Roots of the Maquila Program

Article by Jim McNamara; MaquiLogistics, Inc 05-2004

The roots of the Maquiladora program actually date back prior to the passage of the decree in Mexico creating the "Border Industrialization Program" in 1965. For the period of 1951-1964, U. S. Immigration laws provided for a guest worker ("Bracero") program which allowed Mexican national farm workers to get temporary "seasonal" work visas to come over to the U.S. for the fruit and vegetable harvests in the southern states.

At the time of the termination by the U.S. of the Bracero program in 1964, there were estimated to be a backlog of 50,000 applicants in Tijuana alone, awaiting acceptance into this program. These people from the interior of Mexico , who had come to the border towns in hope of working temporarily in the U.S. , now no longer had that opportunity; and found little available employment on the Mexican side of the border.

Unemployment was said to be 40-50% in some Mexican border towns as the Bracero program was phased out.

The Mexican government felt the need to develop externally-sourced employment opportunities for the border cities, given that the local economies would not be able to absorb the large influx of workers, and they did not want to see movement back to the heavily overcrowded Mexico City area. Mexico certainly had an abundant supply of labor, but lacked the job base, especially in the manufacturing area, necessary to gainfully employ these workers. The major barrier to foreign (non-Mexican) companies making the necessary capital investment in manufacturing operations in Mexico was the concern over ownership rights to the Mexican company, and the extremely high Mexican import duties (100% or higher duty rates were common) that needed to be paid to bring materials into Mexico for further processing. (Even to this day, many Maquiladoras source little, if any, of their raw materials in Mexico). The Maquiladora program allowed both 100% foreign (non-Mexican) ownership and duty-free entry into Mexico of all materials and equipment, regardless of origin needed to support the operations. The Maquiladora decree set the groundwork for significant foreign capital investment in manufacturing operations along the border.

As companies began to examine the possibilities of setting up Mexican manufacturing operations, a still relatively obscure U.S. tariff clause (the "807" assembly provision), passed by the Congress in September 1963, also began to draw attention in the United States . The "807" tariff provision allowed companies to deduct from the dutiable value of items to be imported into the U.S., the value of any solid, discrete components of 100% U.S. origin that were exported from the U.S. "ready for assembly" into the imported article. Although this tariff provision was applicable to imports into the U.S. from anywhere in the world, there seemed to be a special fit for this provision for potential Maquiladora operations. A company could have the best of both worlds; access to an abundant and inexpensive labor force in the Mexican border cities, and privileged tariff status, if U.S. origin goods were used in an "assembly type" operation. As the Maquiladora industry began to take off in the late 1960's and early 1970's, most plants were labor-intensive assembly operations.

The companies who were early pioneers in the Maquiladora industry, however, often perceived that there was a stigma attached to a product marked "Made in Mexico ". In the early days of the industry, most maquiladora production was of "sub-assemblies" which were then imported into the U.S. for processing at a sister, or "twin" plant, into finished goods which could be marked as being of U.S. origin. For these reasons, the industry often was referred to as the "Twin Plant Assembly" industry.

Throughout the last several decades there have been several major transitions in the industry, as the maquiladora program evolved. Mexico eventually opened up to allow the maquiladora program to be set up, with some areas restricted, in the interior of Mexico . Many of the maquiladoras who set up outside of the border area located along a second "frontier" roughly 150-250 miles away from the border, in the Monterrey-Chihuahua-Hermosillo corridor. You now find maquiladora operations spread all throughout Mexico .

Over time, maquiladoras also became more than assembly type operations. Today many maquiladoras engage in all types of manufacturing operations. While the full benefits of U.S. tariff provision 807 (now 9802) are not applicable to manufacturing operations, there have been other tariff laws, most recently the North American Free Trade Agreement, that have significantly lowered U.S. tariffs on maquiladora production.

Also over the time, the stigma of a product being marked "Made in Mexico " has subsided as many maquiladora operations have received special recognition for the high level of quality in their product. With the need for maquiladoras to become increasingly more efficient to compete in the worldwide market place, many maquiladoras now are highly vertically integrated with both assembly and manufacturing operations occurring side by side, and offering a finished product for direct sale into the U.S. marketplace or beyond.

The maquiladora industry has become a vibrant part of both the Mexican and U.S. economies, with employment of over one million workers in the industry. However, the program has not been without its detractors throughout its history, principally from U.S. labor interests, who object to what they feel is unfair competition from low-cost Mexican labor.

As part of the North American Free Trade Agreement (NAFTA) negotiations, special duty treatment on maquiladora production was limited starting in January of 2001. Article 303 of NAFTA became effective on that date and removed long standing across-the-board duty exemptions to maquiladoras, although Mexican duties can still be abated on NAFTA originating materials and equipment.

Mexico has responded proactively to create Industrial Sector Preference programs (called PROSEC's) to allow for continued free or reduced duty entry into Mexico of select non-NAFTA raw materials and equipment used in certain industry sectors.

The post 2001 landscape created by Article 303 of NAFTA, sometimes referred to as the 2nd phase of NAFTA, has resulted in a more complex duty environment for Maquilas in Mexico . NAFTA, while reducing U.S. duties payable by most Maquilas, has created potential Mexican duty liabilities that never before existed. NAFTA, far from simplifying and streamlining Customs duties has actually added a new layer of complexity in the process of determining Customs duties.

After a couple of difficult years triggered by global economic woes and the growth of new investment in China , the Maquila industry has shown some new signs of life in 2004. Despite the risks and threats that exist in the global marketplace the Maquila Industry is here to stay as a significant fixture in U.S./Mexico trade.

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