

USA New Government: Implications for the Mexican Automotive Industry

February 2017

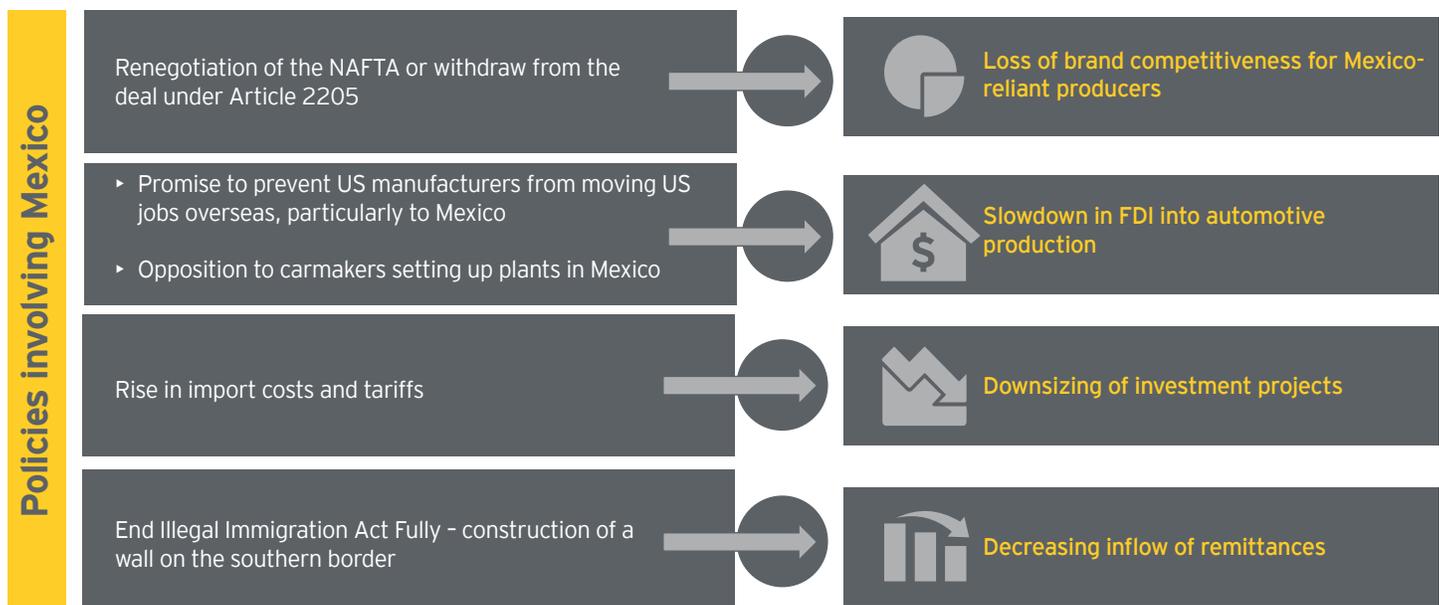




Trump's Presidency

Implications for the Mexican Automotive Industry

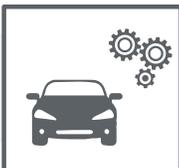
Despite Donald Trump's election, Mexico will not experience an immediate downturn due to the fact that his proposals will require at least 2 years to come to fruition. However, in the midterm, several risks may arise:





Brand Competitiveness

Damage on cost-competitiveness for Mexico-reliant producers



Non-US brands such as Volkswagen and Nissan have the highest risks due to their reliance on Mexican-made vehicles sold in the US. Protectionist policies will damage their ability to protect their Market share in the US.



Slowdown in exports and FDI

Heavy reliance on the US may have repercussions on Mexico's Balance Trade

Trump's protectionist policies will deter investment into Mexican production capacity

The Automotive Industry represents
32%
Of the exports that are not related to oil

85%
Is the share of the US in Mexican automotive exports

There has been a
2.93%
Decline of the industry's exports y-o-y

United States represents
35.7%
of Mexico's FDI

Implications

As oil prices decrease, the importance of Automotive exports increases

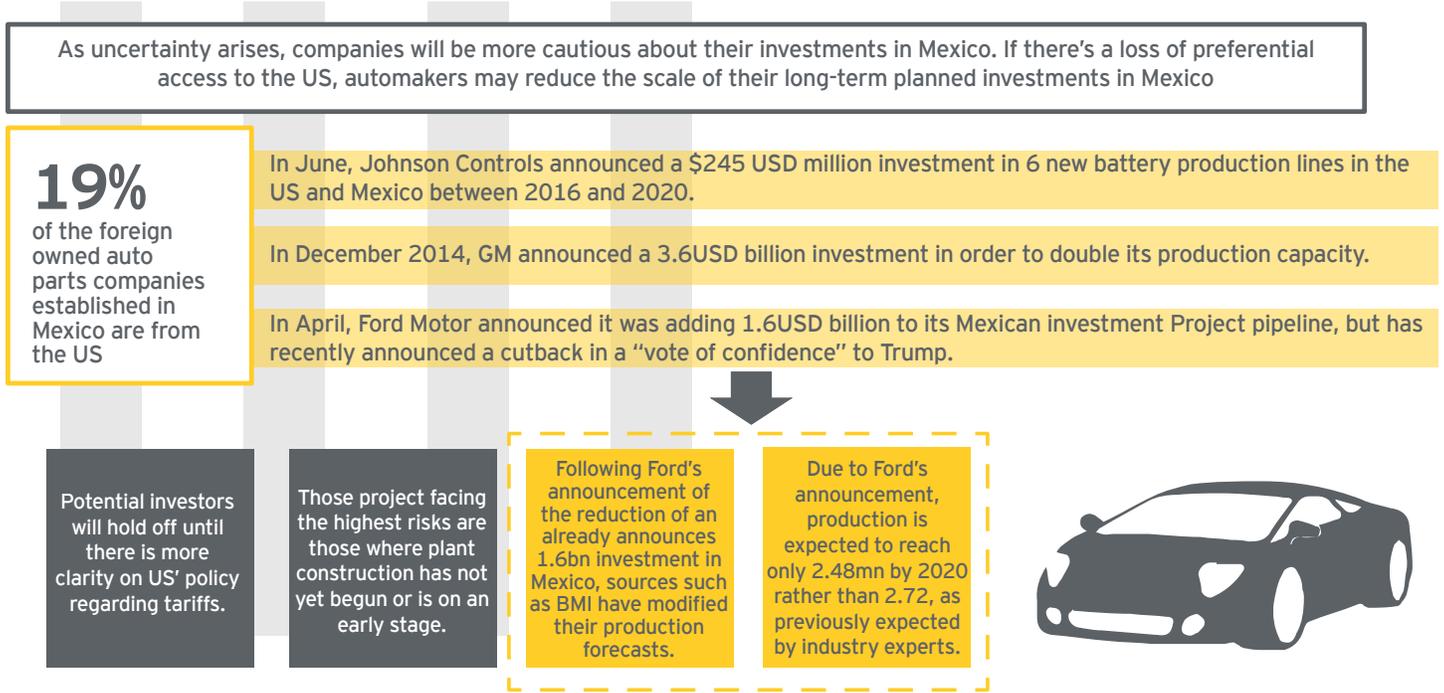
The dependency on the exports to the US increases volatility on Mexico's finances

A decline in the industry's exports would result in a deficit on Mexico's Balance Trade

A decrease in FDI coming from the US would further damage Mexico's BT

Downsizing of Investment Projects

Negative impact due to a possible loss of preferential access to the US



Source/s: International Trade Administration Forbes

Decreasing remittances

Slow inflow will reduce growth opportunities

On the short term, car sales might even increase because those families receiving remittances will have a higher acquisition power due to the high price of the US Dollar as compared to the Mexican Peso. However, tougher immigration restrictions will slow the flow of migrant workers and remittances, reducing the Mexican automotive market's growth opportunities on the mid and long term.

Remittances represent about 2.3% of the Mexican GDP

Around \$2,200 million USD per month are sent to Mexico as remittances

The last few years the significant rise on the inflow of remittances has bolstered Mexican households' disposable incomes.

- ▶ Around 83% of Mexicans who enter the US illegally send money home
- ▶ Trump promise to impound remittance payments holds a big threat to many Mexican families' income
- ▶ Mexico received \$24 USD billion in remittances on 2015
- ▶ Logistically, it is very hard to identify remittances because many payments are now made through mobile apps.

Source/s: Interamerican Development, Congressional Budget Office

Potential Impact on Demand

Moderate and Adverse Trump scenarios

2020 forecasts

0.33mn ▼

LV Sales decrease in the US under a Moderate scenario

3.88mn ▼

LV Sales decrease worldwide under an Adverse scenario

Moderate Trump scenario: Partial implementation of various stated policies which would likely lead to negative consequences for US and global economic growth

Light Vehicle Sales (mn)

	World				USA				ROW		
	Baseline	Moderate Trump	Chg.		Baseline	Moderate Trump	Chg.		Baseline	Moderate Trump	Chg.
2016	93.1	93.0	-0.05	2016	17.45	17.44	-0.01	2016	75.6	75.6	-0.04
2017	94.3	93.9	-0.44	2017	17.45	17.24	-0.21	2017	76.9	76.6	-0.23
2018	97.0	96.3	-0.67	2018	17.47	17.21	-0.26	2018	79.5	79.1	-0.41
2019	100.5	99.6	-0.96	2019	17.50	17.12	-0.38	2019	83.0	82.5	-0.58
2020	103.2	102.3	-0.94	2020	17.59	17.26	-0.33	2020	85.6	85.0	-0.61
2021	106.2	105.4	-0.82	2021	17.72	17.48	-0.24	2021	88.5	87.9	-0.58

Adverse Trump scenario: Many, though still not all, of the stated policies are implemented. The resulting slowdown in the US and global economies, and declining trade flows between several of the world's largest economies, has far-reaching consequences around the globe

Light Vehicle Sales (mn)

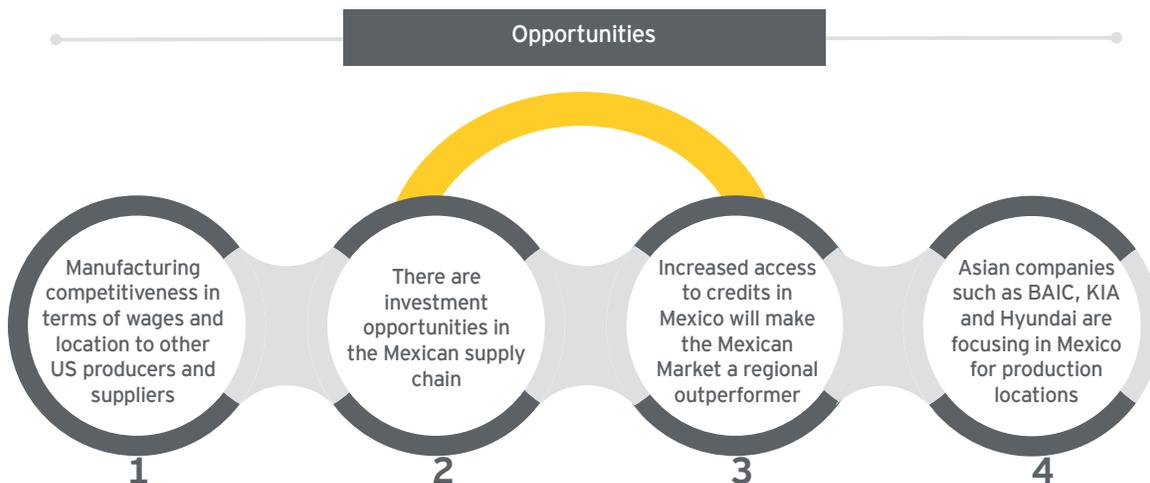
	World				USA				ROW		
	Baseline	Adverse Trump	Chg.		Baseline	Adverse Trump	Chg.		Baseline	Adverse Trump	Chg.
2016	93.1	93.0	-0.06	2016	17.45	17.43	-0.01	2016	75.6	75.6	-0.05
2017	94.3	93.4	-0.92	2017	17.45	17.04	-0.41	2017	76.9	76.4	-0.51
2018	97.0	95.0	-1.95	2018	17.47	16.68	-0.79	2018	79.5	78.4	-1.16
2019	100.5	97.6	-2.91	2019	17.50	16.40	-1.10	2019	83.0	81.2	-1.82
2020	103.2	99.4	-3.77	2020	17.59	16.26	-1.33	2020	85.6	83.2	-2.43
2021	106.2	102.3	-3.88	2021	17.72	16.51	-1.21	2021	88.5	85.8	-2.66

Source/s: LMC Automotive

Opportunities

On the bright side, there are several growth opportunities for the industry

Mexico is overtaking Canada as the #2 exporter of good to the US this year, reflecting the strong pull of lower cost jurisdictions for the US economy.





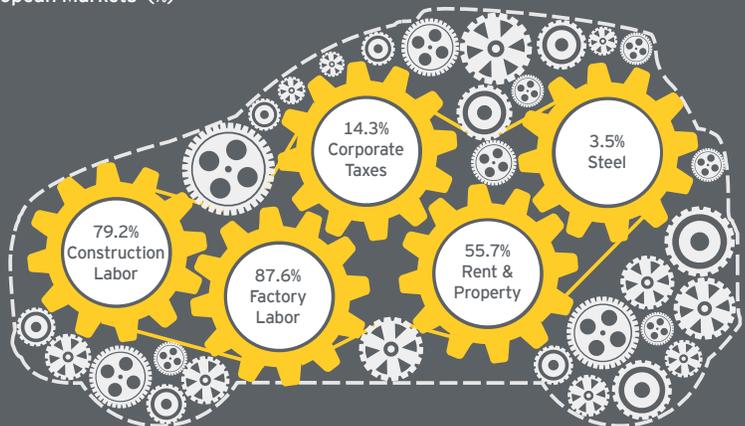
Manufacturing Competitiveness

Low wages and tariffs have made Mexico an attractive export base

Mexico has become the most advantageous auto manufacturing location in the NAFTA region due to the low value of the U.S. dollar

- ▶ Exports from Mexico to **44** countries are exempt from tariffs
- ▶ Overall, passenger cars have a lower margin than larger vehicles. Several OEMs are moving their passenger car production to Mexico and taking advantage of the lower manufacturing costs.
- ▶ **20%** of all North American light vehicles are produced in Mexico
- ▶ In 2013, the average hourly wages for the LV and the automotive parts manufacturing sectors were nearly **1/8** and **1/5** comparable to wages in the US; nowadays the numbers are almost still the same

Cost Advantages of Producing in Mexico for U.S. and European Markets (%)



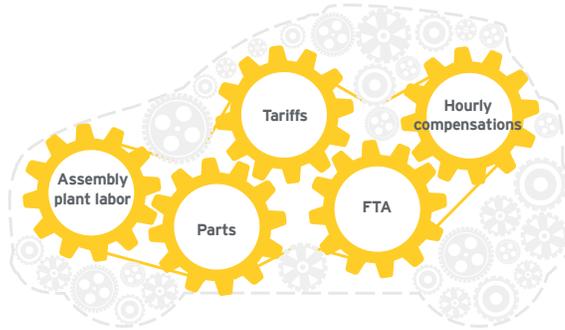
Source/s: Center for Automotive Research



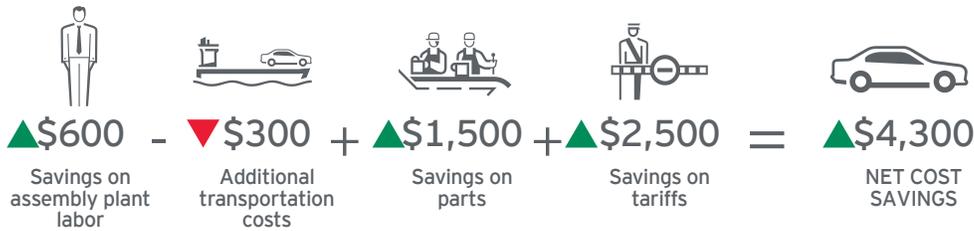
Manufacturing Competitiveness

Trump tariffs might not stop job flight

Additional to the low wages, Mexico has a series of benefits for the automakers who seek to start their production in the country. Mexico's main downside is the lack of transportation infrastructure but it is widely compensated by several other factors



Difference per vehicle costs in Mexico vs US for small cars sold in European markets



Mexico's tariff savings

Automakers save around \$2500 per mid-sized vehicle by building it in Mexico and shipping it to Europe due to the fact that the US does not have trade agreements with the European Union.

\$201
European Union

\$550M
Brazil

\$20M
Uruguay

Tariffs avoided by Mexico in countries where the US has no free trade agreements

In 2014, automakers saved around \$220 million in tariffs that they would have paid if their exports had come from the US instead of Mexico

Source/s: Center for Automotive Research, Bloomberg Research

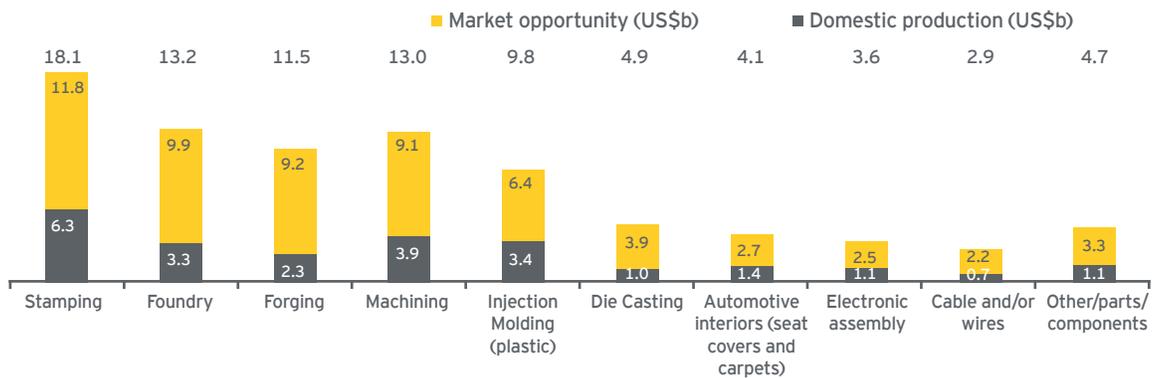


Market Opportunity in Mexican Supply Chain

Despite strong tier-I presence, Mexico lacks low tier suppliers



Mexico has been attracting automotive manufacturing investments; however, the country lacks lower tier manufacturing support



- ▶ Mexican tier-II is concentrated in a few processes such as smelting and plastic injection
- ▶ Stamping, Foundry, Forging and Machining are the processes with most unmet demand from Mexico based suppliers

Trendicators

6%

Of FDI is invested in the Automotive and Transportation Industry

+2,500

Companies manufacturing auto parts across 19 states of Mexico

71%

Of total Mexican demand for processes is met through imports

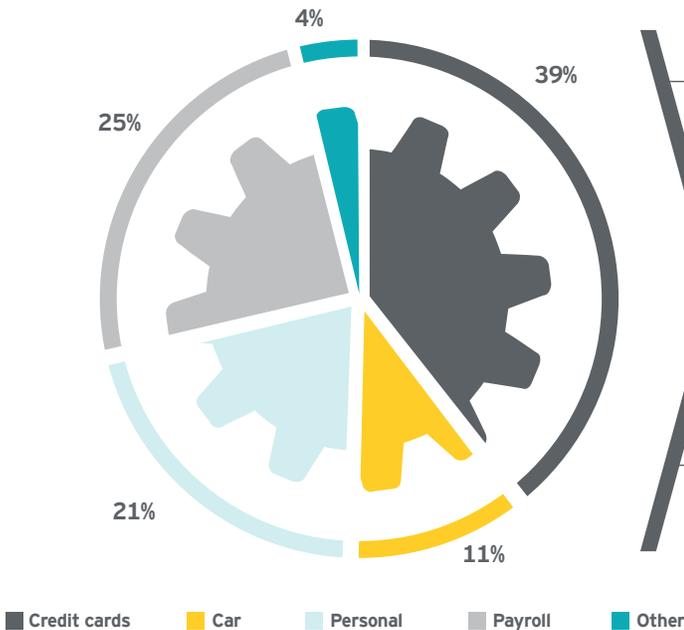
Source/s: AMIA; ProMexico; News analysis "Supply Chain Workshop EY"



Access to Credits

In recent years, access to credit in Mexico has been increasing

Consumer loans by type - October 2016



The market for credit in Mexico still has significant potential

Consumer confidence has been picking up in recent months

There has been a decline in unemployment

Consumer loans increased around 13% YoY

Car loans represent around 11% of the total consumer loans

About 65% of car loans were granted by finance subsidiaries of automakers

Consumer loans are expected to increase in 2017

Source/s: Comisión Nacional Bancaria y de Valores (CNBV)

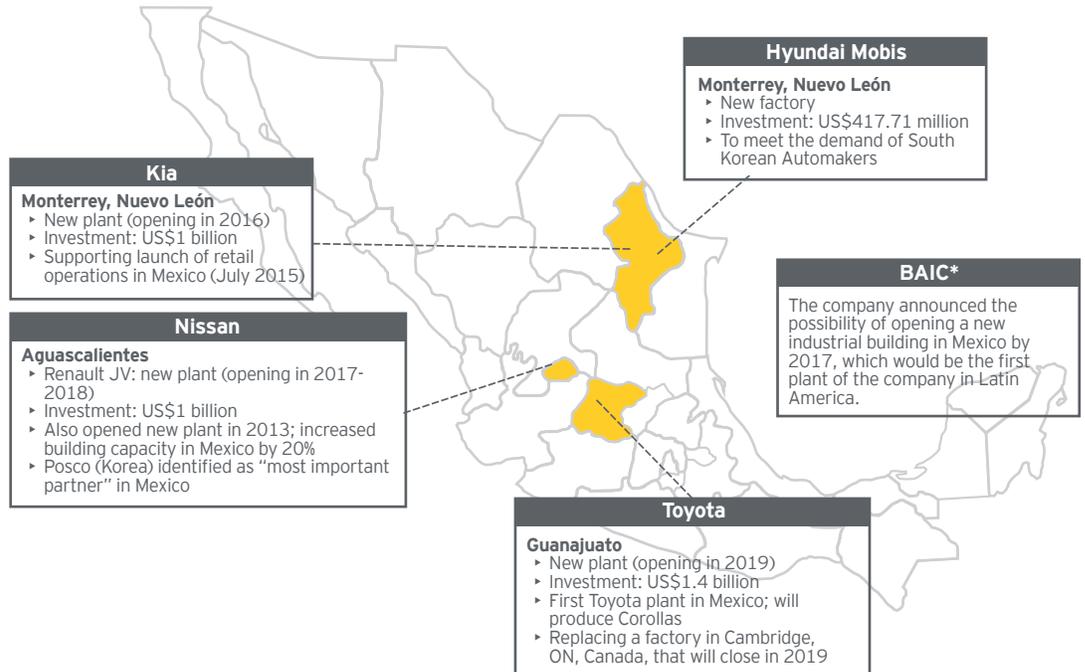
New Investments

Asian companies have announced investments in Mexico

Mexico's ties with Asian OEMs are growing stronger

Several Asian companies have opened new Mexican assembly plants, or disclosed plans for one.

Following the US Presidential election, Mexico and China pledged to deepen ties.



*Not yet confirmed



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