

Moving Forward: Ground Transportation in Mexico

Transportation & Logistics

Author: John Price

When Hernán Cortés returned to Spain after his first expedition to the Aztec nation (encompassing much of modern Mexico and parts of the Southwestern US), the King asked him to describe the exotic terrain of the new world. Cortés took a piece of amate (paper made from a thin bark) and crumpled it into a wrinkled ball. He explained how the parallel obstacles of the Occidente and Oriente Sierra mountain chains made it nearly impossible to cross "New Spain" from East to West.

Five hundred years later, transportation companies still struggle with the challenges of moving products across Mexico. The country's railway lines were built running north-south to transport silver and other minerals. East-west lines were always deemed economically impractical. Today, it takes longer to drive a truck from Mexico City to Tijuana than from Mexico City to Toronto, Canada. Per mile trucking rates are nearly double those in the US. This is the result of several factors, not the least of which is geography.

Mexico - Texas Rail Car Crossings

Year	1995	1996	1997	1998	1999	2000	CAGR
Texas to Mexico	155,918	199,632	235,515	237,395	272,405	298,919	13.9%
Mexico to Texas	95,497	144,545	145,112	145,277	172,874	205,750	16.6%
TOTAL	253,410	346,173	382,624	384,670	447,278	506,669	14.9%

Source: Texas A&M

Tendencias is Brought to you by

Latin America's Business
 Intelligence Leader

INFOAMERICAS

© 1998 - 2007 all rights reserved

www.infoamericas.com

Free Trade Drives Transportation Privatization and Modernization

When Mexico signed onto free trade, both its trucking and rail systems were in shambles. The government-operated rail system, with its archaic union relationships, antiquated technology, and history of low investment, was not fit to move anything other than bulk commodities like mineral ore that were not time-sensitive. Mexico's trucking system was laden with small inefficient operators, none of which could offer national coverage. Large retailers and manufacturers preferred to operate their own fleets rather than rely on trucking companies.

Mexico - Texas Truck Crossings

Year	1995	1996	1997	1998	1999	2000	CAGR
Texas to Mexico	909,266	1,063,643	1,268,229	1,942,091	2,093,370	2,255,987	19.9%
Mexico to Texas	739,981	923,875	959,379	1,047,949	2,291,929	2,410,231	26.6%
TOTAL	1,651,242	1,989,514	2,229,605	2,992,038	4,387,298	4,668,218	23.1%

Source: Texas A&M.

The privatization of Mexico's rail lines attracted both investment and knowledge. The north-south configuration of the lines make them well suited for cross-border traffic but less so for intra-Mexico cargo movement. The sales efforts of the leading operators have helped rail to capture substantial volumes of cross-border tonnage from trucking, especially in the automotive, fruit, and beverage sectors. Rail has also picked up some new products that it did not handle prior to privatization, including appliances, electronics and related parts.

Selected Mexican Exports by Transportation Mode

Metric Tons - 2000

Product	Rail	Truck
Cars and car parts	63.4%	36.6%
Electronics and parts	1.5%	98.5%
Machinery and appliances	9.2%	90.8%
Articles of iron and steel	7.1%	92.9%

Source - US Rail Association

Tendencias is Brought to you by

Latin America's Business
Intelligence Leader

INFOAMERICAS

© 1998 - 2007 all rights reserved

www.infoamericas.com

Cross-border trucking has exploded in Mexico thanks to its 18 percent annual growth rate of US-Mexico trade since 1995, which is three times the growth rate of global trade. The NAFTA provided the impetus for significant new investment in trucking equipment and also drove industry consolidation. Today, nine major US trucking companies operate in Mexico, although they continue to be restricted because of delays in the implementation of the NAFTA regulations that govern cross border trucking.

Major US Trucking Companies in Mexico

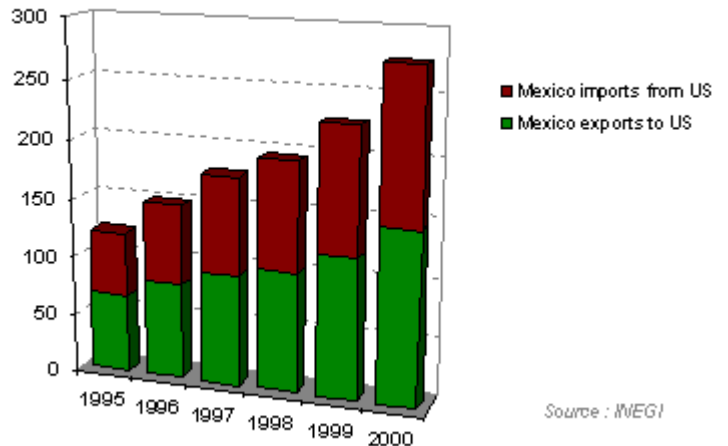
- Alliance Shippers, Inc.
 - American President Lines
 - Atlas Van Lines, Inc.
 - Celadon Trucking Services, Inc.
 - Consolidated Freeways
 - Mark VII Global Transportation & Logistics Solutions
 - MS Carriers
 - Schneider National
 - Yellow Freight
-

Source - American Chamber of Commerce in Mexico

Consolidated Industry Demands More Outsourced Trucking Services

As Mexican retailing has modernized and consolidated, so have the supply channels. Corporate re-engineering following the debt and Peso crisis of 1995 led to divestiture of large internal trucking fleets. The result was a sudden demand for truly national and international trucking services that combined logistics and warehousing and guaranteed timely delivery and product safety. Only the largest players could deliver such a service. These trends will continue and Mexico's small

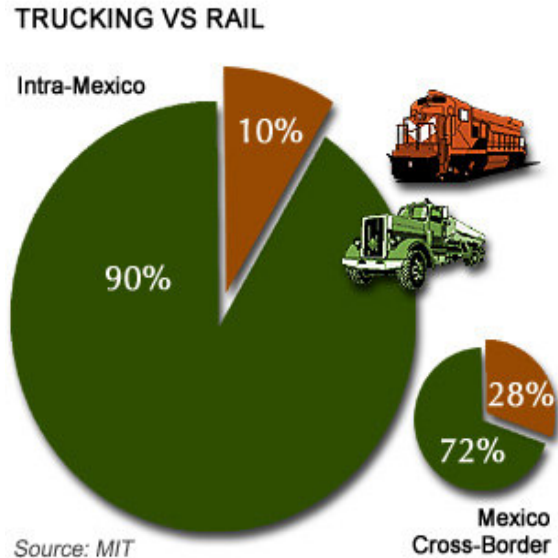
US - MEXICO TRADE
billions of US dollars



Source : INEGI

to mid-size carriers will lose further ground to the larger operators.

Trucking, and to a lesser degree rail, suffers high levels of theft. According to the Mexican Association of Insurance Companies (AMIS) transport insurance providers paid trucking losses at an incident rate of 78 percent in 1997 (i.e. 78 percent of insured trucks made an insurance claim for theft). This rate reached 93 percent in 1999, making insurance costs one of the biggest challenges facing trucking firms. Insurance premiums (and presumably) product loss can be reduced through the implementation of GPS tracking systems. At \$2,000 per truck, these systems are limited mainly to larger carriers. Smaller independent truck operators pay comparatively high premiums or ride without insurance. Rail faces similar problems. Fully assembled automobiles bound for the US market often arrive without the radio, which disappears somewhere along its rural passage in Mexico. To compensate, Chrysler now prefers to install its radios in the US after the car arrives. In spite of these specific problems, merchandise theft for rail transportation is less than 10 percent of that for trucking.



As the Mexican economy continues to consolidate under the pressures of free trade and modernization, larger scale and increased specialization increases the need for cost effective transportation. When Mexican industry in the center of the country was devastated by cheaper and better made US imports, new manufacturing investment shifted to northern Mexico where producers could more readily service the US market. Now, industry is moving south again, away from the relatively costly border towns. This avoids some of the costs of success faced in the north, including water and power shortages, high labor turnover and expensive real estate. Mexico's newest factories are focused on more than just exports. They take advantage of the NAFTA, but are designed to service both Mexican and American customers. As a result, proximity to rail lines has become a big consideration in plant location for the first time.

Private Investment Needed to Overcome Bottlenecks

Cross-border trucking grew by more than 30 percent per year from 1998 to 2000, thanks to the trade boom. This sudden growth doubled delays at border crossings, particularly Laredo, which handles 25 percent of Mexico's cross border truck traffic. Within Mexico, rail lines operate at less than 30 percent capacity while the freeways are considered 55 percent saturated in terms of trucking capacity.

Further hampering the trucking business is the US reluctance to open its border to Mexican trucks. In their first meeting in Mexico, Presidents Bush and Fox promised to begin compliance with the NAFTA, which called for open borders to be implemented immediately. But the American government now wants to limit Mexican trucks that do not pass strict emissions standards. It looks likely that the cross border market will remain restricted for the foreseeable future because of the political conflict. This also means that plans to allow increased foreign ownership of Mexican trucking companies will be further delayed. In reality, few Mexican trucks would bother to drive into the US because of the state laws that demand that trucks carry a license plate for each state they serve. Likewise, many US truckers are not ready to risk travel in Mexico where roads are in poor shape, gasoline is expensive and theft rates are high. Moreover, US insurance companies still have not figured out how to extend their policies to Mexico for their US trucking clients.

In 2000, Mexican rail traffic reached 68 million tonnes, still less than the peak of 71 million tonnes in 1983. Its potential for growth is greater than trucking but the difficulties it faces have attracted fewer interested solution providers. At present, Mexican rail can compete only on long hauls because of the large fixed costs of terminal operations. Improving the availability and efficiency of inter-modal facilities would help rail to compete on shorter runs. Even then, however, massive private sector investments will be required to overcome bottlenecks in the rail infrastructure, especially those at bridges and steep inclines.

Market Opportunities

Even with the slowdown in both the US and Mexican economies, cross-border traffic will continue to grow at between 10 and 12 percent annually over the next three years. Intra-Mexican transport will likely grow at about 8-to-10 percent per year over the same period, as Mexican industry consolidates further and average transport runs grow longer. The expansion of logistics, warehousing and transportation services is also driven by the realization by mid-size manufacturers and retailers that these services are easier, and in the long run cheaper, to outsource than to maintain in-house.

Rail and trucking will both continue to attract considerable foreign investment. Mexico's rail concessionaires are expected to spend \$230 million per year on new equipment. If the call for more private investment in rail infrastructure is heeded, then further privatizations may be forthcoming for new lines, tunnel expansions, bridges, and other improvements. Meanwhile, US trucking companies will continue their toe-first entry into Mexico. The favored strategy at the moment is the use of leasing companies that sub-contract with Mexican trucking firms as a way of skirting the foreign ownership restrictions still in place because of the cross-border dispute. Meanwhile, Mexico's sizeable list of large trucking firms will step up investment heavily over the next 12 months while the peso remains strong, making new equipment more affordable.

Tendencias is Brought to you by

Latin America's Business
Intelligence Leader

INFOAMERICAS

© 1998 - 2007 all rights reserved

www.infoamericas.com