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SEPTEMBER | 2023

Mexico's nearshoring potential: Weighing opportunities and risks

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“Two basic rules of life are: 1) Change is inevitable. 2) Everybody resists change.”

– W. Edwards Deming

To say the past three years have been challenging is an understatement. Supply chains were exposed, causing constant and frequent disruptions. We continue to see many markets return to a higher level of normalcy, but there continues to be a sense of trepidation. What have we learned in the past three years? What can be done differently to build more impactful risk mitigation and resilient supply chains? One possible solution is nearshoring. I invite you to continue reading to explore the potential opportunities and risks of nearshoring in Mexico.

CRITICAL MINERAL IN FOCUS

Mexico is a particularly strong fit for the critical minerals and rare earth elements sector based on the current US regulatory environment focused on reducing dependency on mainland China supply chains. Since 2019, the U.S. Department of Defense has identified more than 50 strategic and critical minerals for which the country was import-reliant. Mexico is among the top three suppliers of 14 of these minerals—and is currently the US's largest supplier of fluor spar, strontium, and gold. Mexican production of most of these minerals has risen in the past five years providing the country the opportunity to increase its market share of US imports, particularly for minerals coming from mainland China such as graphite, lead, and selenium, and integrate these minerals into other critical US supply chains such as pharmaceutical and semiconductor manufacturing. The Mexico mining sector does face numerous risks including organized criminal activity, civil unrest, and contract concerns. Of these, only contract risks are likely to diminish in the five-year outlook once the current government changes after the election season in 2024.

HIGH CAPACITY BATTERY ASSESSMENT

The nearshoring trend to Mexico in the high-capacity battery supply chain has reached a transformative inflection point, propelled by a confluence of global disruptions and shifting market dynamics. Recent surveys, such as the one conducted by Capterra, reveal a remarkable paradigm shift, with a staggering 74% of U.S.-based small and medium-sized businesses (SMBs) planning to overhaul their supply chains by favoring suppliers in the U.S. or Mexico in 2023. This rapid and unprecedented transformation has exceeded earlier predictions, as the industry transitions at an astounding pace.

Current Supply Chain Landscape:

While Mexico's current mineral production only encompasses manganese, its strategic advantages in proximity to the U.S., robust transportation infrastructure, and conducive business environment make it an irresistible magnet for nearshoring endeavors. With the United States-Mexico-Canada-Agreement trade pact reinforcing cross-border trade ties, Mexico has emerged as a focal point for supply chain diversification and expansion.

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Opportunities in Nearshoring for High-Capacity Battery Supply Chain:

1. **Strategic Geographical Proximity:** Mexico's adjacency to the United States serves as a pivotal gateway to North American markets, facilitating seamless logistics and just-in-time deliveries. Companies can harness this geographical advantage to minimize costs and optimize supply chain efficiencies.
2. **Abundant Skilled Workforce and Cost-Effectiveness:** Mexico boasts a highly skilled labor force, abundant in technical expertise, and with competitive labor costs, making it a compelling choice for establishing manufacturing facilities. This workforce advantage enhances production efficiency, ensuring heightened cost-effectiveness and competitive edge.
3. **Sustainable Growth through Green Technology:** Mexico's concerted efforts to align with green technology trends, buoyed by incentives from progressive legislations such as the Infrastructure Investment and Jobs Act of 2021 and the Inflation Reduction Act of 2022, present a unique opportunity for the production of eco-friendly high-capacity batteries.
4. **Mitigating Supply Chain Risks:** As businesses continue to navigate through a volatile global landscape, nearshoring to Mexico offers a strategic solution to mitigate risks associated with long and complex supply chains. By embracing localized manufacturing, companies can enhance supply chain resilience and adaptability.

Risks and Considerations:

1. **Addressing Critical Mineral Shortcomings:** To unlock Mexico's full potential, companies must address the challenge of limited critical mineral production, particularly lithium. Proactive measures such as exploring diverse sourcing options or forging strategic partnerships will be instrumental in securing a stable supply of critical minerals.
2. **Navigating Regulatory Dynamics:** Mexico's evolving high-capacity battery sector necessitates a comprehensive understanding of the regulatory landscape. Businesses must remain agile and responsive to potential changes, ensuring compliance and optimizing operational strategies.

Conclusion:

The nearshoring potential of Mexico in the high-capacity battery supply chain represents a game-changing opportunity for businesses seeking to revolutionize their operations and establish dominance in the U.S. market. With its strategic advantages, Mexico has transcended expectations and emerged as a premier nearshoring destination, accelerating industry transformation. By capitalizing on Mexico's strengths in geographical proximity, skilled workforce, and green technology incentives, companies can usher in a new era of sustainable growth and resilience. Furthermore, addressing critical mineral challenges and navigating the regulatory terrain will be instrumental in unlocking Mexico's full potential as a high-capacity battery powerhouse. The current momentum towards nearshoring signifies an extraordinary juncture for industry leaders to seize opportunities, surmount challenges, and cement Mexico's position at the forefront of the dynamic and burgeoning high-capacity battery industry.

INFRASTRUCTURE AND LABOR

Infrastructure and labor are two key components bringing both headwinds and tailwinds to the efforts of nearshoring. Mexico's infrastructure is well ahead of its other Latin American peers; however, sustained investment is necessary.

Foreign Investment generally goes to northern Mexican states that border the U.S. or to Central Mexico. The current government policy has made attempts to encourage investments in southern Mexico – which are the poorest and have the least connected infrastructure. This misalignment is likely to persist through the next few years – challenging nearshoring efforts to bring manufacturing to the Central and Northern states.

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Labor costs in Mexico present tailwinds on the surface level – peel this back a layer and consider potential headwinds. While the hourly manufacturing labor rate of \$4.90 is much less than that within the US at \$30 – Mexico has realized sustained wage growth that has outpaced inflation. In 2022, a 20% increase in the minimum wage was implemented. Additionally, the government has approved pension reforms that increase employer contributions – which may further pressure operations costs upward.

The overall outlook for Mexico in the next five years is optimistic; however, there are operational, security, and policy risks that pose significant headwinds to firms considering relocating nearer to the US market. Elections coming in July 2024 may improve the business environment; this in turn may improve the investment and economic outlook. How the government will minimize the security and operational risks over time is yet to be understood; however, this will be an important hurdle to overcome as organizations look to fully realize the benefit of nearshoring.

RELATED ARTICLES

- a. [Survey: Nearshoring to Mexico happening 'faster than expected' - FreightWaves](#)
- b. <https://www.visualcapitalist.com/charted-americas-import-reliance-of-key-minerals/>
- c. [As Nearshoring Takes Off, Here's How SMBs Can Shorten Their Supply Chains | Capterra](#)
- d. [Labor Rates In Mexico - Lower Operating Expenses | Mexican Labor Rates \(ivemsa.com\)](#)
- e. [Regionalized supply chains: the key to resilience | CSCMP's Supply Chain Quarterly](#)
- f. [Nearshoring trend sparks demand for logistics real estate in Mexico | CSCMP's Supply Chain Quarterly](#)
- g. [Nearshoring trend shifts trade lanes from China to Mexico, FourKites says | CSCMP's Supply Chain Quarterly](#)
- h. [The Defense Department's Strategic and Critical Materials Review > U.S. Department of Defense > Release](#)