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Nearshoring Manufacturing and De-Risking Global Supply Chains

Part 2: Nearshoring to Mexico – Operating Cost vs. the US

For most executives facing the decision to move production out of the U.S. and into Mexico, the relocation typically results in considerable savings on the labor cost side and in moderate reductions in real estate-related cost. Utility and logistics costs are typically higher than when operating at a location in the U.S. This article aims to shine a light on what costs to expect and potential savings versus comparable U.S. operations. The largest operational cost drivers are labor, real estate and utilities, combined with USD/MXN exchange rates, when moving operations into Mexico.

> ***Cost savings with relocation to Mexico are typically in labor (considerable) and real estate (moderate). Utility and logistics costs are typically higher than in U.S. locations.***

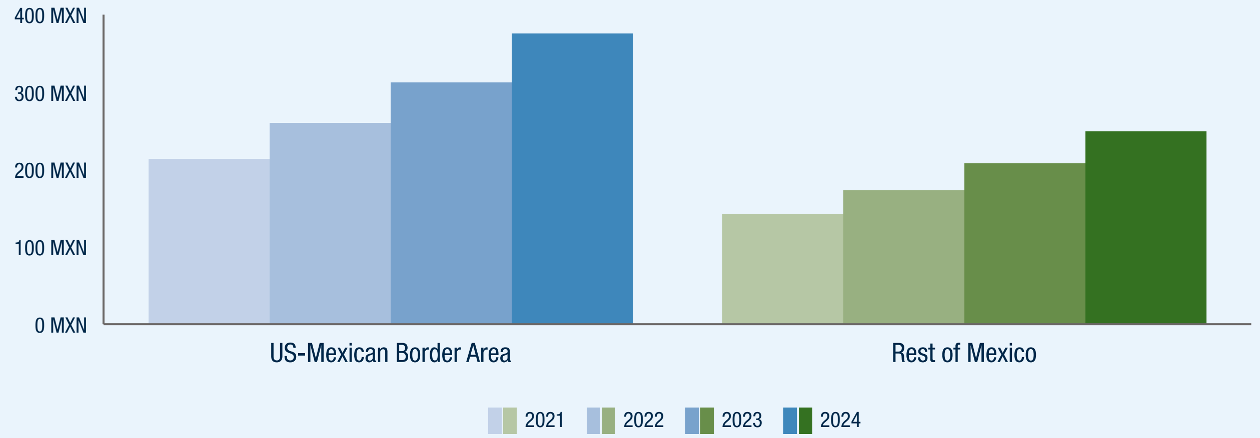
Labor

The labor cost difference between the U.S. and Mexico varies widely depending on the labor type involved. In general, the higher the employee's skill level, the lower the cost savings potential. In addition, considerable cost differences exist between areas close to the U.S. border (classic "maquiladora" locations), metropolitan areas with a strong industrial base (e.g., Queretaro, Guadalajara, Monterrey, Mexico City), and less developed regions in the south and other areas of the country.

Direct Labor:

Alvarez & Marsal's experience shows that for transfers of direct labor, around 70 percent to 80 percent of the U.S. cost can be saved, depending on the respective U.S. and Mexico locations compared. The bottom of wages typically paid to unskilled, entry-level workers is defined by the legal minimum wage, which is ~$375 MXN per day ($21.80 USD, or $2.73 USD per hour) for the border region and ~$250 MXN ($14.53 USD, or $1.82 USD per hour) for the inland areas. (Note that the typical Mexican work week is six days of work at eight hours per shift.) Higher skilled hourly positions may reach up to 150 percent or more of minimum wage. The table below shows the considerable increase of the minimum wage in the past years:

Minimum Daily Wage in Mexico From 2021 to 2024 (MXN)



Source: Minimum daily wage in Mexico from 2021 to 2024; statista.com

On top of wages, benefits paid to workers typically amount to 100 percent to 120 percent of base wage; they range widely from contributions to health insurance, transportation and meal subsidies, to special payments for life events, (modest) scholarships, cost of living add-ons, etc. Including benefits, fully burdened labor cost for direct labor can be between ~$3.60 USD for lower skilled positions inland, to ~$6.00 USD or more for higher-skill hourly manufacturing positions in high-cost areas.

Indirect Labor:

Typical savings for indirect labor, be it hourly or salary, are between 40 percent and 60 percent versus the U.S. Positions in this class include engineers, tool makers, lab personnel, quality-related functions, maintenance personnel, and other manufacturing support roles. English-speaking personnel enjoy a premium in pay at companies that have international exposure. Labor cost in Mexico can vary due to the wide variety of skill sets and education levels. The table below illustrates a few examples of annual wages/salaries and labor cost levels that A&M encountered during recent project work:

Wages by Position in Mexico

Position	Typical Wages/ Salaries (in $MXN; p.a.)	Typical Wages/ Salaries (in $USD; p.a.)	Total Labor Cost (incl. benefits; $MXN; p.a.)	Total Labor Cost (incl. benefits; $USD; p.a.)
Material Handler	100k – 150k	6k – 9k	150k – 260k	9k – 15k
Forklift Driver	120k – 150k	7k – 9k	180k – 260k	10k – 15k
Quality Inspector	120k – 150k	7k – 9k	180k – 260k	10k – 15k
Maintenance Tech.	180k – 280k	11k – 16k	270k – 480k	16k – 28k
Prod. Supervisor	200k – 300k	12k – 18k	300k – 510k	17k – 30k
Buyer/Planner	250k – 450k	15k – 26k	375k – 770k	22k – 45k
Quality Engineer	250k – 450k	15k – 26k	375k – 770k	22k – 45k
Engineer (Entry)	200k – 300k	12k – 17k	300k – 510k	20k – 32k
Engineer (Senior)	400k – 600k	23k – 35k	600k – 1M	45k – 58k

Source: A&M experience; actual client examples. 2024 exchange rate of 17.2 MXN/USD. Values shown are rounded.

The benefits load in Mexico is higher than the U.S., typically between 50 and 70 percent of salaries/wages paid, with diminishing percentages as overall pay and skill levels increase.

Executive/Leadership Positions:

For executive positions (general managers, plant managers, etc.) the labor cost is often comparable to what is paid in the U.S., due to the "globalized" nature of the positions (NAFTA). Plant managers and other senior plant leaders in Mexico are well-compensated for their critical role in overseeing manufacturing operations. Typically, plant manager salaries for a smaller local plant start at around $70,000 MXN (~$4,000 USD per month); however, companies often arrange to transfer Spanish-speaking U.S. residents to lead their Mexican plants or seek out other highly qualified individuals on the open international market, which can lead to compensation that is often double to triple of that or more. These figures, of course, vary based on the size of the plant, the industry and the manager's experience. Additionally, plant managers often receive extra cash compensation, which can range from 15 percent to 50 percent of base salaries.

> ***General managers and plant managers in Mexico are often paid U.S.-level salaries.***

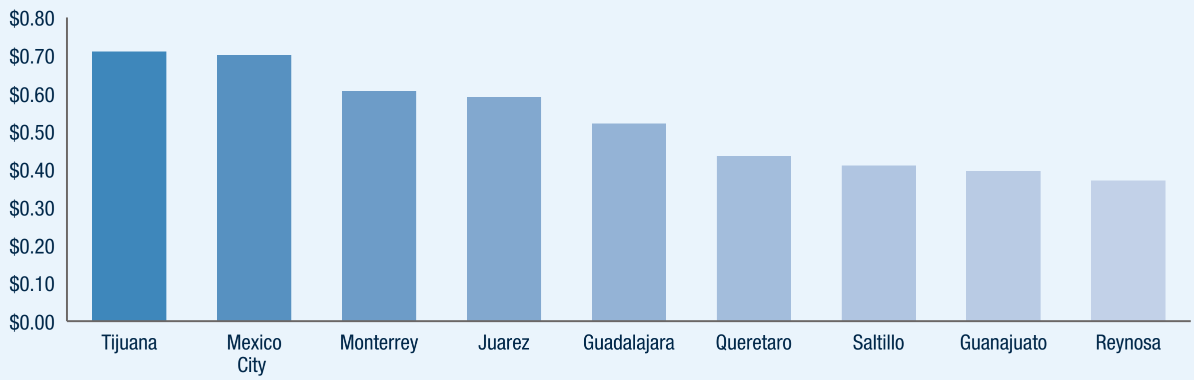
On the benefits side, typical arrangements include comprehensive health coverage as a standard benefit, ensuring that managers and their families have access to quality medical care. Frequent are contributions to retirement plans, bonuses and additional benefits such as company cars, housing allowances and opportunities for professional development.

Real Estate

Due to reshoring and investment activity, the market for commercial and industrial real estate is experiencing shortages and is subject to increasing prices. When embarking on a nearshoring effort into Mexico, given competition and market shortages, the most viable method is to secure a suitable building in the form of a build-to-suit facility in an industrial park that is under development. In this way, specific needs can be considered: utility hook-up is somewhat standardized between all industrial park occupants, and security is part of the rent cost and provided by the landlord.

Typical lease prices are comparable to mid-value American locations, with prices being higher close to the U.S. border and in prosperous industrial centers, while lower in further-away southern areas. The graph below shows average 2023 industrial property lease cost for select areas within Mexico.

Industrial Property – Monthly Lease Cost (Q1 2023; USD per Sq. Ft.)



Source: Annual asking rent for industrial and logistics real estate in Mexico in 1st quarter 2023, by market; statista.com

Please note that above prices are averages; several factors influence the cost of leasing industrial buildings in Mexico:

Proximity to the U.S. Border: Cities closer to the U.S. border, such as Tijuana, Monterrey and Ciudad Juárez, tend to have higher leasing costs due to their strategic location for export-oriented businesses.

Infrastructure: Regions with better infrastructure, including transportation networks and utilities, command higher leasing rates.

Demand and Supply: High demand for industrial space in key markets drives up leasing costs. Conversely, regions with higher vacancy rates may offer more competitive leasing rates.

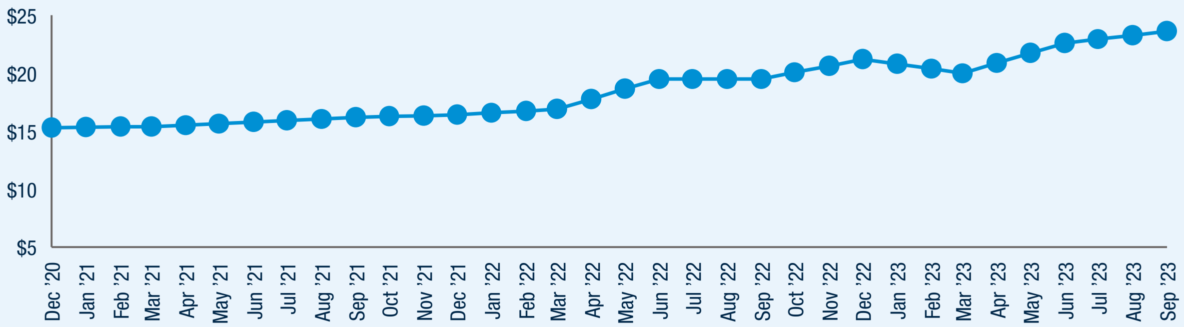
Industry Focus: Cities with a strong presence in specific industries, such as automotive in Saltillo or technology in Guadalajara, may have higher leasing costs due to specialized infrastructure and workforce availability.

Property Quality: As within every other country in the world, the quality ("class") of the property in question strongly impacts lease asking price. Foreign companies in Mexico tend to lease higher-quality facilities to assure safety and attractiveness (both for international customers and local work force). Class A buildings can cost up to 50 percent more than Class B or C facilities, even if located near to each other.

Utilities

With the U.S. providing manufacturer-friendly cost for electricity (except some states in the Northeast and California), industrial electricity cost is typically between $0.08 to $0.15 per kWh. As a comparison, average businesses in Mexico pay $0.15 to $0.25 per kWh, depending on the specific location within Mexico, usage patterns and overall volume. Note that rates can also vary significantly from industrial park to industrial park even within the same city.

Mexican Electricity Cost per kWh, Industrial (USD)



Source: Average electricity prices for enterprises in Mexico; statista.com

That said, electricity prices in Mexico are still competitive compared to other international locations. For example, in Europe, prices reach up to $0.40 per kWh, depending on the country. On the other hand, energy prices continue to increase in almost every part of the world, including Mexico.

While access to electricity is — assuming a little bit of patience in the initial hookup phase — available across the country, the situation with natural gas can be trickier due to limitation of direct access in various areas within the country. If the planned facility is expected to be a large consumer, it is wise to make access to natural gas (and proximity to pertinent pipelines) a must-have criterion for site selection.

Another factor to take into consideration is that initial hookup and setup can take a long time. A&M has seen long delays in connecting facilities to the grid leading to the need to bridge transition with the help of expensive diesel generators. Working with well-connected and experienced real estate developers or moving into a well-established industrial park can shorten initial hookup and setup times.

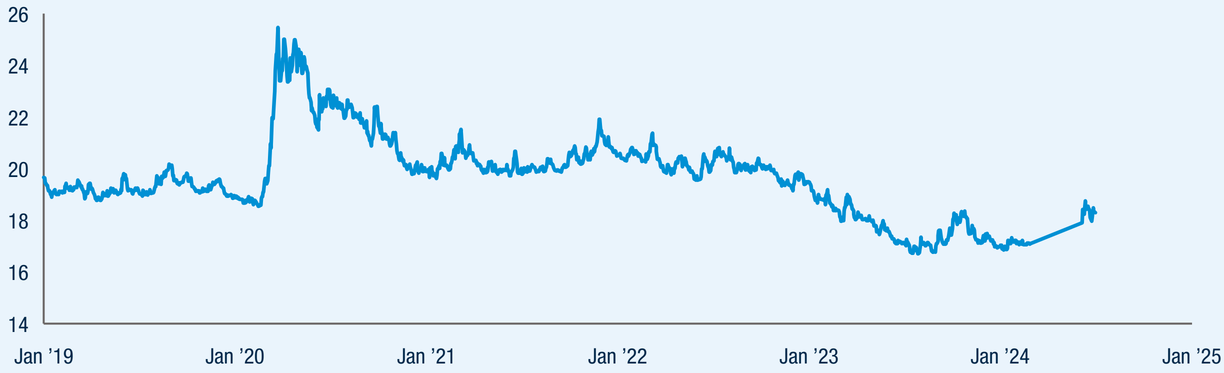
Transportation

The proximity of Mexico to the U.S. drastically reduces delivery lead times and costs compared to other offshoring destinations. This allows for lower inventory levels, further reducing risk and improving responsiveness to market changes. The cost to bring a truck trailer from a border location in northern Mexico to the U.S. is around $250 to $500 USD and will take less than a day, compared to ocean freight from, e.g., Southeast Asia, which can take up to several weeks to arrive.

Currency Exchange Rate Fluctuations and Impact

COVID and other macroeconomic trends have put the relationship between the Mexican and U.S.-American currencies into a historically unique position: For the first time in recent history, the U.S. dollar has continued to lose value uninterruptedly for almost four years, from a peak in early 2020 of more than $25 MXN per dollar, to early 2024 at below $17 MXN. The U.S. currency seems to have recovered a bit since then, hovering between $19 MXN and $20 MXN as of October 2024. Given continued large in-bound investment volumes and higher interest rates on the Mexican side, it is not clear if the USD will regain value in the upcoming years to reach 2020 heights soon again.

USD/MXN Exchange Rate 2019 to 2024 (MXN per USD)



Source: Macrotrends (macrotrends.net)

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The strong domestic currency in combination with inflationary forces (mainly labor cost increases) have led to Mexico-based manufacturers having to fight headwinds on two fronts. This situation is illustrated by showing minimum wage cost development (for northern border territory) in MXN and USD, as shown in the table below:

Daily Minimum Wage Mexico (Mar 2020 – Mar 2024): MXN versus USD

Time	Minimum Wage (in $MXN; p.a.)	Increase in MXN	Exchange Rate (USD/MXN)	Minimum Wage (in $USD; p.a.)	Increase in USD
March-20	185.56		23.7871	7.80	
March-21	213.39	15.0%	20.4307	10.44	33.9%
March-22	260.34	22.0%	19.8703	13.10	25.4%
March-23	312.41	20.0%	18.0165	17.34	32.3%
March-24	374.89	20.0%	17.0986	21.93	26.4%

Source: macrotrends.net; A&M calculations

While costs in domestic currency have increased by slightly more than 100 percent in the last four years, costs in USD have almost tripled.

Outlook

The decision of which country to target when considering a move to a low-cost country has never been more complicated than today. While most options still secure access to a lower-cost labor pool, import taxes, supply chain considerations, transportation costs, security concerns and political changes muddy the picture.

The lower average cost of manufacturing in Mexico (versus the U.S.), the country's membership in United States-Mexico-Canada Agreement (USMCA), and relative ease in transportation are compelling arguments to choose Mexico as a destination for manufacturing investments. On the other hand, open questions in terms of security (organized crime), political stability, changes to the electricity/utilities sector, and future development of labor costs make the decision less clear-cut than it was in the past. With the new government elected, it seems that the policy of aggressively pushing for higher minimum wages and worker rights of the previous government will continue, or even accelerate, further driving operating cost up.

There are many factors to consider for your strategy, such as local availability of skilled labor, infrastructure and the availability of suitable partners to support the nearshoring effort within North America. Developing an entrance strategy, modeling scenarios, careful analysis and finding the right partners and service providers are key steps in the process of ensuring successful execution of a manufacturing start-up in Mexico.

At Alvarez & Marsal, our professionals have extensive experience in evaluating global supply chains, identifying risks and alternatives, quantifying costs and benefits, and implementing solutions.

Contact us to find out how we can assist you.

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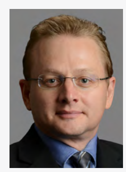

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Companies, investors and government entities around the world turn to Alvarez & Marsal (A&M) for leadership, action and results. Privately held since its founding in 1983, A&M is a leading global professional services firm that provides advisory, business performance improvement and turnaround management services. When conventional approaches are not enough to create transformation and drive change, clients seek our deep expertise and ability to deliver practical solutions to their unique problems.

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