last name' only – e.g. Presidente Fox.

The overwhelming majority of the population professes to the Roman Catholic faith, in spite of the strong Mexican tradition of anticlericalism. **Religion** may not be overtly visible in the workplace, but the values which lie at the heart of the faith inevitably have molded societal attitudes. Amongst these are a fatalistic view of both success and failure as being outside an individual's control.

This also supports the predominantly authoritarian structures and centralised decision-making common to Mexican **business management**. Hierarchies are well defined with little authority given to lower ranks and all decisions taken at the peak management levels. If the decision-maker is not there, the decision is not taken, as devolution of responsibility and decision-making is rare. This can create delays in responding to even urgent matters. Mexicans are not overly fond of joint ventures as they have difficulty in relinquishing control.

The extent of **formality** in the conduct of business can depend on the industry concerned. In some cases large business deals will be agreed even without a contract, where trust exists and the nature of the industry is such as to make it difficult for any of the parties to escape the commitment they have entered into. In other circumstances even the smallest transaction can be subject to much red tape. However, concluding large deals without proper contractual arrangements is not recommended.

Mexicans tend towards being guarded. It will not be unusual for even a large company not to have a business plan, as such plans would reveal too much. If a business plan exists, it will not surface in the early stages of exploring a possible venture or partnership. More important is the process of getting to know each other.

Women in the workplace are a relatively new phenomenon, resulting from a change in attitude and the dramatic increase in the number of women with higher education. Many companies now accept women for key positions, but this is likely to be in larger and more progressive enterprises. The ease with which foreign women can operate in this environment will depend on how they approach the occasional hurdle, such as not being taken as seriously as their male counterparts. Persistence, determination and achieving results tend to overcome gender-related misconceptions.

Mexicans work hard. The priority, however, is not work, but family and leisure. **Punctuality** is not generally a Mexican virtue, and yet it is advisable to be punctual while not expecting it in return. Take along this book for something to read. If in Australia four or five meetings are possible in a day, scheduling more than two or three a day in Mexico may be optimistic. Everything takes longer than expected, but it is not good form to look at the watch.

Dealing with the Mexican **bureaucracy** is time consuming and sometimes frustrating. Permits are required for many activities and these take time to acquire. People are protective of their administrative procedures, and this can occur in companies as well as government agencies. Nevertheless, in the past decade there have been dramatic improvements through deregulation, and further changes are planned, including greater access to government through internet services.

Excessive bureaucracy can contribute to **corruption**, as the attraction of circumventing procedure is heightened by urgency, and the helpfulness of decision-makers. Taking a strong and vocal anti-corruption stance as a business leader is often effective in influencing behaviour in the home organisation. Eliminating corruption is a high priority for government, and the case of a former President's brother accused of "illicit enrichment" is seen as a landmark, a precedent and a deterrent.

The problem, and it is a diminishing problem, is how an Australian company should deal with situations where it is clear that certain "incentives" are expected in order to resolve a problem, secure a permit, or obtain a license. In general Australian companies operate in foreign markets in accordance with the ethics and codes of conduct required of them domestically and are not necessarily used to confronting such situations. It is important for it to be known that Australian companies will not engage in unlawful behaviour in order to secure contracts or other benefits.

Having said that, there are occasionally local customs relating to **gifts and gratuities** which may be an inherent part of moving things along. These are of a minor nature and, more often than not, are perceived as being built into an employee's remuneration structure. It may, for instance, consist of a gift at Christmas time or at another appropriate local occasion. In these circumstances a company's local agent will probably include any such events in the day-to-day expenses billed to the company, and it would be reasonable to regard it as a valid business expense.

While in the Anglo-Saxon ethic **nepotism** is generally frowned upon, in Mexico it is an accepted part of business. It is a cultural phenomenon related to the importance of relationships (including within a family) and the need to have in place people of trust. Not only may a business owner's son work in a responsible position in the company, but a number of other relatives and those of senior employees may be populating key points in the hierarchy.

Australian business, well-versed in Asian ways, will discover that negotiation in Mexico has an unexpected familiarity and twist: "Yes can mean no, and no can mean maybe".

And if the former is the case, the practice of *dar largas*, or procrastination, may be adopted by the party who had meant to say "no". The difficulty is deciding whether further pushing and negotiating could bring results, or whether the deal is dead. What lies at the heart of this ambiguity is that it is regarded as impolite to verbally disappoint – to say "no". This habit can have unexpected results: it can happen that a sit-down dinner party will only have half the guests turning up – in spite of assurances from all that they will be there.

As a result of their gregariousness and their national pride, there will be continuous sharing of sights, history, culture and **food**. Mexican cuisine is considerably more diverse and subtle compared to what, with few exceptions, passes for Mexican food outside the country. Sharing food is sharing culture, and often business is done during breakfast or lunch. The bill at a restaurant is normally picked up by the person who invites the others: the meaning of the words "invite for lunch" are synonymous with "let me buy you lunch".

Other business habits worth remembering are:

- Shaking hands is common on introduction and every meeting. Close friends of opposite gender exchange cheek kisses, while close male friends embrace and shake hands. There are variations in this theme, and after a while the nuances become clearer.
- Telephones are for making arrangements, having a chat and confirming appointments. They are not for closing deals. Faxes are used for that purpose. It is useful to remember that spoken words are not worth the paper they're not written on. E-mails are gaining ground, but are still far from being widely used.

Keeping the following in mind may prove useful:

- Check the local as well as national holidays before planning a business trip.
- Many Mexican companies close for the comida (lunch), usually between the hours of 2–4 p.m. It is best to check working hours when planning your schedule.
- Videos need to be in NTSC format.
- Never drink the tap water; bottled water is readily available throughout Mexico.
- Do not eat uncooked food, unless it has an outer skin, for instance, banana, orange, avocado.
- Most Mexican cities are at a high altitude. It is best, on arrival, to allow a day and a night for the body to adjust to the change in altitude, by resting and taking gentle exercise.
- Beware of drinking too much alcohol at a high altitude!

Security is an important consideration for tourists and expatriates living in Mexico. Precautions are the order of the day. Muggings and car-jackings are a feature of the major cities and in the vicinity of the US border. A Mexico City newspaper reported that in the space of two years one in seven residents claimed to have been a victim of personal security crime. Fortunately, foreigners are not prime targets, and common sense quickly reduces risks. Kidnappings occur, but again foreigners generally are not targets (unlike Colombia).

Identifying the Best Strategy and Local Partner

Some basic strategic decisions lie at the beginning of an engagement in the Mexican market. In this respect the issues are similar to those which are relevant to any business engagement. Some companies will wish to set up in Mexico simply to use the free trade access to the world's largest market from a lower-cost manufacturing base, with sales to Mexico itself as a subsidiary strategy. Others see the Mexican market as a good adjunct to their operations in the US, while others again may wish to develop Mexico as an export market for their goods and services.

The starting point in a business engagement, assuming the strategy is sound, is to identify the local partner who will make the business work for you. That partnership is likely to require research and due diligence in the following quarters:

- The Austrade office in the Australian Embassy in Mexico City is equipped to identify and assist in the background checks of potential partners and in the selection of agents and distributors.
- A number of well connected and reputable local legal firms can suggest linkages, carry out checks and all the legal work associated with establishing a commercial presence. The Austrade office will have a list of reputable law firms which, in turn, can recommend partners, accountants and virtually any other local contacts including relocation specialists.
- The industrial/commercial associations relevant to the particular sector for the company, including Chambers of Commerce, can provide useful contacts. The business association which links up Australia, New Zealand and Mexico (ACANZMEX) is situated at the Australian Embassy.
- Bancomext, the Mexican Export Bank, can assist with foreign investment or import enquiries, but will not assist the Australian exporter.

- COMCE, the Mexican Foreign Trade Council, will assist any business venture between the two countries and is well equipped to do so.
- The Australia Latin America Business Council (ALABC) can assist companies in Australia with doing business in Mexico.

Contact details for all these organisations are in the Appendix.

Exporting to Mexico

As part of its restructuring program, Mexico has dramatically improved the transparency and efficiency of its customs administration and its customs procedures. Its **import classification system** has been modified to match that of most industrialised countries, which goes under the name of the Harmonised System for Merchandise Classification and Codification. In addition, Mexico applies the WTO-approved valuation rules for what constitutes normal price levels, and has dramatically reduced the number of products requiring import permits.

Import authorisations may be required from relevant ministries for reasons of health, safety, environmental impact, and national security (see *The Mexican Bureaucracy*, page 19). The Ministry of Health will want to issue an import authorisation or notice *(aviso)* for food items, medicines, and medical instruments. The Ministry of Agriculture (SAGARPA) will want to authorise imports of animals and plant material. The Ministry of the Environment and Natural Resources (SEMARNAT) will want to do the same for animal and forestry products. The Ministry of Defence (SEDENA) likes to be involved in authorising firearms and explosives. When it comes to chemicals, the Intersectoral Commission on the Processing and Use of Pesticides, Fertilizers, and Toxic Substances (CICOPLAFEST) may have the odd thing or two to say. Just to make things interesting, there may be overlapping responsibilities in the case of some products (check the websites listed on pages 74-75).

There is a list of restricted products[20] which needs to be checked, because there may be some surprises amongst the more obvious prohibitions (e.g. restrictions on guns, agricultural commodities, automobiles, heavy construction equipment and some textiles may be expected, but not so for used computers, peripherals and printers and some used car parts).

There has also been dramatic change in **Mexico's tariff regime**: when in the past tariff rates could reach highs of 100 per cent, these can now be 3, 5, 8, 10, 13, 14, 18, 20, 23, 25, 28 and 35 per cent with certain items duty free, and the change continues[21]. The average weighted tariff runs at approximately 11 per cent. For a range of products Australian suppliers are at a disadvantage due to Mexico's free trade agreements with the large trading blocs, but it may be that specific tariffs are destined to be phased down or out, or that their effect is negligible. In May 2002 Australia's Minister for Trade secured Mexico's agreement to remove a three per cent tariff on a range of import products, including coal, wool and live cattle and sheep. The tariff, which had been in place since 1999, is expected to be removed shortly.

Most duties are based on FOB or CIF value or at specific rates, whichever is the greater. A 15 per cent value-added tax is payable on the duty-paid price of most imports (staple goods and medicines excepted). Products such as alcoholic beverages and tobacco are subject to a special tax on production and services (IEPS).

20 From the Ministry of the Economy www.secofi.gob.mx
21 More permit and tariff details (in Spanish) on www.economia.gob.mx/?P=955

Mexico's requirements on standards, certification and labeling will require attention fairly early in an exporting strategy. Called **Mandatory Mexican Standards** with the Spanish acronym of **NOMS**, these must be certified as applying to the products, processes, emblems, services and methods which are imported, sold, used or processed in Mexico. Here, too, the move is towards internationally accepted norms such as ISO/IEC, but testing for the issuing of a certificate has to occur at laboratories accredited by Mexico. Since none in Australia have this accreditation, this needs to happen in Mexico and a list of such laboratories is published on the website of the Ministry for the Economy, which also issues the certificate of compliance. This certificate will be of particular significance to the customs official at the port of entry.

The NOMS also determine the labeling requirements for a product. The information on the label (in Spanish) generally includes a product description, net weight, usage and safety instructions, name and contact information of both the importer and producer, and country of origin.

The Export Finance and Insurance Corporation (EFIC) provides short-term cover for Mexico, with demand from exporters being mostly on the basis of open account or documents against acceptance. At the time of publication, EFIC has Mexico rated with a Market Grade 3 (1 = low risk, 6 = high risk), putting it on a par with China, Thailand and India. What keeps Mexico in this classification is EFIC's assessment of high local interest rates, tight liquidity and the dependence of Mexican companies on the US market. Buyers with a turnover of US$25 million or less are carefully scrutinised due to problems accessing bank credit at reasonable rates.

The Paperwork

The challenge of Mexican paperwork is best taken up by a customs broker. In fact, to use a customs broker is a legal requirement for permanent imports if the shipment is worth more than US$1 million. Even with a shipment a small fraction of that value, such local experts are indispensable. What they will need from Australian exporters is a suite of six documents, as listed below.

Export Documentation

1 Commercial invoice – it needs to be in Spanish or have a Spanish translation attached (signed by the seller, consignee or customs broker) and there need to be five copies. Included in the information on the invoice must be:

- place and date of issue
- port and date of shipment
- name of ship
- Mexican port of entry and date
- name and address of consignee
- marks
- number and kind of packages
- quantity of items
- country of origin
- detailed description of goods, including all marks, numbers etc engraved by the factory

– itemised current domestic value of each type of goods and total value (FOB and itemising all charges up to CIF).

The valuation must include the exporter's signed declaration with the following words: *Declaramos bajo protesta de decir verdad que los valores y especificaciones aquí descritos son ciertos y coinciden con los del mercado local*, which translates to " We declare, under oath, that the values and specifications described herein are true and coincide with those in the local market".

The copies of the invoice need to reach the consignee before the goods arrive in Mexico, otherwise heavy fines are imposed.

2 Certificate of Origin – exporter-issued, it must be presented with the shipment at the point of entry, so that any preferential tariff treatment can be applied (and to avoid payment for compensatory quotas).

3 Bill of Lading – as in normal commercial practice, a bill of lading must be issued by the exporter. "To Order" is in order and should show names, contact numbers etc of the Mexican customs broker and freight forwarder.

4 Free Sales Certificate – this is a document from the country of origin that declares that the product requires no special permit and is free to be sold in that country. Fortunately this applies only to some products (ask the customs broker) and is needed at the point of customs clearance.

5 Certificate of Insurance – nothing unusual.

6 Packing list – the information required, matching that given in the commercial invoice, needs to include the exact description of the product, value, weight and volume.

Accessing the Market

Mexican law allows for a variety of vehicles by which foreign companies can get their products and services to the Mexican customer. And just as in any other market, each arrangement has its advantages and disadvantages. It is worth doing a lot of listening, both to business people who have already been through the exercise and to local allies, before deciding on a strategy.

Direct sales have an immediate appeal, as they provide maximum control over revenue, the product, the rate of progress and information on the needs of customers. Large one-off shipments or regular sales to a small group of customers are most likely to lend themselves to direct market promotion, including via internet. There is also another advantage: Mexicans prefer to deal personally with the foreign supplier.

Representation in Mexico provides the kind of footprint in the market that adds significantly to all aspects of doing business there: better local knowledge, better acceptance within the market, better capability in dealing with unexpected problems and better responsiveness to market needs. This will add to costs, but is also more likely to add to business volume over a longer time period. It can be achieved by establishing a **representative office**, which can conduct research and market promotions but cannot conduct business or generate income. The tricky bit is to avoid doing something that might be regarded by the Mexican authorities as having established a legal entity permanently in Mexico, and therefore becoming subject to Mexican income tax.

For some specialised services or for sales to large customers, such as governments or the large monopolistic concerns, an **agency agreement** may be a preferred option. It can also be an effective way of reaching smaller cities and remoter locations. Depending on the agreement, the agent usually has no primary responsibility for the product and any risks regarding product liability, transactions, third parties or guarantees, as the agent is only acting on behalf of the foreign supplier. That responsibility remains with the supplier. The advantage is that any costs associated with the agency are fixed, normally as a fixed commission or as a percentage of the value of sales made. There is a potentially tricky wrinkle to this: the agency agreement may confer upon the agent the status of an employee under Mexican labour law and the foreign company may be required to fulfil all obligations due to employees under that law. It has to be made clear that the agent is a contractor, not an employee.

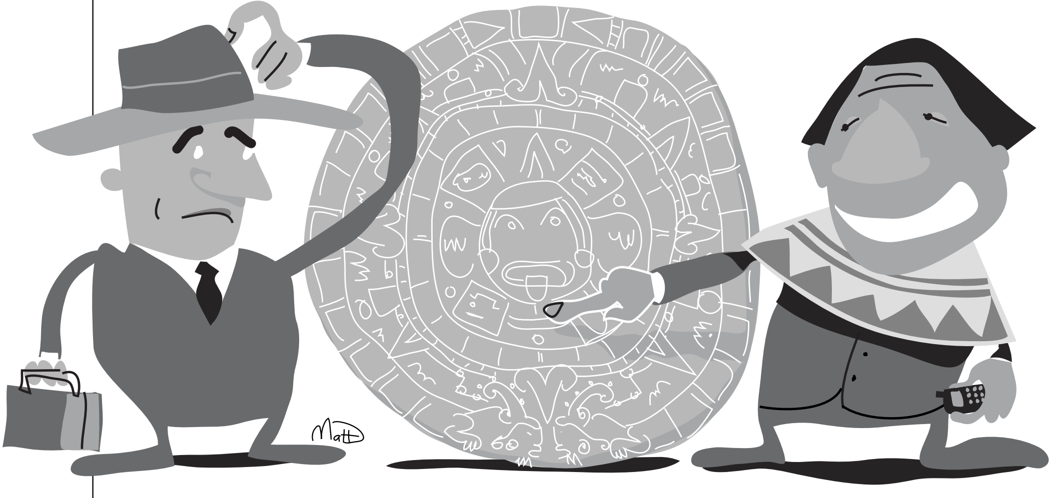
The more arms-length arrangement is through an agreement with a **distributor**, more suitable to, for example, consumer goods, computers and car parts, where there is a warehousing and regular servicing requirement. In this agreement the distributor in effect becomes the foreign company's customer, buying product and on-selling with a mark-up. The positives are that any losses, merchandise damage or customer claims are the responsibility of the distributor, and that there can be no mistake about employment relationships. But the foreign supplier also becomes no more than a seller, with no legal control over marketing or distribution and will find that the reputation of the product is only as good as that of the distributor. A good understanding between the two business entities involved in a distribution agreement can make this all a little more flexible: the passage of time, a mutual track record of looking after each other and frequent personal contact will do much to lubricate the cooperative effort.

In either an agency or distribution arrangement it should be remembered that Mexican companies, particularly the small and medium-sized variety, have very limited access to financing. This means that marketing and advertising budgets become much more rubbery and the timing of payments for goods also a little flexible. However, much can be achieved in marketing through distributors and agents, if training and technical support is top quality.

As the commitment to the Mexican market increases, so does the involvement and the length of the strategy's time-frame. Some businesses are best conducted as a **franchise**, and Mexican law provides for this. The definition of a franchise is when the license to use a trademark is accompanied by the transfer of technical knowledge and assistance to sell a product and/or service uniformly and under tight quality control to maintain the image of that trademark. The franchise agreement has to be registered with the Mexican Institute of Industrial Property as though it were a trademark, but it does not require government approval. As elsewhere, franchises have enjoyed rapid growth in Mexico, with foreign franchises making up 40 per cent of the 450 operating in 2001. Service sector franchises make up 24 per cent of the market and include advertising, financial consulting, printing, training and automotive services. Since there is full contractual freedom in setting up franchises, the franchisor can include the usual precautionary clauses in the contract to ensure against pitfalls after the conclusion of the agreement (such as the erstwhile partner setting up in competition). Australian franchises in Mexico have become a more feasible option with the introduction of a double-taxation agreement, signed in September 2002 as this ensures better withholding tax treatment.

Greater permanence of company presence is ensured through the establishment of a **branch** office, which allows engagement in business activities and therefore the privilege of paying taxes on par with a local entity. The motive for taking this step has to be an internal matter for the parent entity, as this arrangement normally allows for better coordination, communications and accounting. There are no real tax advantages, although obviously Mexican expenses are deductible from Mexican earnings (except for payments to the parent), but since a branch is a part of the parent legal entity, the parent is also liable for the branch's obligations.

Not so in the case of a **subsidiary** company, which is an independent legal entity and separate from the parent company. Such incorporation requires a much larger capital outlay, but also has a higher potential for profits (or losses). In legal terms it is considered a Mexican entity and will be treated as such. The form that such a company might take could be the most common, the *sociedad anónima* (limited liability company). There are other varieties available, which are tabulated under Legal Issues (page 36).



"The regulations on foodstuffs start here..."

It is important to remember that the bureaucratic process for establishing a Mexican business can be quite involved and, if discontinued, can involve substantial fines. Advice from Mexican accounting and law firms will ensure that the right choices are made and that the processes run smoothly and correctly.

AN AUSTRALIAN-MEXICAN JOINT VENTURE

Gulf Rubber Mexico SA de CV (GRMex) manufactures pipe sealing gaskets for PVC and Ductile iron pipe primarily for export to the US, Canada, and Central and Latin America and for Mexico itself. These are high quality, high specification products and are produced in a range of polymers.

GRMex is a joint venture between the Australian company Gulf Rubber (GR) and its Mexican partner, Mexico SAO de CV, which commenced production in August 1998. The company is ISO 9000 accredited and was established with new manufacturing equipment plus a fully equipped tool room. It employs two expatriate Australian managers, both of whom speak Spanish, and has a total workforce of 90 operating three shifts, six days a week.

For some years GR had tried to build its market share in the US, supplying the pipe seals from its Malaysian plant, but could not meet the response time of its competitors which led to the strategic decision to move GR's manufacturing base to North America. Mexico was the obvious choice, given its NAFTA status, proximity to the prime market, Pitex benefits (GRMex is Pitex registered, see "Mexico as a Base"), lower labour costs, and reasonably good infrastructure.

The first step GR took, based on experience in Southeast Asia, was to identify a local partner. This took six months and in the end also influenced the location of the plant. The US/Mexico border area was discounted on advice from the Mexican National Chamber of Industries (CANACINTRA), that the workforce was more transient and labour costs higher closer to the border. It was essential for GRMex to train and retain its employees and this had to be weighed against a higher freight cost into the US. A suitable partner was eventually identified in the city of Leon following an exhaustive search from North to South including Monterrey, Chihuahua and Mexico City.

GR attributes the success of its operation in Mexico to the decision to establish a joint venture, and to the investment of time and resources in the selection of the best possible partner it could find. According to GR's CEO, Rob Emerson, "the business culture and environment in Mexico are very different from that which prevails in Australia and New Zealand. Distance and communications are also a major difficulty without a local partner". Even though two expatriate managers (an Australian and a New Zealander) were sent to Mexico to establish the plant and train the workforce, it would have been extremely difficult, if not impossible, to adapt to the Mexican culture without the guidance of the Mexican partner. Emerson adds: "Given that Gulf Rubber Group is a single shareholder private company with global sales around A$40 million per annum it does not have unlimited resources in terms of HR and finance. Mexico represents a large investment for the company and it could not afford to fail. The success of the venture is inconceivable without the outstanding contribution from José Luis Díaz, our local partner."

Among some of the challenges identified by GR in operating in Mexico are the following:

- Retaining a well-trained workforce at a competitive cost. Wages and on-costs are significantly higher than most of Southeast Asia and China and the work ethic a little more "laid back". Well-trained tradespeople, such as toolmakers, are in short supply, but the Government is making a considerable effort to address this problem. Emerson says, however, that "the quality of middle management personnel is a positive factor and there is a good supply of reasonably young (mid to late 20's) English speaking people available. Employees at all levels are very keen on both internal and external training programs".
- Dealing with government agencies. Local expertise in dealing with government instrumentalities is essential. The regulatory compliance burden seems large at first, but is probably no more than would be experienced in Australia, just different. In the area of exporting product and importing manufacturing materials, machinery and equipment, regulatory compliance can be a minefield, especially the paperwork involved in recovering tariffs and taxes already paid. The government was helpful in facilitating the entry of expatriate personnel.
- Financing from local banks is very restricted compared to GR's experience in Australia and New Zealand, Malaysia and the US. None of the banks appear to be interested in export or trade finance. Financial security requirements appear to be based on "bricks and mortar", which foreign companies would not normally possess in Mexico.

Emerson believes that GR would make the choice to establish in Mexico again, but would allow a longer time-frame in the feasibility study to achieve production efficiency and performance targets. He also would not locate the plant in the same site as the partner's established manufacturing facilities. Despite the benefits of being on the same site, there were a number of complications arising from a small multinational operation manufacturing alongside a pure Mexican operation with five times the number of employees.

Investment Issues

Some businesses are keen to develop Mexico as an export market for their goods and services, others see the Mexican market as a good adjunct to their operations in the US and some companies have set up in Mexico to use the free trade access to the world's largest market from a lower-cost manufacturing base. If setting up operations in Mexico involves an investment, the venture will be subject to the Foreign Investment Law (FIL), which sets out the rules governing the engagement of foreign entities, including proportion of ownership.

Introduced to coincide with the commencement of NAFTA, the FIL in its current form has substantially deregulated foreign investment restrictions to the point where foreign investors can hold 100 per cent of the capital of any Mexican company or partnership, except in a few areas expressly mentioned in the law's regulations. For the purposes of the FIL, a foreign investment exists when foreign investors hold any equity in a Mexican company, or when all the shareholders are Mexican companies, but foreign capital holds a majority interest in any of these shareholders.

There are three groups of regulated activities that have varying levels of restriction. Starting with the most restrictive, which were expressly exempted from NAFTA, the following key activities are reserved for the **Mexican State**:

- oil production and oil refining,
- basic petrochemical production,
- sale of electricity to the public,
- nuclear power,
- satellite communications,
- local postal service (excluding courier),
- bill issuance and coin minting,
- control, supervision and surveillance of ports, airports and heliports.

Originally reserved for **Mexican investors** only were:

- domestic ground transport,
- retail petrol sales, distribution of LPG,
- radio and television broadcasting (free-to-air),
- credit unions and development banks,
- professional and technical services, as determined by other laws.

Since the beginning of 2001 the shares of Mexican companies operating in these areas of activity can be 51 per cent foreign owned, and from the beginning of 2004 this will move up to 100 per cent.

Some activities have **percentage restrictions** for foreign participation, including:

- cooperative production companies (10 per cent),
- domestic and specialised air transportation and shuttle services (25 per cent),
- the 49 per cent limit to foreign ownership applies to
  - a range of services, including insurance and bonding, currency exchange, leasing and factoring, special purpose financing, companies operating investment companies, etc.,
  - manufacture and commercialisation of explosives, firearms, ammunition and fireworks (their use in industrial or extractive activities is permitted),
  - printing and publishing of newspapers for circulation in Mexico,
  - series "T" shares in companies owning agricultural, cattle-raising or forestry land,
  - cable television and basic telephone services,
  - fishing (excl. aquaculture, which can be 100 per cent foreign-owned),
  - some coastal shipping and related services,
  - supply of fuel to ships, aircraft and railway locomotives.

National Foreign Investment Commission (NFIC) approval is necessary for foreign investors to hold more than 49 per cent of a Mexican company involved in the following:

- port services,
- international shipping,
- air terminal administration,
- private educational services,
- legal services,
- credit information companies,
- institutions for categorisation of securities,
- insurance agencies,
- mobile telephone services,
- oil and gas drilling.

Foreign ownership of any Mexican company which has assets valued at greater than 712 million pesos (approx. A$136 million) also requires NFIC approval.

There is another limit which has its origins in the Mexican Constitution, and that is the prohibition on foreign ownership of real estate within 100 kilometres of the national borders, and within 50 kilometres of the coast. The FIL allows, however, for foreign participation in a Mexican company, which owns real estate for non-residential purposes, as long as the Ministry of Foreign Affairs is notified. If the land is for residential purposes, then additionally the title of the real estate must be held through a trust operated by a Mexican bank.

Legal Issues

Coupled with Mexico's market-oriented restructuring has been the change in the country's legal environment: laws and regulations have been simplified, the courts' operations overhauled and practices aligned more closely with international standards. Consequently, doing business in Mexico has become easier in a legal sense and some of the basic features of laws, governing the types of business entities, labour, bankruptcy, intellectual property, dispute resolution and competition, are essential background information. It is vitally important to obtain legal advice in drawing up contracts, especially regarding mutual expectations and obligations, and settlement of disputes (arbitration).

Establishing a business

It is possible for foreigners to conduct business in Mexico as representatives of foreign-based firms. The use of the FM3 visa for business allows unlimited trips into and out of Mexico for one year, and it can be renewed four times for a total of five years' access. Eventually this can become problematic, particularly if more than 183 days in a year are spent in Mexico and the frequent visitor meets the definition of a resident for taxation purposes. Perhaps before then it may be necessary to open a Mexican business.

Mexican commercial law provides for a wide range of business structures, as listed in the tabulation. As anywhere, the type of business entity will be determined by the individual concerns and circumstances of the venture being contemplated, where taxation matters, expected time to profitability and management control all play a part. The process for incorporation in Mexico is described in the box.

Type of Business Entity	Features
Sociedad Anónima (SA) Limited liability corporation with fixed capital	• minimum of two shareholders • minimum capital of 50,000 pesos • 20% of capital in advance, if shareholder contribution is in cash • 100% paid up upon incorporation, if shareholder contributions are in kind (equipment or property) • shares are freely transferable and tradable • shareholders' liability is limited to stake. • changes in capital require authorisation[22]
Sociedad Anónima de Capital Variable (SA de CV) Limited liability corporation with variable capital	• most popular among foreign investors • features similar to above, except changes in capital can be approved internally
Sociedad de Responsibilidad Limitada (S de RL) Limited liability partnership	• popular form • at least two individuals or entities • minimum capital of 3,000 pesos • no share certificates • transfer of ownership interests (participaciones) legally restricted • liability is limited to the partnership interest
Sociedad en Nombre Colectivo (S en NC) General partnership	• unlimited liability toward third parties • partners have joint liability • minimal formalities • mostly used by Mexicans
Sociedad en Comandita (S en C) Partnership of limited and general investors	• used by investors offering professional services, eg. lawyers and accountants • general partners have joint liability • limited partners are liable according to capital contributions

22 From the Ministry of Foreign Relations (Secretaría de Relaciones Exteriores: SRE) and sometimes the National Foreign Investment Commission (Comisión Nacional de Inversión Extranjera: NFIC).

Type of Business Entity	**Features**
Sociedad Civil (SC) civil partnership	• used only for non-commercial enterprises (eg. non-profit)
Asociación en participación (AP) Joint venture agreement	• often used by foreign investors, particularly small and medium-sized companies. • not a legal entity, but a contract • asociante (managing venturer, normally local partner) liable to 3rd parties • asociados (silent venturer, normally foreign partner) has limited liability

STEPS TO INCORPORATION IN MEXICO

The following are obligatory federal business formalities for forming a company in Mexico. Additional sector-specific requirements may apply:

1. Request authorisation from the National Foreign Investment Commission (CNIE) where applicable. Maximum response time: 45 working days.
2. Apply for incorporation permit from the Ministry of Foreign Relations (SRE): This step is applicable to all companies, both Mexican and foreign-owned. Applicants must submit three possible corporate names. Maximum response time: 5 working days.
3. Apply for federal taxpayer registration number with the Ministry of Finance. Also submit a letter indicating that the permit granted by the Ministry of Foreign Relations is being used. Response time: immediate.
4. Companies with any foreign participation must register with the National Foreign Investment Registry within 40 days of starting business activity.
5. Submit annual statistical information to the Institute of Geography and Statistics (INEGI). INEGI has 30 days to verify the submitted information.
6. Register the company's safety and health committee with the Ministry of Labour and Social Welfare (STPS) within 30 days of initiating business operations.
7. Submit employee training program to STPS within 15 days of signing collective work contract with employees, or within 60 days if no collective contract is required.
8. Create company's supervisory committee for the internal training program.
9. Register the business and all employees with the Mexican Social Security Institute (IMSS). In addition to SRE and, where required, NFIC approval, the following will affect the speed of incorporation:
   - **a** drafting the company's by-laws (charter);
   - **b** getting an appointment with a local Notary Public for signing the incorporation deed;
   - **c** execution of the special powers of attorney to incorporate (if any).

Labour Laws

Heaven for an employee could be Swiss wages with Mexican labour laws. The Federal Labour Law of 1970 (LFT) favours employees in its intent. In its effect it often does the opposite. Companies need to be fully aware of the hefty obligations they take on when entering into an employment agreement. Any person working at the instruction of another is regarded as an employee. There is a long list of mandatory entitlements, and the guidelines for termination of employment are lengthy and potentially costly. There is collective bargaining, industry-binding contracts *(contratos-ley)*, obligatory union memberships *(cláusula de exclusión)*, mandatory profit sharing, limits on temporary and apprenticeship contracts, rules on seniority-based promotion, firm-provided training programs which have to be registered and an indirect liability for subcontractors' employees *(patrón indirecto)*. As a result about half the workforce stays in the informal labor market, and of these about half do so involuntarily, with the result that foreign investors pass the cost on to workers through lower wages. These extra costs have been calculated at about 31 per cent of the payroll.

The following employment conditions and benefits are the minimum requirements:

- **Maximum Hours, Overtime Pay:** the working week has a maximum of 48 hours divided into eight-hour shifts (day) and seven-hour night shifts. The first nine hours of overtime attract double pay and triple pay thereafter. Management ("Employees of confidence") does not receive overtime pay.
- **Paid holidays:** Nine official public holidays per year. Additional holidays may be part of labour contract negotiations. Work on holidays attracts a holiday premium.
- **Paid Leave/Leave Premium:** After one year of service, employees receive a minimum of six days of paid leave, increasing by two days for each of the next three years of service. Thereafter two additional days per five years of additional service. During paid leave employees are entitled to 125 % of their salary.
- **Christmas Bonus:** Employees are entitled to an annual bonus of not less than 15 days' pay on or before 20 December.
- **Paid Maternity Leave:** Women are entitled to 12 weeks paid maternity leave, after which employers must make the old position available, and pay accrued benefits.
- **Mandatory Profit Sharing:** Businesses are required to distribute 10% of their taxable income to their employees.
- **Employer Housing Contribution:** Employers contribute an amount equal to five per cent of payroll to the national housing fund (INFONAVIT).
- **Social Security:** All employers must register themselves and their employees with the Social Security Institute (IMSS). Employers contribute 17.7% of the amount of each employee's salary, while employees above the minimum wage, which varies by region, contribute 5.25 per cent (capped at 25%).
- **Pension Fund:** Employers are required to contribute 2% of employees' salaries to the Retirement Savings System (SAR).
- **Training:** All businesses are required to have a staff training program, approved by the federal government. An in-house training committee, with labor and management representatives to oversee its implementation must be established.
- **Security and Health:** A security and health committee to address work-related illnesses and accidents has to be established.

It is almost more important for an employer to understand the laws applying to severing the employment relationship than it is to understand the obligations while it is ongoing. According to the LFT, an employer can terminate the employment relationship without liability on a number of justifiable grounds, including for dishonesty, disclosure of trade secrets, mistreatment of the employer and the like. But ending the relationship without these causes draws severance pay equal to three months' salary, plus 20 days' salary for every year of service. Employees of more than 15 years' service are entitled to a seniority payment of 12 days' salary per year of service, even if the departure is voluntary. A severance package is preferable to a lengthy court dispute, since a failure to show just cause by the employer can mean at least an additional liability for back wages to cover the time between dismissal and judgment.

Real employee costs run at between 37 and 100 per cent above the nominal rate of salary; this is still advantageous, particularly for unskilled employees, in comparison to rates in the US.

When establishing a company of any size in Mexico, it is important to consult a specific labour law specialist, usually attached to large and reputable law firms.

Unions

The right to unionise is constitutionally enshrined. Improvements of working conditions above the legal minimum were the main reason for union membership, so unless companies are active in areas of a strong historical union tradition or there are problems in personnel policies, there will be little interest in unionisation. Unions tend to work with management, often assisting companies by performing administrative chores.

It is compulsory for the business to enter into a contract with a union. If it has not done so it is legal for any union to call a strike in the workplace. A number of "*sindicatos blancos*" have emerged. These are "friends of the company", tame unions who will help the company meet its legal obligations in this area. In exchange for a fee, of course.

Intellectual Property Rights

The reform of the Mexican treatment of intellectual property rights occurred with three noteworthy actions:

1. adjustment of the Mexican Property Law *(Ley de Propiedad Industrial)* in 1994 to comply with the NAFTA patent and trademark requirements;
2. creation in 1994 of the Mexican Institute of Industrial Property (*Instituto Mexicano de la Propiedad Industrial* or IMPI) to administer and protect property rights;
3. introduction of a new copyright law (*Ley Federal del Derecho de Autor)* which extended the definition of copyrightable material.

But what is a law without enforcement? In 1998 the means were found to fund enforcement measures and an anti-piracy campaign, followed in 1999 by stricter penalties. Piracy is still a serious problem, and companies have a better chance of making their ownership stick in Mexico, if they register their trademarks, patents and copyrights in Mexico.

Dispute Resolution

Although much improved over recent years, the Mexican court system is still not the best place for resolving commercial disputes, as often the civil codes are not clear, court rulings are not published and they favour defendants through the use of delaying mechanisms.

Occasionally what is a civil matter elsewhere can be treated as a criminal matter in Mexico. Disputes are therefore better settled privately and informally. Alternate dispute resolution processes are available, but rarely used.

Bankruptcy Law

This is mentioned primarily as an example of a dramatic improvement in Mexico's commercial laws: in April 2000 two new laws governing corporate insolvency and the use of collateral in lending were enacted. The outdated bankruptcy act of 1943 has been described as the worst law Mexico has ever had. It promoted long, costly and complex court proceedings, which left creditors with few assets when a company was finally liquidated. It had encouraged debtors to transfer assets out of the reach of creditors, resulting in an understandable unwillingness by financial institutions to lend money. The new procedures, which employ government-appointed mediators and liquidators, allow for a year of negotiations between debtors and creditors, after which the court takes control of the company. A new government agency, the *Instituto Federal de Especialistas de Concursos Mercantiles* (IFE-COM) manages the increasing use of third-party professionals in bankruptcy procedures.

Competition Law

Efficiency comes before fairness – this is an unusual principle for a law, but it summarises Mexico's Federal Law of Economic Competition (*Ley Federal de Competencia Económica* or LFCE). Introduced in 1993 to address private anti-competitive behaviour and ensure competition in non-tradable sectors, the law also created the Federal Competition Commission (*Comisión Federal de Competencia* or CFC). Taken together, they make for what the OECD regards as one of the best systems anywhere. The law bans horizontal agreements (price fixing and market division), but allows vertical agreements (exclusive dealing and tied sales) as long as there is adequate horizontal competition. The CFC reviews all mergers, restructuring plans, privatisations, concessions and licenses for anti-competitive actions and has the power to block them.

How does that accord with state monopolies? They also get into trouble with the CFC if they overstep the limits of their monopoly, as the oil monopoly company Pemex discovered when its subsidiaries were pulled into line for engaging in discriminatory pricing and other anti-competitive behaviour. Changing laws, however, take some time to change attitudes, and in a traditionally protectionist country like Mexico this process continues.

Taxation Issues

There are no big surprises for Australian business in Mexico's taxation regime. It has been comprehensively revised to make it competitive with the taxation systems of Mexico's major trading and investment partners. Nevertheless, there is the occasional diversion and, when linked with complicated accounting procedures, it makes it essential that professional advice and guidance be sought in Mexico.

The basic structure of federal, state and local government taxes is a familiar one: the major ones are federal and include income tax, value added tax, a form of capital gains tax, import and export taxes. There are also social security premiums, mandatory retirement savings and contributions to the National Workers' Housing Fund, as well as payroll taxes. At the state and local level, all or some jurisdictions tax employers on salaries and professional fees paid, and levy rates on real estate and the equivalent of a stamp duty on real estate transfers.

Income tax (graduated, with a top rate of 35%) is imposed on the basis of residency and income source, whereby residency is established by living in the country for a total of more than 183 days in one calendar year. Residents are taxed on worldwide income, and all income generated by foreign residents with a base in Mexico is taxed. Such a base exists, if there is a branch, office, factory, mine or workshop, or an agent acts like one (e.g. signs contracts for the foreign entity). Earnings made in Mexico by anyone are also taxed, so if a technician from an overseas company is posted in Mexico for four months to work with the local distributor, then that income is taxable in Mexico. Withholding tax at varying rates is applied to remittances to foreign entities, dependant on the purpose of the remittance (ie interest payments, dividends, royalties, income).

Some of the characteristics of Mexico's major **federal taxes for companies** are listed below. They change with time, so confirmation of current details will be necessary.

Tax	Comments and Rates
Corporate Income	• assessed at federal level only • tax calculations are adjusted annually for inflation • capital gains are taxed as standard corporate income • income from sale of shares in a Mexican company taxed as income, regardless of where sale is made (non-resident companies selling stock traded on BVM pay 5% on gross or 20% on net gain) • companies engaged in agriculture, forestry, fishery and transport have 50% reduction of payable income tax • rate is 35%, reducing to 32% by 2005
Fixed and Financial Assets	• assessed on the average value of fixed and financial assets, starting with 3rd year of business operations • only paid if amount due exceeds the regular assessed corporate income tax • 1.8% on net assets
Dividends	• dividends to shareholders from the company's net after-tax account (CUFIN account) are not taxed • distribution tax (at income rate) on dividends from untaxed profits can be credited to income tax liabilities during following three years
Royalties	• taxed at income rate, if the technology or trademark is not patented • taxed at 10% rate if patented • technical assistance draws a withholding rate of 25%
Interest	• interest paid subject to variable withholding tax rates, depending on the company's business activity • 10% or 15% of gross

Tax	Comments and Rates
Value Added Tax	• 15% VAT on most goods and services purchased in Mexico • exporters are refunded the full amount paid • 15% VAT is assessed on imports, though exceptions apply • liability incurred on payment (ie. cash basis, not accrual)
Employee-related taxes	• Gross Payroll Tax: 3% on total compensation • IMSS (Social Security): 17.7%–22% of employees' salary • INFONAVIT (Housing): 5% of payroll • Pension Fund: 2% of salaries

In the 2002 tax changes, states have been permitted to tax the incomes of individuals in business and professional activity and to levy a maximum of three per cent sales tax on goods and services to the general public. Most states already collect payroll taxes at different rates and the states may waive these and real estate-based taxes as an incentive for investment.

Mexican income tax law allows for the effect of inflation on the depreciation of fixed assets, the cost on sales of fixed assets, the sale of shares, monetary gains and losses and on the carry-forward of tax losses.

Of some interest is the recent taxation change allowing investments in new equipment made by local entities in areas outside the big three cities to be written off in the year in which the equipment is brought into service.

Mexico has rules covering transfer pricing. Acceptable methods of transfer pricing include the comparable uncontrolled price method, the resale price method, and the cost-plus, profit split, residual profit-split and transactional net-margin methods. Mexican authorities are quite keen in their scrutiny, and it may be worthwhile to reach transfer-pricing agreements with the tax authorities in advance.

Mexico as a Base – the *Maquila* Program

A *maquiladora* is a Mexican company that operates under the *maquila* (in bond assembly plant) program approved by the *Mexican Secretaría de Economía* or SE, formerly the Ministry of Commerce and Industrial Development (SECOFI). The program allows the company to:

- be 100 per cent foreign-owned and managed, without special authorisation, and
- receive duty-free and value-added tax exemptions for the temporary import of goods and services intended for the manufacture of exports.

The maquila program has been a phenomenal success for Mexico and for the companies participating in it, although some of the shine has worn off in response to sluggish US demand and rising Mexican labour costs. In June 2002, according to the Economist Intelligence Unit, *maquila* output fell 9.6 per cent.

Maquiladoras are heavily concentrated near the US border, and in Mexico City, Guadalajara and Monterrey to the point where new facilities in the urban areas will no longer be approved. Land ownership by foreign interests is not permitted in restricted areas (see Investment issues), but leases are unrestricted in both duration and location. The process for incorporating a *maquiladora* takes about three weeks after approval by the Ministry of Foreign Relations (SRE), and further permits and registrations, depending on the kind of industry being proposed, take another 30 days.

The *maquiladoras* were originally intended and operated exclusively as export-oriented manufacturing facilities. All products and services from a *maquiladora* were to be either an input to another *maquiladora* or exporter, or a direct export. *Maquiladora* products and services could span the whole production process, such as a complete assembly operation using imported and local parts, or be confined to just one stage of the process, usually labour-intensive. The main flow of *maquiladora* products is into the US, although since 2001 sales have been allowed into the Mexican market, subject to the payment of import duties on imported components.

Since January 2001 tougher rules governing input imports have been enforced under NAFTA. Mexico has had to eliminate duty drawback programs that refund or waive import duties on materials from non-NAFTA countries used in the manufacture of exports to the US or Canada. How this affects Australian companies is that products sold to *maquiladoras* will be subject to import duties at the border, which can be paid and a refund requested when the product is exported, or the amount deposited in a bank and withdrawn when export occurs. The new rules also mean that *maquiladora* companies pay import duties on machinery and equipment when they are imported. VAT exemption continues for *maquiladora* imports. To partly counter the negative effects of these changes, Mexico has instituted 20 sectoral programs which cap import duties on inputs at five per cent, in accordance with “end use tariff provisions” in US and Canadian law. Businesses setting up *maquiladora* operations to service the NAFTA market should get US customs rulings on the intended export product. The tip is to keep a close eye on the rules of origin, as it is the percentage deemed to be from the source country that determines its treatment. Notwithstanding the benefits of participating in the *maquila* program, companies intending to do so need to seek advice on the latest legal and economic circumstances before going too far down this path.

PITEX

The less famous relative of the *maquila* program is the PITEX program, which allows ordinary Mexican companies with annual export sales greater than US$0.5 million, or more than ten per cent of total sales, to import products duty-free and VAT-exempt. If these products are machinery, equipment or tools, the exports must be at least 30 per cent of total sales. The four available PITEX programs work on the basis of:

- the total operations of the company,
- the operations of one plant,
- a specific export project, or
- a Sector Promotion Program *(Prosec)*. This mirrors the sectoral program introduced for the *maquiladora*.

Approval to participate in PITEX is given by the *Secretaría de Economia* (SE).

Both the *maquila* and PITEX programs are complex arrangements which are often caught between the conflicting demands of domestic economic development and of international obligations and agreements. The terminology can become complex and the rules even more so, but the rewards for having a go continue to draw companies into Mexico. The right local help can make all the difference.

CASE STUDY HOWE LEATHER AND THE MAKING OF A *MAQUILADORA*

An efficient manufacturing operation attracts attention. Sometimes that attention can become unwelcome. When Melbourne-based Howe Leather managed to establish itself as a competitive supplier to the US automotive industry, it attracted the attention of its US competitors, and embroiled the company in action before the WTO. The US claimed that Australian industry assistance provided to Howe Leather under Australia's textile, clothing and footwear and automotive industry plans were equivalent to export subsidies. The dispute was eventually resolved in 2000, but it highlights the competitive advantages to be had from working within the settings of a free trade area.

In the town of Ciudad Juárez in Mexico's Chihuahua state, in one of many industrial estates where *maquiladora* operations sit cheek by jowl, is Howe Leather's factory. Depending on the volume of work, between 200 to 300 workers cut finished leather into the patterns which are eventually sewn into car seat covers by other companies close by.

Howe Leather has been doing this since 1996, now generating sales worth A$100 million in the US, of which 80 million go through Mexico. Howe supplies the OEM "system suppliers" or Tier 1 companies. It works like this: the major car manufacturers in the US (called OEMs) outsource entire vehicle interiors to Tier 1 suppliers such as Lear Corporation, Magna and Johnson Controls. These system suppliers provide the complete package of styling, engineering, validation, harmonisation, craftsmanship and commercial management functions, taking total responsibility for the car interior. Tier 2 companies contract with these integrators to supply such parts as instrument panels, leather seats and trims, etc., while Tier 3 companies supply the makers of products such as leather seats with their input supplies, such as the cut finished leather patterns.

The most labour intensive part of the process is completed in Mexico, taking advantage of wages significantly lower than those in Australia and the US. The value-added by Howe Leather in Juárez (about 10 per cent) becomes part of the local content which determines the "Mexican-ness" of the finished product exported to the US under the NAFTA. The sales function remains with Howe Leather in Australia and the US. The Juárez plant is not treated as a profit centre and is managed as an integral part of the value adding chain.

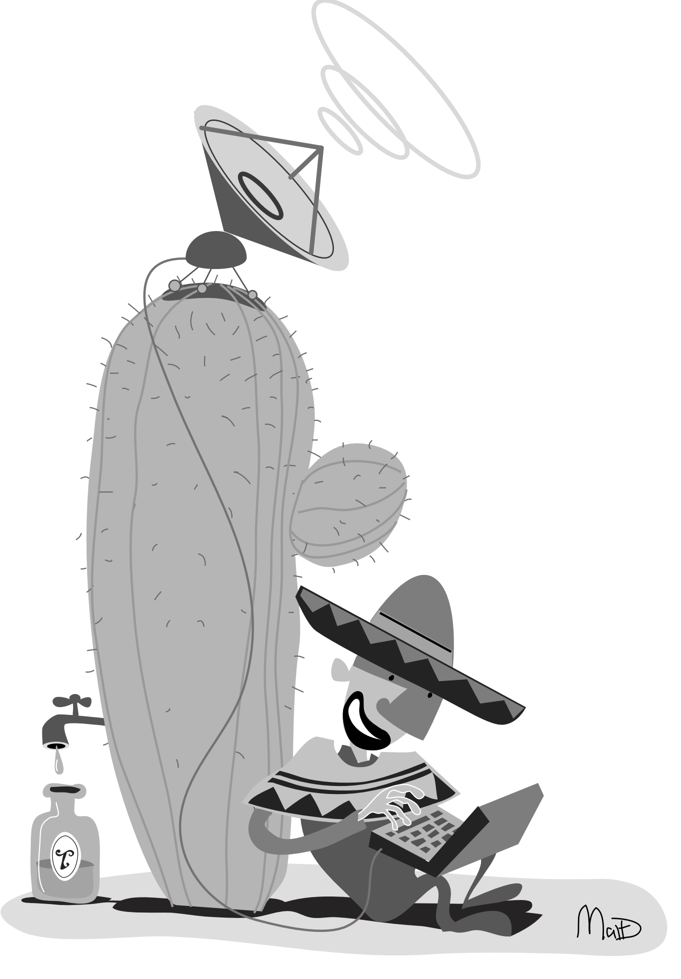
The company considers itself fortunate in the quality of the people it was able to attract to its Mexican operation. Unlike many other automotive *maquiladoras*, which mostly have US citizens running operations, Howe opted for a local General Manager, whom they recruited from a sewing plant. He brought a team of managers with him, including the HR manager. This ensured a rapid absorption into an existing and fully operational network of relationships. The management team of about 10 was brought to Melbourne for training, and in Mexico duplicated the Melbourne plant with the same machines, systems, methods, quality control and, importantly, the computer systems, so that inventory control is first class (trust is good, control better).

The logistics infrastructure from Juárez works very well, due to the close integration with the US market. A recent move to new premises also occurred without difficulty as there were no site-specific installations in Howe's Mexican operations.

PART THREE The Opportunities

The Opportunities

Modern Mexico is a predominantly open market offering opportunities in every sector of the economy for Australian companies able to meet Mexican requirements competitively, are prepared to invest in sound groundwork, research and relationship building and are able to "think outside the square". Mexico has actively liberalised and deregulated its economy. Most activity is in the hands of private companies, including, for instance, infrastructure such as railroads and airports. Controls on new entrants in the mining and fisheries industries have been significantly reduced. Most restrictions on foreign investment have been eliminated and over 90 per cent of the approximately 800 economic activities registered by the Institute of Geography and Statistics (INEGI) are now open to 100 per cent foreign ownership[23]. Even in many regulated sectors it is now possible to obtain authorisation for foreign participation beyond the prescribed level.



Teqnology

23 Information provided by the National Foreign Investment Commission 2001).

Opportunities for Australia in Mexico flow from the following factors, a common feature of which is the impact of NAFTA and other free trade arrangements:

- Mexico's sheer physical and economic size and expected future growth as the economy further integrates with that of the US. This must be tempered by an analysis of Mexico's purchasing power. According to InfoAmericas, "there is an enormous gap between the purchasing power and technology adoption rates of Mexico's middle and upper classes and those of its working and underclass, and the latter two comprise roughly 70 per cent of the population". Only the remaining 30 per cent is considered to have a purchasing power equivalent to Western European standards. Even so, this represents 30 million consumers and a segment of the population which will continue to grow.
- Due to a combination of preferential access, low cost structures and relative proximity to the United States, Canada, Europe and the remainder of Latin America, Mexico has become a strategic location for investment, particularly in the manufacturing zones – the *maquiladora* sector.
- There is a growing requirement for resources to fuel Mexico's industrialisation process and for commodities and processed foods to supply increased demand unable to be met by local production. The problem Australia faces from the double-edged sword of Mexico's preferential trading arrangements is not insurmountable.

These changes in Mexico's economic management have opened up opportunities, but competition has also increased in most sectors. Much of the competition comes from foreign sources, but leading Mexican business groups and families are also a major force in many industries, and Australian companies should, as part of their research, consider the impact, both positive and negative, that these family groups could have on the conduct of their business. Some sectors remain in state hands and others are restricted to Mexican nationals and companies with foreigner exclusion clauses in their by-laws. Moreover, key industries such as electricity, natural gas, water and telecommunications still limit private investment. It is, however, possible to secure approval for investment in these areas from the NFIC (see pages 34-36).

There are four main, surmountable constraints to Australian companies:

- lack of familiarity with the market – this can be addressed through research, visits and development of local relationships;
- language – English is becoming more widespread, particularly among the business community and government officials, but it is desirable and possible for Australians dealing with Mexico to learn some Spanish;
- disadvantages stemming from Mexico's preferential agreements with other countries and the absence of such an arrangement with Australia – these do not necessarily render Australian companies uncompetitive and for some businesses can be overcome through investment in *maquiladora* operations;
- distance to the market – this is largely a matter of perception: it takes less time to reach Mexico than it does to reach Europe.

Opportunities to export, invest or both exist in every sphere of economic activity for Australian companies, but a number of sectors appear especially promising. While greater detail is provided for these selected sectors, good business opportunities are to be found much more widely.

Agriculture and Food

Changing tastes and a growing urban, affluent and young middle class have increased demand for imported food products, a trend that is likely to continue.

The large increase in **processed-food** imports into Mexico over the past decade is also due to inefficient agricultural production and a growing focus on exports with attendant failure to supply local demand of certain products, such as milk and beef. Despite important reforms increasing agricultural production and giving it an export orientation, Mexico will continue to rely on increased food imports, including grains such as wheat, barley, maize, and sorghum. Fruit and vegetable crops for the US market will displace other crops destined primarily and traditionally for the domestic market.

There are opportunities for Australia in meeting the demand for imported processed foods, and in supplying technology and investment for a more efficient, export-oriented agricultural sector. Foreign investment in this sector has become more attractive following privatisation of state-owned enterprises involved in purchasing, production, processing, storage, importing, price controls and marketing and reform of the land tenure regime.

UPGRADING MEXICO'S AGRICULTURE – THE AUSTRALIAN ELITE GENETICS STORY

Steve Holt (third from left) and Mexican Partners.

Steve Holt has been doing business in Mexico with Australian tropical dairy and beef genetics, and the associated technology, since 1994. As Managing Director of Australian Elite Genetics, Steve introduced an initial livestock shipment by air in April 1996, consisting of the nuclei of Australian tropical dairy and beef genetics. This shipment was the first into Mexico since the advent of bluetongue in Australia in 1989. As a result of the success of the initial shipment, AEG has been able to access a niche market in tropical breeding livestock in the tropical states of Mexico.

AEGPL's product range includes the AFS (Australian Friesian Sahiwal) breed, Australian tropical beef breeds, livestock breeding technology developed from Australian research into tropical livestock management, and tropical plants and associated technology. In the wake of its success, AEGPL recently bought land in the tropical State of Campeche to establish a tropical dairying business using Australian tropical dairy cattle and systems. It anticipates this business will be operating by February 2003.

Research by AEGPL revealed that the tropical regions of Mexico have no dairying infrastructure, and that there was considerable scope for change. The breeds of cattle and management systems used in Mexico have remained unchanged for many decades. Mexico is the largest importer of milk powder in the world and Mexican governments for the last 20 years have been providing financial assistance to farmers to enter the dairying industry. AEGPL's strategy was driven by the huge growth potential of the Mexican market and its close proximity to the Central American market, but it has now become obvious that it cannot supply the demand in the Mexican market, let alone make an impact in any other markets in the region.

When talking about AEGPL's venture in Mexico, Holt says: "Most people with any experience in Mexico will tell you it takes a long time to make the right connections, but I was lucky. I knew that we required a strong financial partner who was located in the tropical states, one that could handle the disappointments in trying to introduce a new technology into a region with virtually no livestock infrastructure. I was very fortunate to find a strong family company with a lot of business experience who had introduced new technology in their respective industries".

Holt makes a number of revealing observations:

- "Most good business with Mexico is done on the basis of trust and understanding. The Mexicans need to like you to do business. Mexicans like to do business face-to-face. Don't expect to do repeat business by telecommunications; they like to see you slogging it out in their country".
- "They have a lot of experience in trading and getting the best position out of a negotiation. Basically you have to be a Latin, or think like one, to compete, and that is very difficult for non-Latin cultures".
- "A lot of business is undertaken socially, so it takes forever. You have to learn to be very, very patient. The business will be completed when the Mexicans are ready, not when you think it is time. In the regional areas they will often be two to three hours late for a meeting, and may not even turn up".
- "On many occasions you can be encouraged by the Mexican enthusiasm for a particular product or deal and leave a meeting thinking you have been successful, only to be disappointed later. Their enthusiasm often outweighs their ability to do the deal, and they find it very hard to say "no" to your face. This is not premeditated, it just happens".
- "An essential ingredient of the Mexican is optimism. When I asked why this was so, I was informed: 'That's about all we have'".
- "In my experience the only time to relax when doing business in Mexico is when you have been paid. I guess it the same in most countries, but the Mexicans, because of their friendly and very cordial nature, tend to get you off-guard. Mexican financial markets are volatile; there is a definite lack of financial liquidity in Mexico, particularly in the regional areas".

Holt adds that "patience and persistence are the keys to doing business in Mexico; you need to be well capitalized and ensure you trade in high-margin products or services".

AEGPL is developing a user-friendly, low-cost tropical dairying operation in its Campeche property. In Holt's experience, a mistake many companies make when introducing new products or technologies is to expect the technology or product to be used just like at the source. Often that is not possible due to cultural differences, so: "you have to find a formula whereby all parties win. Campeche has no experienced management, trained labor nor livestock infrastructure. You have to make the operation totally user-friendly, so that it requires minimum supervision.

In grains, wheat and barley imports are subject to quota restrictions. In 1998 and 1999 the US and Canada supplied all of Mexico's import requirements for these two products and this is likely to continue in the foreseeable future. Canada has provided 90 per cent of Mexico's canola imports, while the US has an 80 per cent share of the soybean market. Together they supply virtually all of the country's cottonseed imports, and 100 per cent of the imported corn market. According to Austrade, there may be room in the canola, sunflower seed, and cottonseed markets for Australian competitors.

The **dairy** sector has a number of strong domestic as well as foreign suppliers. Major foreign competitors with a local presence include: Unilever, Nestle, Parmalat, Danone, Kraft, and the New Zealand Dairy Board. While competition is high, additional opportunities exist for Australian exporters in powdered milk, cheeses, and other milk by-products. Local demand for milk consistently outstrips local production four to five times, making Mexico the world's largest importer of powdered milk. Purchases are made through a government buying agency *(Liconsa)* or its subcontractors. Some high-end product is imported on a quota system. Opportunities exist in upgrading local herds and adding warm climate know-how to Mexican dairying methods.

DAIRY TARIFFS AND REGULATIONS

Milk and cream – 10-20% tariff, with a 24-hour shelf life for milk after pasteurisation.

Whole milk powder – import quotas, tariff based on fat content.

Other milk powders – 10% tariff

Cheese – 20-40% tariff, but varies up to 125% with the variety. NAFTA sources duty-free from 2003.

Milk fat, butter, cultured products – 20% duty.

Source: Austrade

The **meat** sector, in which Australia already has an important presence, is worthy of more detailed consideration. Mexican meat consumption has been rising steadily in line with the country's recent economy recovery from the peso crisis of 1995. The bulk of the Mexican market remains extremely price sensitive, which means that meat consumption tends to be strongly influenced by the state of the economy. Beef and chicken are the most commonly consumed meats in Mexico, but there is a growing demand for sheep meat, particularly mutton. Retail outlets are also showing a growing interest in lamb, a market traditionally dominated by New Zealand, but with growing Australian participation. Most of this demand is met either domestically or from the US, which is the largest beef exporter to Mexico.

Total Australian meat exports to Mexico in 2001 were A$99.6 million, up from A$8.2 million in 1995. Bovine meat accounted for $A30.8 million, and other meat (mostly mutton and lamb) for the remaining A$68.8 million.

Mexico should remain a strong buyer of Australian mutton, while at the same time continuing to develop as a market for imported lamb. Bone-in legs, square-cut shoulders and shoulder chops are the principal cuts sold. Until recently, New Zealand was the only lamb exporter to Mexico. However, Australian lamb and mutton is now also sold through supermarket outlets. Some product is also available from the US and Chile.

Domestic and imported goods and services must comply with the Official Mexican Standards (NOMs), where these apply.

NAFTA eliminated tariffs on beef sales between member countries. This had a big, negative impact on Australian beef sales to Mexico. Tariffs for sheep meat within NAFTA countries have not yet been eliminated.

SPECIFIC MEAT TARIFFS FOR NON-NAFTA COUNTRIES

Beef – 20% on fresh beef, 25% on frozen beef and 20% on edible offal

Sheep meat – 10% on lamb and mutton. (Duties phased out for NAFTA countries by 2003)

Pork – 20% and import licenses are required

Poultry – 10% and import licenses required

Processed meat – 20%

Source: Austrade

Meat-related market entry strategies

There are a number of well-established Mexico-based meat importers. Mexican businesses typically do not respond to cold-call offers and suppliers or their agents should visit potential buyers and establish a personal relationship before attempting to make sales. Payment is not by a Letter of Credit in the Mexican meat market, it is generally 30 – 90 days Open Account, no security, high risk. Specific opportunities exist for lamb legs and shoulder cuts, mutton carcasses 15-20 kg (fat score 1-2), and offal and other fancy meat cuts.

The traditional sheep meat market is dominated by a relatively small number of importers. It is important to develop a personal relationship before making specific offers. The market and potential for Australian lamb is also growing, but will typically need to be supported by point-of-sale and in-store promotions at retail level.

The Mexican government and industry are keen to improve processing and slaughtering facilities and technology. Specific opportunities for Australian companies in the slaughtering and meat processing sector include modernisation of coldrooms, meat cutting and commercialisation systems, meat cut classification systems, product and by-product classification.

CASE STUDY: DAVID AARONS AND AUSTMEX PTY LTD

Preparation of Tacos with Australian lamb supplied by Austmex.

Austmex is a fully owned subsidiary of the Keys Trading Group of Companies. It was the first Australian company to establish a representative office in Mexico and by the end of 2001 accounted for about 65 per cent of Australia's frozen mutton and lamb exports to Mexico. David Aarons, Managing Director, attributes the company's success to a multiplicity of factors.

Their thorough **research of the market** (which included accessing Austrade's services) during 1987-89 revealed the key foundations for a marketing strategy. Structural reforms in the economy were starting to expand the Mexican middle class, which offered the potential to rapidly grow the market for high quality meat. There was a significant New Zealand presence employing expensive (but essentially subsidised) distribution methods, including sales of small lots from cold storage in bonded stores. It was certainly clear that a shift in tastes, and the fact that Mexicans are very quality conscious, would ensure a market worth building.

Aarons needed **better shipping services** than were available at the time, so he lobbied shipping companies and convinced them to offer a regular service to Mexico. This greatly reduced freight rates, enabled considerably faster deliveries and made the Austmex product more competitive.

Austmex then established a **sales office in Mexico**. This worked well until 1993 when Aarons decided to change the structure of the office from that of a selling operation to a service office. Experience had shown that Mexicans preferred to deal directly with exporters in their own countries for reasons of privacy and efficiency. Sales were handled direct from Australia, while Austmex in Mexico concentrated on shipping matters, customs clearances, trouble-shooting for their wholesale customers, to following up on accounts issues and engaging in general public relations and promotional efforts to support the importers. This formula has had greater acceptance than that adopted by other Australian exporters, who have relied on indirect sales and service through agents or brokers mainly in the United States.

Part of Austmex's effort included a long-term investment in the **education and training** of its customers in better understanding the products they were handling. Key Mexican personnel were brought to Australia to be trained in local abattoirs. Austmex seeks to deliver consistent quality to its customers. Each customer is supplied with a differently **branded product**, rather than whatever might be opportunistically available at the cheapest price. This has led to greater consistency and predictability in quality, a factor much appreciated by the company's wholesale buyers in Mexico. Lying at the heart of this approach is that selectivity in customers, and the product supplied to them, pays long-term dividends.

The Melbourne-based sales staff of Austmex **visit Mexico** several times a year, to liaise with buyers, assess trends and generally keep abreast of market developments and changes in regulations. This is done more frequently when a new product is introduced or the market developed further. Such ongoing investment in the market is considered vital.

Education Services

Mexico is a first tier market for education services. According to studies undertaken by the Australian Embassy, upwards of 40,000 Mexican students study internationally each year, not including students undertaking English courses on tourist visas. The United States and Canada between them account for close to half of these numbers. There are more students in higher education (1.7 million) than in Latin America's most populous country, Brazil, and more postgraduate students as well (88,000). Some 400,000 students are enrolled in private institutions, where the tuition costs are in some cases higher than at Australian universities.

Mexico is a country with great income distribution disparities. In the wealthy triangle of Guadalajara, Monterrey and Mexico City, there are substantial means dedicated to the top end of the education pyramid. Monterrey Tec is one of the world's great modern universities. There is a great deal of symbiosis between private universities and the private sector, especially in the area of Information and Communications Technologies. This influences the universities' resources, location, areas of priority research and employment for graduates.

At the level of basic education there are still significant disparities between regions as well as within them. Basic education is a decentralised responsibility. The World Bank is active with projects in Mexico and these offer some limited opportunities for Australian consultants, although most of these consultancies are filled from Mexican sources.

There is a gap within the Mexican education system in the VET sector. Opportunities exist for custom-designed courses in sectors such as Information and Communications Technologies, diploma-level engineering specialisations and in tourism and hospitality studies. Some work between Australia and Mexico has been carried out in the area of competency-based training and there are opportunities to build on this.

The US and Canada have been the main destinations for Mexican students studying abroad. The numbers coming to Australia have started to grow, however, following the establishment of an IDP office in Mexico City (IDP is a private company which promotes most Australian Higher Education institutions globally), as well as the emergence of education agencies dedicated to promoting Australian education providers. Two such agencies are Australian Education Services and Mexico Australasia Student Services, both of which promote a smaller group of Australian higher education institutions (who feel they can be more effective by using both IDP and a more specialised agency) and English language colleges. The Embassy is able to provide contact details for the education agencies.

Under the liberal Mexican foreign investment regime it is possible for Australian institutions to establish campuses in Mexico as well as entering into joint ventures or making acquisitions (approval is needed to own more than 49% of a local higher education establishment).

English language courses are the primary means of opening the market.

Postgraduate studies are an area of opportunity as is the VET sector. Successful entry into the Mexican education market needs a solid set of local relationships with Universities, government agencies responsible for technical training and with a reputable and energetic agent able to conduct marketing and recruitment, assist with securing international development projects and oversee any joint ventures.

Australia and Mexico decided in July 2002 to commence negotiations on a bilateral framework agreement on educational and cultural cooperation. When finalised, this agreement will facilitate links and exchanges between educational and cultural institutions in both countries.

Australian companies intending to explore the Mexican market need above all else to identify a sound local agent who will give them priority attention; they need to conclude an agreement with the National Science and Technology Council (CONACYT), the main government agency dealing with funding for studying abroad, in order to participate in the CONACYT fair (typically such an agreement involves granting discounts in tuition fees); and finally they should consider participating in appropriate education exhibitions, including those held by IDP. The market should be visited at least annually.

Energy and Resources

Lying at the heart of Mexico's future developments in the energy sector is the resolution of a uniquely Mexican dilemma. The supply of electricity and the operation of the country's hydrocarbons industry are constitutionally and politically defined as government responsibilities. Over the years, dependence by government on income from particularly the oil industry, and the provision of subsidised electricity, has kept investment in these industries to a bare minimum. The results are evident and major investments are needed throughout this sector. Private sector involvement has therefore become imperative, but faces the constraints imposed by politics and the law of the land. Constitutional reform is difficult and new investments are urgent. Inventive means are therefore being devised to enable private sector involvement, and opportunities for business emerge from these arrangements.

Inventive means are being devised to enable private investment in the energy and resources sector.

Electricity

Mexico is facing some major new investments in electricity generating capacity in the coming decade. The pressure for this is coming from rapidly increasing demand as well as the need to change the generating fuel mix. During the decade to 2001 the demand for electricity in Mexico has increased by an average of 5.2 per cent a year and is expected to increase by an average of 6.3 per cent a year in the period 2001-2006. The 2001 total installed capacity of the country is 38.5 GWe (compared to 44 GWe for Australia), and in its development plan for 2001-2006, the Mexican Ministry of Energy (Energia) estimates that Mexico will need an additional 27 GWe over the next decade in order to meet its projected consumption. This translates to expected investments in the electricity sector for the period 2001-2010 of US$74 billion of which over US$39 billion will need to come from the private sector.

Since the passage of the Law for the Public Service of Electric Power in 1992, activities such as self-generation, co-generation, independent power production and small-scale generation (less than 30 MW) are now open for private investment but require a permit from the Energy Regulatory Commission (CRE) based on a recommendation by the Federal Electricity Commission (CFE). Unfortunately CFE also sets the electricity price. Apart from owning the entirety of the electricity distribution and transmission systems in Mexico, CFE owns 92% of the electricity generating capacity. *Luz y Fuerza Del Centro*

(LFC), Mexico's other state-owned electric utility, operates about 2% of Mexico's generating capacity.

A reform proposal currently being considered by the Mexican Congress seeks to allow private companies to sell electricity in the wholesale market. Private generators would compete with CFE and LFC and the transmission of electricity would remain under the exclusive control of the Mexican Government, but the state monopoly in the generation and distribution of electricity for public service would end. The reform proposal is opposed by the Institutional Revolutionary Party (PRI) which holds the majority in Congress, but should it eventually be passed, this would open up some opportunities for Australian businesses, not least in that the reforms would increase demand for natural gas. Increased use of natural gas has cost and environmental motives with the latter as a particular accelerator for renewable energy, mainly from geothermal sources.

Oil

Mexico ranks as the world's fifth oil producer on the basis of crude oil, lease condensate, natural gas liquids and refinery gain. Mexican crude oil reserves are estimated at 26.9 billion barrels. Oil is a state monopoly administered by Petroleos de Mexico (Pemex) and only primary and secondary petrochemicals are open to private sector participation. Only the production of secondary petrochemicals is open to foreign investment. Mexico's downstream oil sector was nationalised in the 1950s, and while privatisation is not envisaged, private companies may retail refined petroleum products. Major investments are required to maintain current production levels. Mexico suffers from insufficient refining capacity and imports about a quarter of its petrol requirements.

Opportunities for Australia in this sector are limited, but may include exploration, the provision of environmental services and the supply of equipment to Pemex.

Natural Gas

Mexico has proven natural gas reserves of 29.5 trillion cubic feet (Tcf), with 1999 production of about 1.29 Tcf and consumption of about 1.26 Tcf. As with oil, Pemex retains exclusive rights to exploration and production of Mexican natural gas, in keeping with the country's constitution. Natural gas nevertheless offers greater prospects for private investment. Currently private companies can provide services to Pemex, including drilling, transport, storage and distribution. With prior approval, foreign investment may participate in these activities to any ownership level (see pages 35-36). The rights to the reserves and the profits, however, remain with Pemex, while service-providing companies are to be paid fees, rather than share in the profits, in an arrangement called "multiple service contracts".

The transportation, storage, and distribution of natural gas has been open to private investment since the passage of the 1995 Natural Gas Law, although it limits companies from ownership in more than one function within the industry. Private-sector participation in these areas currently is subject to 30 year permits granted by the Mexican Energy Regulatory Commission (CRE), based on competitive bidding. Natural gas distribution has a number of private participants with over 20 permits issued since 1995.

In order to keep up with the growing demand for natural gas, Energia and Pemex have designed a strategic ten year program which involves the development of four basins for natural gas. As part of this program Pemex announced in December 2001 plans to enter into multiple service contracts with foreign companies to exploit reserves located in the 50 square km Burgos Basin which will be divided into a number of geographical blocks.

The projects are expected to lead to an increase in production of natural gas of one billion cubic feet per day by 2005. Pemex expects to be in a position to tender for these contracts towards the end of 2002.

Mining

Australian mining and mining services companies are already well established in Latin America, especially in Chile, but their presence in the Mexican mining sector is relatively small by comparison. Currently, Australian companies operating in the Mexican mining sector include Mincom (which designs and supplies asset management software for capital intensive mining), MIM Exploration (which is involved in copper and gold exploration), Orica (which supplies explosives and blasting technology to mining companies), and Secotec Mining (which is involved in gold-extraction activities).

Seventy five per cent of Mexico's territory remains unexplored and is thought to be highly prospective. Mexico already leads the world's production of silver and is an important producer of strontium, fluorite, bismuth, arsenic and graphite production, copper, gold, lead, zinc, graphite, mercury, antimony, cadmium, sodium sulfate, felspar and barite. The chances are that there are some opportunities for Australian companies in exploration.

The mining sector has been in decline since 1996 and mining's contribution to GDP stands at 1.6 per cent, compared to 2.6 per cent 25 years ago. Nevertheless, investment in the sector since 1995 reached US$6 billion, of which US$2.18 billion was foreign investment. Further investments of US$3.35 billion are forecast for the 2001-2006 period, including over US$800 million in equipment purchases.

Australian companies with technology, know-how and equipment aimed at improving the efficiency of existing mines and processing plants are likely to find business in upgrading Mexican resource processors. Mining equipment imports from countries without free trade agreements with Mexico will typically face a tariff of between 10 and 20 per cent. Bilateral cooperation in the mining sector will be further assisted by the conclusion of a mining Memorandum of Understanding between Australia and Mexico.

The Mexican mining industry is dominated by six consortia, which are responsible for over 80 per cent of the country's mine production.

THE BIG BOYS IN MINING

- ***Grupo Mexico*** – copper, molybdenum, copper blister concentrate. Owns Asarco and Southern Peru Copper.
- ***Industrias Peñoles*** – gold, silver and zinc.
- ***Compañía Minera Autlan*** – iron alloys.
- ***Empresas Frisco*** – lead.
- ***Grupo Acerero del Norte*** – iron and steel, coking and steaming coal.
- ***San Luis Corporación*** – gold and silver.

Australian companies interested in Mexico should leverage off Australia's existing presence in Latin America in the first instance, as well as taking advantage of contacts with Mexican counterparts elsewhere. They should also consider participating in Mexico's major mining show, Expomineria, which is held every second October in Acapulco. Finally, they should explore possible commercial arrangements with the six principal groups operating in Mexico.

Mexico has recoverable coal reserves of about 1.3 billion short tons, just over 70 per cent of which is anthracite and bituminous. Local production is more costly than imports. Coal-fired power generators supply roughly 10 per cent of Mexico's electricity, but power plants fired by natural gas are favored to meet rising demand. Australian exports of coal to Mexico grew more than threefold from 2000 levels to total over A$115 million in 2001. Mexico blends high quality imported coal with its own high ash content coal and coal imports are expected to continue into the foreseeable future. Australian companies could increase their share of Mexican imports. There is potential to change Mexican perceptions about the emissions from burning coal for fuel by marketing Australia's expertise in clean coal technology. There may also be opportunities in the areas of local mine management, including software, and environmental services.

Mexico is highly prospective in the area of mining and technologies which minimize the impact of mining on the environment. It is one area of Australian international best practice which is becoming increasingly relevant in Mexico.

Infrastructure and Development

Australian companies operating in the diverse fields of infrastructure and development, and interested in diversifying into Latin America, will find a series of projects offering investment as well as consultancy and technical service opportunities.

Plan Puebla-Panama (PPP)

Just south-east of Mexico City is the state of Puebla. It is where the least developed parts of Mexico begin, stretching to the Yucatan Peninsula. The neighbouring countries of Mesoamerica, that stretch along from the Mexican border through Guatemala, Belize, El Salvador, Honduras, Nicaragua, Costa Rica and Panama, are even further behind in economic development terms. Apart from a cavalcade of natural disasters and political misfortune, the lack of cross-national cooperation has kept Mesoamerica from pulling itself out of its economic stagnation.

This situation is not surprising, when a simple truckload of goods departs La Union in El Salvador and then takes 24 hours to reach Chinandega in Nicaragua, some 130 kilometres down a highway. The trip is not easy: road maintenance is not what it should be, there are no paved shoulders and there is the occasional traffic congestion. But that's not the main problem. The delays are mostly caused by the two border crossings the truck has to negotiate, and the frontier formalities chew up 60 per cent of the time taken. Not surprisingly, there isn't a lot of trade volume flowing between these countries particularly when freight charges are triple what they are in Australia; more business is done outside the region than within it.

The region's political leaders came up with the Plan Puebla-Panama which is designed to promote the economic integration and sustainable development of the region by addressing infrastructure and social problems and by seeking to make the most of its ecological and cultural diversity. The focus is on what can be done to allow the 65 million people of the region to bridge the ever-widening gap with Northern and Central Mexico. And there are the pesos to back up the words for eight projects in the Plan Puebla-Panama portfolio covering:

- highways integration (US$3,421 million);
- interconnecting electricity grids (US$445.7 million);
- sustainable development (US$16.5 million);
- human development of traditionally marginalised groups (US$31.5 million);
- prevention and mitigation of natural disasters (US$27 million);
- tourism projects (US$51.7 million);
- export facilitation (US$23.5 million);
- telecommunications (US$1.2 million).

Mexican authorities have sought to involve Australian companies in projects under the PPP, primarily as investors.

National Development Program

The National Development Plan 2001-2006 proposes reforms in education, the energy sector, the federal system of government, the finance sector, the justice system and the labour market as well as improvements in the government's own fiscal framework and its budgetary processes and in environmental standards and compliance. Underpinning the National Development Plan is the National Program to Finance Development 2002-2006 managed by the Ministry of Finance and Public Credit.

Mexico and the World Bank

The World Bank loves Mexico. And the feeling is mutual: in December 2001 Mexico awarded the country's highest honour given to foreign institutions (other than Heads of State or Government), the *Aguila Azteca en Venera*, to the World Bank Group, through its President, Mr James Wolfensohn. As of 28 February 2002, the International Bank of Reconstruction and Development (IBRD) had an exposure to Mexico of US$10.9 billion, its third-largest country portfolio, and 9.5 per cent of the total IBRD portfolio[24].

Working in three-year strategy cycles, the World Bank's activities in Mexico have concentrated in areas that match Mexican government priorities (see National Development Plan). The World Bank considers that the National Development Plan 2001-2006 poses five administrative challenges: consolidating the macroeconomic gains of recent years, accelerating growth through competitiveness, developing the stock of human capital, balancing growth and poverty reduction with environmental protection, and building an efficient, accountable, and transparent government. The interest for foreign business in this World Bank approach is how these perspectives shape the business climate, what specific projects are approved and which offer opportunities for participation by Australian consultants and firms specializing in economic and social development work.

24 The World Bank Group consists of five closely associated institutions: the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA), and the ICSID (International Centre for Settlement of Investment Disputes. Details of the role and function of each of these institutions are available on www.worldbank.org in "About Us" under "Organization". The term "World Bank" refers specifically to the IBRD and the IDA.

The World Bank is proposing to back this coordinated strategy with lending of US$5 billion during 2003-05. Mexico's IBRD exposure is also projected to increase to US$12.1 billion by the end of this period, although it is expected to level off thereafter. In addition, another arm of the World Bank Group, the International Finance Corporation (IFC), will be backing the private sector component of the strategy. A study of the 24 World Bank projects approved for Mexico since 3 April 1999 shows the priorities: environment (8 projects), education (1), health (1), finance (4), law/justice/public administration (4), economic policy (1), energy (1), transportation (1), agriculture (2) and private sector development (1). Full details of the World Bank Group's program for Mexico can be obtained by reviewing the Bank's Country Assistance Strategy for Mexico, accessing the World Bank's website and individual country portal:
http://www.worldbank.org/html/extdr/regions.htm#m.

Australia is able to bid for World Bank Projects in Latin America as it does in Asia and elsewhere. While, as distinct from Asia, Ausaid does not have an aid program in place for Latin America, it is possible to access multilateral procurement project funds through strategic alliances with well-placed local partners and through investment projects which can complement World Bank projects.

Telecommunications

Mexico privatised the government-owned telephone company, Telmex, in 1989 and its monopoly ceased in 1997. Telmex still controls 95 per cent of local telephone services, 66 per cent of long distance services, and 55 per cent of data and internet services. Telephone density remains low, with less than 12 per cent of the country's population of 100 million having fixed line telephones. Mobile phone use grew exponentially up to 2000. It is expected that 23 per cent of Mexicans will have a mobile phone by the end of 2003 [25], the overwhelming majority employing pre-paid systems. This represents almost one phone per inhabitant in the middle and higher economic consumption brackets. The expansion of cellular networks was made possible by an appreciating peso (expansion investment plans rely on imported equipment and technology), the perception of the cellular telephone system as an alternative to fixed lines, and by economic growth and regional development.

Mexican law allows up to 49 per cent foreign participation in telecommunications networks and services – with the approval of the National Foreign Investment Commission (NFIC), foreign participation in cellular phone services can be higher. Exporters to Mexico not enjoying free trade status face tariffs ranging from 10 to 20 per cent.

Possible areas of opportunity for Australia are in the high technology end of telecommunications activity. Areas that could be explored include the provision of technology for wireless local loops, ISDN equipment, "last mile" enabling solutions, billing and management software, and wireless application protocol (WAP) applications and software.

25 InfoAmericas

Companies looking to enter the Mexican market should in the first instance review Austrade's most recent analysis of the telecommunications market (at www.austrade.gov.au). They should then approach the major operators in the market, to assess their needs and Australia's capacity to supply them.

The Major Operators

Telmex – the equivalent of Australia's Telstra and the largest telecommunications company in Latin America. Sales are in the US$10 billion region. Telmex's cellular telephony subsidiary, Telcel, has over 70 per cent of the market. Ericsson has been the main infrastructure supplier to Telmex/Telcel.

Iusacell – Mexico's second largest mobile phone company. Vodafone, Bell Atlantic and Verizon are part owners of Iusacell, which is investing heavily in capacity and coverage expansion. Iusacell grew by 27% in 2001.

Alestra – a joint venture between US-based AT&T, BBVA-Bancomer and Grupo Alfa. It is one of Mexico's largest telephone carriers. In its first phase, Alestra deployed 4,000 kilometres of fibre optic network, including switching centres in the major cities. The recently completed second phase extended the network to 8,600 kilometres.

Avantel has captured 16 per cent of the long distance market. It is a joint venture between Banamex-Accival and US-based Worldcom (the demise of its US partner will not affect Avantel's operations).

Unefon – began commercial operations in February 2000 and is one of Mexico's fastest growing wireless operators. It has been particularly successful using a prepaid card scheme to penetrate the lower end subscriber base. Unefon's controlling shareholders include TV Azteca and the Saba family, each with 46.5 per cent of the company.

Axtel – one of the fastest growing local exchange carriers in the major metropolitan areas, it has 51 per cent Mexican ownership, as well as foreign investment from AIG-GE Capital, Bell Canada and MetLife.

Pegaso PCS – is one of Mexico's newest mobile operators and one of the first companies to offer mobile internet services. It has an alliance with Microsoft, Qualcomm and Ericsson to develop wireless internet applications and products.

Motor Vehicle Industry

They are all there, the well-known names of the global motor vehicle industry. Together they account for 2.6 per cent of Mexico's GDP, 12 per cent of imports and 20 per cent of exports. They are Mexico's second largest employer and produce close to two million vehicles annually, making Mexico the 9th largest vehicle manufacturer in the world.

THE WELL-KNOWN NAMES

- **BMW** owns an assembly plant and has an active parts purchasing program for its factories worldwide.
- **Daimler Chrysler** has two locations for assembly plants for passenger cars, engine and stamping plants and the assembly of trucks.
- **Dina/MCI** has become Mexico's largest manufacturer of buses, trucks, agricultural equipment and automotive parts. Grupo Dina controls 70 per cent of the motor coach and bus market in Mexico.
- **Ford** assembles cars, light trucks and mini-vans, operates a stamping facility as part of one assembly plant and makes engines in Chihuahua.
- **General Motors** has three plants making trucks, sedans and utilities, supplying a quarter of the market.
- **Honda** makes 20,000 Accord cars in Mexico with parts and engines from its other North American plants.
- **International** started in Mexico in 1926, importing trucks from the US. With NAFTA, it started assembling buses and now can make 150 medium-sized and 70 heavy trucks per day.
- **Kenworth** began assembling heavy trucks and trailers in Mexico and now exports products to the US, Chile, Colombia, Canada and Puerto Rico, amongst others.
- **Mercedes-Benz** makes trucks and buses in Mexico and imports passenger vehicles from its production facilities in Germany, the US and Brazil.
- **Nissan** is Mexico's second largest motor vehicle producer, manufacturing passenger cars, light trucks, car parts and components (including machined, stamped, cast and aluminium).
- **Peugeot** imports cars and has built a huge distribution facility on the edge of Mexico City, aiming for sales of 30,000 by 2005.
- **Renault** uses its Nissan partnership to make compact cars in Mexico, targeting markets from Mexico to the Caribbean, Central and South America.
- **Scania** makes a quarter of its sales in Latin America and is aiming to take one fifth of the bus and one tenth of the truck market in Mexico.
- **SEAT** has had success with sales of fully imported vehicles through 15 dealerships.
- **Toyota** imports passenger cars and is investing in a plant to make pickup truck assemblies.
- **Volkswagen** is Mexico's largest vehicle exporter and at Puebla keeps 16,000 workers busy building almost 1,000 new cars a day (270 of them new Beetles, only produced in Mexico).
- **Volvo** makes trucks, assembles cars and buses and sells Mack trucks.
- **Audi**, **Jaguar**, **Land Rover** and **Porsche** are also active selling imported vehicles.

Australian automotive product suppliers for whom these names are customers, or who supply to their aftermarket, may well be able to do business in Mexico. It is an attractive *piñata*. By 2004 the demand for passenger motor vehicles is expected to hit one million units, of which three-quarters will be supplied from local production. Mexico is the world's biggest bus market, worth around US$636 million in 2001. About 10,600 new buses are sold every year and this volume is expected to grow five per cent annually over the next ten years.

The growth of trade between the US and Mexico has fuelled the demand for trucks and there are about 450,000 units in the Mexican truck fleet. The average age of the fleet is 16.3 years. Demand for heavy trucks is expected to reach 24,600 units and 9,500 trailers in 2003.

Australian manufacturers exporting to Mexico need to contend with import tariffs from 13 to 30 per cent, which often places them at a significant disadvantage against imports from NAFTA countries, the European Union and a number of Latin American countries which enjoy duty-free or preferential access on many items. Just-in-time supply constraints and limited shipping options create difficulties for Australian companies competing for contracts to supply the Mexican automotive industry.

If established in Mexico, however, an Australian manufacturer would enjoy the competitive benefits of the maquila program (see page 43), proximity to the US border, a qualified workforce and the lowest (albeit growing) wages in the NAFTA region. Importation under maquila receives special treatment and, if included within a larger assembly, enables easier access to markets otherwise protected.

Opportunities: Parts for the Domestic and Export Markets

Demand for input parts for Mexican assembly plants cannot be met domestically, partly through difficulties in meeting the stringent quality requirements of car manufacturers. Moreover, Mexico's automotive parts industry is becoming increasingly focused on exports. In 1993, 86 per cent of the auto-parts manufacturers were Mexican-owned companies. By 1997 30.7 per cent of the auto-parts producers were German-owned and 29.6 per cent were US-owned [26].

Gasoline to LPG conversion – Conversion to LPG is becoming increasingly popular, from a small base. Mexico is the world's biggest consumer of LPG for domestic use and the 4th largest consumer of LPG overall. As it is considered a household necessity, the government controls the price of LPG, which makes conversion competitive.

Manufacturing systems – Mexican manufacturing plants are increasingly adopting international efficiency standards. This opens opportunities for Australian companies with appropriate systems, technologies and ICT solutions.

Vehicle Location Systems/Antitheft Systems – Over 100 cars are stolen daily in Mexico City. There is a growing demand for vehicle location/detection systems. Manufacturers are planning to include such systems as an option on their new vehicles.

Computer Based Training (CBT) – a potentially profitable niche for Australian software companies with experience in developing CBT for car manufacturers.

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26 Austrade figures

Market Entry Strategy

1 Survey local manufacturing assembly plants and their specific parts needs and assess the feasibility of supplying from Australia in competition with countries enjoying duty-free access, or from Australian plants located in these countries.

2 Explore the option of producing locally, preferably in a joint venture with an established Mexican parts manufacture with facilities located near the vehicle production facility.

3 Orient the potential business towards exports, taking advantage of Mexico's free access to major world markets.

4 Emphasise quality and efficiency to meet international benchmarks, and focus on complete systems.

Niche Opportunities

Industrial Machinery and Equipment

The demand for almost all industrial machinery and equipment is covered through imports, with annual imports of capital goods exceeding US$20 billion for the first time in 1999. Close to 70 per cent of these imports are machinery for metal shearing, metal transformation equipment, drilling, industrial technology and equipment for power generation. Australian companies with innovative industrial solutions can expect to arouse interest among Mexican customers, as packaging machinery manufacturer TNA discovered.

MACHINERY TO MEXICO – TNA

TNAMEX, a subsidiary of TNA which manufactures and sells food packaging equipment, was established in April 2001, after a very successful five years of sales principally in Mexico but also to other parts of Latin America. During those five years TNA almost completely displaced its main opposition in this area, an old and well-established company based in Georgia, USA. As TNA's success spread through the region it realised that it was not just due to its superior equipment, but also to the complete lack of attention its new customers had previously received from main rivals. It eventually reached a point where the next logical step was to localise this service.

So TNAMEX was established in Mexico in order to serve as the sales and service center for Mexico, Latin America and the Caribbean, and to develop Mexico as one of TNA's principal regional centres of technical support personnel to supplement regional and home offices in Dallas, Birmingham, Sydney and Melbourne.

As an added bonus to providing its customers with specialised local sales and technical service, TNA worldwide could now tap into a very highly educated, skilled, motivated and young workforce. Already TNAMEX's technical team has received high praise for the service provided to TNA customers not just in Latin America but also in the US, England and Spain.

Although Latin America is at this time experiencing a period of economic downturn, and as a result TNA's sales have also declined there is no doubt that the decision to establish TNAMEX was correct. TNA's main opposition today is a Japanese manufacturer of packaging equipment which has also established similar facilities in Mexico.

Steps taken prior to entering the Mexican market included opening an office in Dallas Texas and commencing to staff that office with people who not only spoke Spanish but were also very attuned to the Mexican culture. This proved to be much harder than expected. Until TNAMEX was established there was a very high turnover of bilingual staff, especially in the technical area. Lack of knowledge of Mexican laws, especially labor laws, resulted in some mistakes. Contracting the services of reputable firms of lawyers and accountants minimised these.

According to TNA Vice President for Latin America, Luigi di Palma, there are not many additional requirements to run a business in Mexico to what there are for any other part of the world. However the points below, although important anywhere, are especially important in Mexico:

1. Support your customers (some are tired of being kicked around and find it a relief that foreigners treat them as equals).
2. Get close to your customers.
3. Understand and support local culture.
4. Have staff knowledgeable of the company's products, enthused by its strategies and proud to belong to the team. "Ponerse la camiseta" (Be proud of your team's shirt).

"The biggest pitfall is to take people for granted, or believe that you are smarter and therefore superior simply because you are from elsewhere. Australia and all things Australian are greatly appreciated; use this to get close to people, not to belittle them."

Health Care

The main providers of health care are the IMSS *(Instituto Mexicano del Seguro Social)* and the ISSSTE *(Instituto de Seguridad y Servicios Sociales de los Trabajadores del Estado)*, both being social security organisations. IMSS covers over 47 million people, while the ISSSTE services over 10 million and are both funded by employer and employee contributions, investment returns and transfer payments from the federal government. There are several other health care providers run by or for defence forces, the state-owned oil company Pemex, indigenous people and private institutions. Of the 500 hospitals operating in the year 2000 and open to all Mexican residents, some 431 are operated by the Ministry of Health and the remaining 69 by IMSS. A further 467 hospital units, open to beneficiaries only, are run by IMSS (267), ISSSTE (103), Pemex (23), Defence (42) and the Navy (32)[27].

27 www.ssa.gob.mx

Importing from Mexico

There are business opportunities in importing from Mexico particularly suited to small and medium-sized companies, for instance: handicrafts, furniture, specialist food products and photographic equipment. Companies looking to import could start by checking the products currently being imported from Mexico (see page 78) and then contact Bancomext for a list of Mexican products available for export and their suppliers.

CASE STUDY SMALL BUSINESS AND IMPORTING FROM MEXICO

Mexican Glassware imported by Mexican Imports Pty Ltd.

Libby Harold established Mexican Imports Pty Ltd in 1976. At its peak the company employed 12 people and had a turnover of A$2 million. On average it imported two containers per month of a large range of Mexican products, "primarily glass products, but everything except clothing and food". It has been a successful business, supplying mainly home ware retailers, furniture stores, restaurants, and also retailing to the public.

The road to success was not easy. While Libby did not find the language barrier a major issue ("Mexicans are very tolerant of people who don't speak Spanish"), there were many issues of business etiquette to learn. In particular, Mexicans place great store on respect, personal relationships and courtesy. It is not feasible to "set something up, go away and expect it to happen". Two visits a year were necessary even with agents on the ground. And frequent communication, confirmation, monitoring, reconfirmation and restatement of agreements, understandings and requirements are important.

It is essential to have a representative on the ground who is completely trustworthy and is "working for you 100%".

In the import business it was necessary to factor in up-front payment of a deposit. Letters of Credit and other similar financial instruments did not work, at least in her trade.

Sourcing handicrafts from Mexico also had problems: balancing supply and demand, and identifying the right contacts (e.g. it was not a good idea to deal directly with the manufacturer, but to work through the village wholesale agent, who would normally have a higher level of business sophistication).

Shipping was effective and reliable. There is a weekly service across the Pacific. It normally took 20 days port to port. On the other hand, banking was not completely straightforward as Australian banks did not quote or deal in Mexican Pesos, but had to operate via the United States Dollar.

Finally, Libby considers that part of the secret of her success was to focus on genuine Mexican products, rather than on copies made in other countries.

Environmental Products and Services

Air, water and ground water pollution, solid waste disposal problems, population, industrial and economic growth pressures, problems with bush and pasture fires, a lack of domestic technologies and expertise, the Mexican government's commitment to abide by international environmental standards in response to international pressure, and growing public awareness are all creating a demand for environmental products and services. These represent opportunities for both foreign and domestic firms. According to Mexican government sources, environmental problems represent a drain on GDP of around 11 per cent.

Only five per cent of Mexican ground water is sufficiently uncontaminated to be made available for all uses without prior treatment. 22 per cent can be rendered potable with traditional water treatment methods, 49 per cent requires advanced treatment techniques. Any technology improving the economics of this process will have a market in Mexico.

As with much of the developing world, recycling is not practised in Mexico in a comprehensive and systematic way. Technologies which make recycling competitive as an economic activity could have relevance in a market which is experiencing rapid industrialisation[28].

Cultural Exports

There appear to be export opportunities in specific service sectors in Mexico. A successful exporter of cultural services tells a story of persistence, relationships and wisdom.

CASE STUDY MACDONNELL PROMOTIONS

Macdonnell Promotions has been exporting Australian cultural product to Latin America for over 20 years and is the only company which has done so continuously and consistently. Managing Director Justin Macdonnell first visited Mexico in early 1991, on an itinerary set up by the Australian Embassy. Amongst his contacts was the then manager of the Gran Festival Ciudad de Mexico, Jaime Suárez. He and his colleagues were intrigued by the idea of presenting Australian work and wanted to see more. Upon returning to Australia, Macdonnell reported this to the Australia Council – the Federal Government's arts funding and advisory agency. In concert with them, and at their expense, Macdonnell arranged for Suárez to visit the 1992 Adelaide Festival of the Arts where he saw an enormous quantity of Australian product and went away enthused. This marked the beginning of a relationship in which there was a sense of reciprocal obligation and a commitment to move forward.

In mid-1993 the Gran Festival Ciudad de Mexico ran the first ever arts market in Latin America called MercArtes, in which Australia became the only non-Spanish participant. Australia took a stand to sell its wares but also brought buyers from the Perth and Sydney Festivals thereby strengthening Australia's capacity to be seen as serious about a two-way trade. Both sides were able to satisfy their buying and selling needs. It was the beginning of a ten-year partnership with Mexico, which has had ongoing benefits for Australia. These

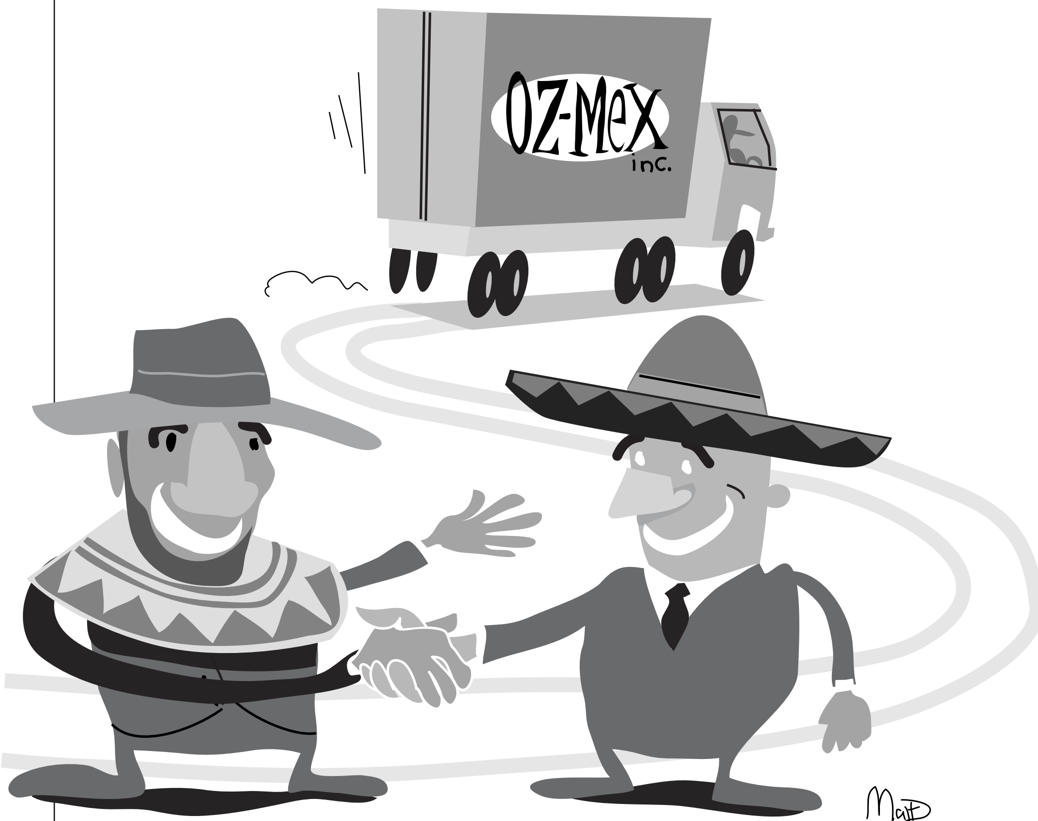
28 www.semarnat.gob.mx

have included acceptance of Australian product at Palacio de Bellas Artes in Mexico City, university circuits in regional centres, multi-arts festivals in both the Federal District and state capitals and tourist promotion centres like Cancun.

Gradually the market grew sufficiently for Macdonnell to be able to sustain involvement there for a series of one-off presentations. The big production came in 2001 when Suárez's company was appointed to manage the prestigious Cervantino International Arts Festival in Guanajuato, the most important arts event in Mexico and the largest multi-arts festival in the Americas: Australia was the focus nation. Macdonnell's company produced the program of music, dance, theatre and visual arts, literature and scholarship. The monetary value of Australian participation in this event was in the region of A$1.3 million.

"What I learn from all of this, and what I would want to pass on to anyone starting out, is that relationships must be based on realism: both sides must have the capacity to deliver consistently and over time. There are no short cuts. There is no substitute for regular face-to-face contact. When all is said and done, the arts are luxury goods. They are subject to fad and fashion and thus are always changing and are always being renewed. In the end, what I have to trade is my reputation for the delivery of quality, on time and intact."

'Strange Fruit' performing at Mexico's Cervantino Festival.


OZ-MEX
inc.

PART FOUR Contacts and Points of Reference

Useful Tips for the Business Traveller

Websites

Appendices

Index

Bibliography

The Authors

Useful Tips for the Business Traveller

The Mexican Embassy in Canberra will issue the correct visa for the purpose of the visit. Tourist visas are issued on the flight into Mexico or at the immigration counter at international arrivals in the major airports. The business visa is normally the FM-3, renewable annually for four years, but this will require some background documentation. Contact details are:

Embassy of Mexico
14 Perth Avenue
Yarralumla ACT 2600
Tel: (02) 6273 3963, 6273 3905
Fax: (02) 6273 1190
Email: embamex@mexico.org.au
www.embassyofmexicoinaustralia.org
Hours of business: Monday – Friday: 8.00 a.m. – 3.00 p.m.

Travel

While there are no direct **flights** from Australia into Mexico, the connections via the US (Los Angeles, Houston, Dallas) are plentiful and take about three and a half hours into Mexico City from these points. Its airport (Benito Juarez) is the main international airport in Mexico, but Guadalajara and Monterrey as well as the big tourist destinations all handle international traffic.

The airport-to-town trip in Mexico City should take 40 minutes to one hour, but if it is during peak hours it can take twice that time. The cost is about 120 to 140 pesos (US$13 to 15) if the **taxi** is the accredited white-and-yellow variety. These can be pre-paid in US dollars at ticket booths in the airport. Cheap and reliable are the metered green-and-yellow Volkswagen taxis, but a little caution is recommended: a risk of hailing these cabs in the street is there may already be an unsavoury passenger in it. There are also the taxis from the sitios de taxi, a slightly up-market variety, but these are without meters and a fare needs to be worked out at the start. Older model Yank tanks get a guernsey as private taxis from most of the major hotels, but they're a little dearer.

Accomodation

Most business visitors to Mexico City will wish to stay in either the Polanco area (where the Australian Embassy and Austrade are located, or in the Downtown area (Centro):

Hotels in the Polanco area include:

- Camino Real, Mariano Escobedo #700;
- The Four Seasons, Paseo de la Reforma #500;
- Nikko,Campos Eliseos # 204.

In the Downtown area there are:

- Maria Isabel Sheraton, Paseo de la Reforma #325;
- Crowne Plaza, Paseo del La Reforma #1;
- Presidente Intercontinental, Campos Eliseos #218.

For price information, reservations and other information on the above hotels and the full range of available hotels in Mexico City, Monterrey, Guadalajara and elsewhere in Mexico, the web site www.tripadvisor.com/Hotels with its search facility can be useful. This information can also be accessed through the usual search engines.

Time difference is 16 hours behind Australian Eastern Standard Time (17 in the Australian summer with daylight saving). Mexican daylight saving time runs from the first week of April to early September, when Mexico City is 15 hours behind AEST.

Tips run at ten per cent and bag-carrying should attract between 10 and 20 pesos a bag. Taxi drivers normally get no tip, unless they are particularly helpful, but supermarket check-out packers and attendants who help with car-parking should get a small amount.

Electrical power outlets provide 110-volts through US-style plugs.

Visitors may wish or may need to call on the Australian Embassy in Mexico City. The coordinates are as follows:

Australian Embassy
Ruben Dario 55
Col. Polanco
Mexico City 11580
Telephone: (52) 55 5531 5225
Fax: (52) 55 5203 8431

Websites

Information on Mexico from the Department of Foreign Affairs and Trade is available from the following internet addresses:

The latest Fact Sheet – www.dfat.gov.au/geo/fs/mexi.pdf

The latest Country Brief – www.dfat.gov.au/geo/mexico/index

The latest Travel Advice – www.dfat.gov.au/zw-cgi/advice/mexico

Latin America Desk at the Department of Foreign Affairs and Trade can be contacted at latin.desk@dfat.gov.au

For **Austrade** information on Mexico check on www.austrade.gov.au and in particular www.austrade.gov.au/ci_display/ and select Mexico in the Country window. Further links are accessible from there.

The Council on Australia Latin America Relations (COALAR) can be visited on – www.alabc.com.au/public/Coalar_frame.html

The Australia Latin America Business Council (ALABC) contains a number of useful links. Visit www.alabc.com.au

Export Finance and Insurance Corporation – www.efic.gov.au

International organisations

OECD – www.oecd.org

OECD country page for Mexico – www.oecd.org/htm/M00008000/M00008476.htm

IMF – www.imf.org

WTO – www.wto.org

The World Bank Group – www.worldbank.org

World Bank individual countries – http://www.worldbank.org/html/extdr/regions.htm#m

A resource centre on all things Mexican – www.mexconnect.com

Mexican sources

Note: Most of the information contained in these websites is provided in Spanish.

Federal Agencies

Ministry of Agriculture – *(SAGARPA)*
Tel: (52) 55-5584-8000
Website: www.sagar.gob.mx

Ministry of the Economy
– *Secretaría de Economía (SE)*, formerly the Ministry of Commerce and Industrial Development *(SECOFI)*
Tel: (52) 55-5729-9100
Website: www.economía.gob.mx
See '*Servicios, Comercio al Exterior*' for information on import permits.

General Directorate of Standards – *Direccion General de Normas*
– sets and administers the Mandatory Mexican Standards *(NOM)*. See '*Acreditación*' link for a list of laboratories accredited by Mexico to test for compliance with NOM, and '*Catálogo de Normas*' for a list of NOMs.
Website: www.economía.gob.mx/dgn1

Federal Regulatory Improvement Commission *(COFEMER)*
– includes the Federal Registry of Business Formalities, and links to individual state regulatory agencies
Website: www.cofemer.gob.mx

Ministry of the Environment and Natural Resources
– *Secretaría del Medio Ambiente y Recursos Naturales (SEMARNAT)*.
Tel: (52)55-5628-0600
Website: www.semarnat.gob.mx

Ministry of Finance and Public Credit
– *Secretaría de Hacienda y Crédito Público (SHCP)*
Tel: (52) 55-5228-2500
Website: www.shcp.gob.mx

Ministry of Foreign Relations
– *Secretaría de Relaciones Exteriores (SRE)*
Tel: (52) 55-5782-4144
Website: www.sre.gob.mx

Ministry of Health – *Secretaría de Salud (SS)*
Tel: (52) 55-5553-6888
Website: www.ssa.gob.mx

Audit and Administration Development Office – www.secodam.gob.mx

Ministry of Energy – www.energia.gob.mx

Ministry of Labour and Social Welfare – www.stps.gob.mx

Ministry of Social Development – www.sedesol.gob.mx

National Statistical Office – www.inegi.gob.mx

Mexican Institute for Social Security – www.imss.gob.mx

Federal Competition Commission – www.cfc.gob.mx

Federal Telecommunication Commission – www.cft.gob.mx

Federal Electricity Commission – www.cfe.gob.mx

Energy Regulatory Commission – www.cre.gob.mx

Mexican Petroleum – www.pemex.mx

Ports information – www.infoport.com.mx

Mexican Association of Marketing and Public Opinion Research Agencies
(Asociación Mexicana de Agencias de Investigación de Mercado y Opinión Pública)
Website: www.amai.org

Association of Mexican Private Industrial Parks – www.ampip.org.mx

Financial markets

Mexican Bank for Foreign Trade *(Bancomext)* – www.bancomext.com.mx

Bank of Mexico *(Central bank)* – www.banxico.org.mx

Institute for the Protection of Bank Saving *(IPAB)* – www.ipab.org.mx

Banking and Securities Commission *(CNBV)* – www.cnbv.org.mx

Insurance Commission *(CNSF)* – www.cnsf.org.mx

Retirement Fund Commission *(CONSAR)* – www.consar.org.mx

National Protection Agency for Users of Financial Services – www.condusef.org.mx

Mexican Stock Exchange – www.bmv.com.mx

State governments

North Region

Baja California – www.baja.gob.mx

Chihuahua – www.chihuahua.gob.mx

Coahuila – www.coahuila.gob.mx

Durango – www.durango.gob.mx

Nuevo Leon – www.nuevoleon.gob.mx

Sinaloa – www.sinaloa.gob.mx

Sonora – www.sonora.gob.mx

Tamaulipas– www.tamaulipas.gob.mx

Zacatecas – www.zacatecas.gob.mx

Central Region

Aguascalientes– www.aguascalientes.gob.mx

Distrito Federal– www.ddf.gob.mx

Mexico – www.edomex.gob.mx

Guanajuato – www.guanajuato.gob.mx

Guerrero – www.guerrero.gob.mx

Morelos – www.morelos.gob.mx

Queretaro – www.queretaro.gob.mx

San Luis Potosi – www.sanluispotosi.gob.mx

South Region

Campeche – www.campeche.gob.mx

Chiapas – www.chiapas.gob.mx

Oaxaca – www.oaxaca.gob.mx

Quintana Roo – www.qroo.gob.mx

Tabasco – www.tabasco.gob.mx

Yucatan – www.yucatan.gob.mx

East Region

Hidalgo– www.hidalgo.gob.mx – www.hidalgobusiness.com

Puebla – www.puebla.gob.mx

Tlaxcala– www.tlaxcala.gob.mx

Veracruz – www.veracruz.gob.mx

West Region

Colima – www.colima.gob.mx

Jalisco – www.jalisco.gob.mx

Michoacan – www.michoacan.gob.mx

Nayarit – www.nayarit.gob.mx

Agribusiness

Mexican Agriculture Department (SAGARPA) – www.sagarpa.gob.mx

National Cattlemen's Union – www.cng.com.mx

Secretaría de Economia – www.economia.gob.mx

Telecommunications

Telmex/Telcel– www.telmex.com

Iusacell – www.iusacell.com.mx

Alestra – www.alestra.com.mx

Avantel – www.avantelcom.mx

UNEFON – www.unefon.com.mx

Axtel – www.axtel.com.mx

Pegaso PCS – www.pegasopcs.com.mx

Mining

Mexican Chamber of Mines – www.camara-minera-mexico.com

Mineral Resources Council – www.coremisgm.gob.mx
contains geological and mining maps

Ministry of Economy – www.economia-cgm.gob.mx
Contains a comprehensive outline of developments in Mexico's mining sector, the legal framework, government priorities and strategies and information about companies operating in Mexico. Much of the information is available in English.

An interesting site about mining – www.imdex.com

APPENDICES

Australia's Trade with Mexico

A$'000		1997-98	1998-99	1999-00	2000-01	2001-02
Total exports		**215,596**	**314,438**	**253,770**	**369,893**	**478,153**
Total imports		**270,243**	**365,254**	**381,961**	**582,011**	**520,744**
Balance of merchandise trade		**−54,647**	**−50,816**	**−128,191**	**−212,118**	**−42,591**
Principal exports						
001	Live animals	16,337	10,210	10,206	17,096	31,194
011	Bovine meat f.c.f.	10,096	12,276	11,870	34,132	29,203
012	Meat (excl. bovine) f.c.f.	27,410	35,497	48,009	62,269	77,159
022	Milk and cream	15,367	12,534	4,645	33,109	26,111
023	Butter	7,500	25,480	6,488	12,721	14,224
024	Cheese and curd	6,977	8,093	8,155	13,909	13,057
054	Fresh vegetables	691	1,112	2,935	2,023	241
098	Other food products	83	1,448	2,128	4,221	1,288
222	Oil seeds & oleaginous fruits 'soft'	8,926	49,209	33,800	141	198
268	Wool	38,219	36,224	19,911	41,605	24,379
287	Other ores	0	5,145	0	6,115	0
2*	Crude materials (excl food & fuels)	751	1,891	1,557	1,562	856
321	Coal	23,083	41,350	27,158	63,202	166,985
512	Alcohols phenols phenol-alcohols	0	0	0	335	5,770
542	Medicaments (incl. veterinary)	784	1,045	2,373	3,107	2,354
582	Plastic plate sheet film & strip	1	28	59	84	4,839
592	Starches inulin & wheat gluten	6,086	6,873	9,000	13,530	13,133
5*	Chemicals & related products	1,345	2,505	2,626	1,495	1,911
65	Textile yarn & fabrics	1,305	805	966	579	481
676	Iron & steel bars rods shapes	2,040	1,684	689	80	8
685	Lead	154	461	7,152	0	0
6*	Manufactures classified by material	1,145	875	1,372	376	1,128
721	Agricultural machinery (excl. tractors)	3,516	889	3,070	805	1,226
723	Civil engineering equipment	1,014	1,204	1,366	2,361	1,155
727	Food-processing machines	1,055	2,014	85	225	3,329
728	Specialised machinery	5,972	6,734	2,960	2,832	1,099
731	Lathes	3,565	2,791	0	548	136

* denotes remainder of classification

748	Transmission shafts parts	1,722	1,189	1,703	1,691	1,080
74*	General industrial machinery	1,015	1,863	2,370	2,208	3,763
764	Telecommunications equipment	392	7,217	2,705	492	523
772	Electrical equipment for circuits	3,416	799	266	842	1,849
778	Other electrical machinery	890	85	5,628	1,810	126
784	Motor vehicle parts	80	303	1,360	10,206	9,925
7*	Machinery & transport equipment	1,493	1,785	3,191	7,232	4,738
874	Measuring and controlling instruments	2,877	2,885	2,968	2,709	1,958
89	Miscellaneous manufactured articles	382	325	1,599	806	798
8*	Miscellaneous manufactured articles	600	1,806	774	1,831	3,475
988	Confidential items	18,234	27,275	22,384	20,435	24,903
	Other	1,073	528	246	1,172	3,556
Principal imports						
058	Preserved fruit and preparations	5,200	6,846	6,379	5,947	5,074
05*	Vegetables & fruit	2,581	2,535	3,485	3,601	3,741
0*	Food & live animals	3,672	2,122	2,527	2,641	2,685
112	Alcoholic beverages	9,340	9,381	9,849	16,845	17,953
222	Oil seeds & oleaginous fruits 'soft'	4,130	3,968	3,297	3,838	3,175
287	Other ores	0	2,699	0	0	0
29	Crude animal & vegetable matter nes	1,275	2,028	3,217	2,150	2,260
515	Organo-inorganic compounds	1,620	1,210	837	1,070	8,402
51*	Organic chemicals	2,422	1,513	1,229	1,550	1,174
522	Inorganic chemical elements	7,607	4,887	72	4,637	2,554
523	Metallic salts & peroxysalts	11,891	5,720	4,864	652	8,612
532	Dyeing & tanning extracts	2,140	2,230	1,801	1,425	84
533	Pigments paints varnishes	6	143	57	3,971	7,838
541	Medicinal & pharmaceutical products	4,443	3,116	1,345	1,789	1,572
542	Medicaments (incl. veterinary)	571	3,144	4,731	19,074	28,159
562	Fertilizers (excl. crude)	17,955	37,523	24,925	53,358	109
598	Miscellaneous chemical products	1,391	6,703	6,741	11,434	12,634
5*	Chemicals & related products	4,389	2,527	3,545	4,179	7,570
642	Paper manufactures	1,466	2,187	3,158	3,253	1,704
657	Special yarns and textile fabrics	1,655	2,698	3,002	2,098	822

* denotes remainder of classification

65*	Textile yarn & fabrics	4,842	4,915	6,853	7,699	7,791
66	Non-metallic mineral manufactures	2,630	2,903	3,214	4,220	3,772
679	Tubes pipes & fittings of steel	3,389	249	25	121	4,363
696	Cutlery	5,404	7,862	9,643	11,445	6,574
69*	Manufactures of metals nes	2,332	3,451	4,104	5,152	4,792
741	Heating & cooling equipment	7,132	6,081	6,884	2,194	2,583
744	Mechanical handling equipment	2,886	4,959	6,213	6,497	5,049
74*	General industrial machinery	3,812	2,999	2,731	8,387	9,830
752	Computers	40,350	82,355	36,928	25,723	38,712
759	Computer parts	8,519	19,942	27,176	28,066	42,430
762	Radio-broadcast receivers	188	1,707	7,292	9,458	6,112
764	Telecommunications equipment	9,865	10,890	49,832	163,425	115,931
771	Electric power machinery	2,783	2,043	742	2,388	1,820
772	Electrical equipment for circuits	2,138	4,479	3,968	5,190	5,023
774	Medical electro-diagnostic equipment	3,480	6,717	7,325	6,181	4,524
775	Household type equipment	2,414	3,296	1,530	1,257	1,665
776	Integrated circuits	1,727	4,228	2,609	2,027	2,030
778	Other electrical machinery	3,005	3,911	3,802	5,674	8,573
781	Passenger motor vehicles	17,024	12,579	21,818	55,211	29,103
784	Motor vehicle parts	2,031	6,459	12,235	23,126	34,197
7*	Machinery & transport equipment	4,821	4,905	4,070	7,952	9,891
84	Clothing	2,518	5,309	4,845	5,245	5,090
851	Footwear	2,306	2,307	2,290	593	35
872	Medical instruments	7,095	4,771	4,484	4,901	6,682
874	Measuring and controlling instruments	4,009	3,727	4,023	3,622	6,498
882	Photographic supplies	14,557	12,931	16,622	10,819	8,940
893	Other articles of plastics	1,351	1,898	3,255	2,433	1,743
894	Toys games & sporting goods	6,586	5,963	6,570	8,187	5,785
898	Musical instruments	6,585	12,679	20,453	6,419	5,445
899	Miscellaneous manufactures	3,211	3,557	3,754	4,941	5,697
89*	Miscellaneous manufactured articles	2,642	3,527	3,111	3,054	4,475
8*	Miscellaneous manufactured articles	3,020	3,145	3,607	3,607	4,878
	Other	1,844	5,329	4,896	3,285	4,592

* denotes remainder of classification

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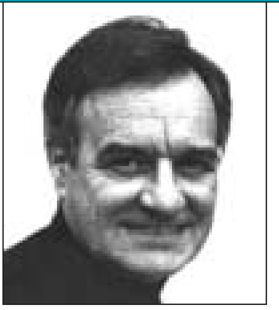
The Authors

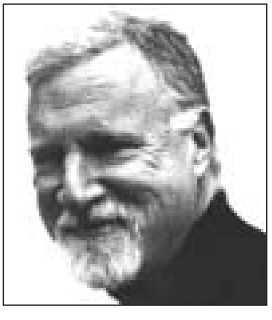


Frank Unger

Frank Unger is an executive with over 25 years' experience in international business development and diplomacy. Ten years were on location overseas matching products, markets and companies and providing advice, support and business to hundreds of companies.

Frank's international business facilitation skills were developed as an Australian Trade Commissioner, as Commissioner for the Government of Victoria and, since 1996, as Managing Director of frank advice (international) pty ltd.

He is a Fellow of the Australian Institute of Company Directors (FAICD) and is the author of *Australia-Germany: Advancing Global Enterprise* published in 1999.



Roger Frankel

Roger Frankel has a strong record of commercial success in Latin America. He is a former career diplomat and in his most recent assignment, from January 1996 to March 2000, was Australian Ambassador to Venezuela, Colombia, Ecuador and the Dominican Republic.

Born in Brazil, Roger is a fluent speaker of Portuguese and Spanish and has a unique awareness of how to achieve commercial success in Latin American markets.

As a Director of frank advice (international) pty ltd he is placing is experience, skills and networks in Latin America at the service of Australian businesses and governments.