DUCKER CARLISLE

GLOBAL CONSULTING, STRATEGY AND M&A SERVICES

Are Chinese Automakers Making Inroads in Mexico to Target North America as a Whole?

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Chinese automakers in Mexico have captured nearly 10% of light vehicle sales in only 6 years. Although they remain far from legacy OEMs from Europe, United States, Japan, and South Korea, they have shown an unprecedented growth in the Mexican market. Among the Chinese OEMs selling in Mexico, SAIC MG, Chery Group (including Chirey and Omoda), JAC Motors sold a total of almost 120,000 vehicles in 2023, representing 8.9% of the total light vehicle sales last year.

Mexico is the world's seventh-largest in terms of light vehicles production, and the fifth-largest for components. According to the USMCA agreement, companies with factories in Mexico that are sourcing a minimum of 75% of vehicle components in North America can export to the United States duty-free. This positions Mexico as a key entry point for North American automotive investments.

Typical Entry Strategies for Chinese Automakers

Whole Vehicle Export (CBU)

- Used in the early stages of global expansion
- Advantages: Quick entry into overseas markets and increase brand awareness; low initial cost
- Challenges: High tariffs and trade barriers; potential difficulties adapting to local markets

Knocked Down (KD) Export

- CKD and SKD are preferred entry solutions for OEMs when exploring new markets
- CKD (Complete Knocked Down) are preassembled vehicles broken down to be reassembled in the target country
- SKD (Semi Knocked Down) are partially preassembled vehicles broken down to be reassembled in the target country with a minimal amount of components sourced locally to get around tariffs and quotas
- Mainly used in developing countries and regions
- Advantages: Lower car production costs for the automaker and avoid tariffs and trade barriers
- Challenges: Require a complex disassembly and assembly process, placing high demands on the supply chain and production management

Brand Mergers and Acquisitions (M&A)

- Acquire overseas car brands, including their technology and equipment
- Mainly used to enter mature markets
- Advantages: Allows car companies to quickly acquire brand recognition and improve their production capabilities
- Challenges: Require strong management and resource integration skills, and may lead to debt burdens and financial crises

Greenfield Investment

- Build entirely new production facilities in overseas countries
- Often receive the support of local governments
- Advantages: Allow production according to the company's requirements, offering greater flexibility, and boost the development of local supply chain
- Challenges: High investment costs, long construction period, difficulties establishing expertise, and requiring strong risk management and market development capabilities

(Sources: Ducker Carlisle, iResearch)

As Mexico became a large component manufacturing location, Chinese suppliers joined the North American and European Tier 1s in key areas, with Joyson Electronics, Tuopu Group, Xu Sheng Group, andBethel, who have set production in Mexico. This represents a threat to local Mexican suppliers and legacy ones from the US, Europe, Japan and Korea alike. The Chinese suppliers are now competing with them to supply

Company	Facility Location	Facility Status	Product
Asiaway	San Luis Potosi	SOP	Casting
Bethel	Saltillo	Construction	Chassis/Suspension/Brake
Daimay	Monterrey	SOP	Interior
Desay SV	Monterrey	Construction	Cockpit
IKD	Leon	SOP	Casting
Lingyun	Leon	SOP	Thermal Mgt./CMS
Lizhong	Monterrey	SOP	Wheel
Minth	San Luis Potosi	SOP	Extrusion
Minglida	Irapuato	Construction	Extrusion
Rongtai	Leon	SOP	Casting
Sanhua	Saltillo	SOP	HVAC/Thermal Mgt.
Tuopu	Monterrey	Construction, SOP 2024	Interior/Chassis/Thermal Mgt.
Wencan	Querétaro	SOP	Casting
Xinquan	San Luis Potosi	SOP	Interior
Xusheng	Saltillo	Construction, SOP 2024	Casting/Extrusion/Forging
Yanfeng	Monterrey	SOP	Interior/Seat
Yinlun	Monterrey	SOP	EV Thermal Mgt.
Zhongding	Querétaro	SOP	Sealing/Thermal Mgt./Air Spring

(Source: Ducker Carlisle)

In addition to the traditional whole vehicle export model, several Chinese automakers are now exploring the possibility of building factories in Mexico. With Chinese suppliers growing in Mexico, several Chinese OEMs now have local partners to invest in local production. In March 2023, Jetour announced a $3 billion investment to build a plant in the Mexican state of Aguascalientes or Guanajuato, which is expected to open in 2024. The OEM intents to produce gasoline-powered vehicles and pure electric vehicles within the next three years. Chery plans to build a plant in Mexico with an annual production capacity of 400,000 vehicles, mainly to produce new energy vehicles. In addition, there are reports that SAIC MG, BYD and Geely are all in talks with Mexican authorities about factory site selection.

Automaker	BAIC	BYD	CHANGAN	CHIREY	Great Wall	JMC	JAC	SAIC
Brands	BAIC	BYD	CHANGAN	OMODA / JETOUR	HAVAL / ORA	JMC	JAC	MG / CHEVROLET SAIC-GM
Models	X35, BJ40, X55	Han, Tang, Yuan, Dolphin	Alsvin, CS35, CS55	Tiggo 2/4/7/8, OMODA 5	HAVAL H6, ORA 3	Vigus	10x, J7, Sei 2/6/4/7, Frison T6/T8	MG GT, MG 5, MG ZS, MG RX, Chevrolet Aveo
Sales in MX	√	√	√	√	√	√	√	√
Production MX	√ Lagos de Moreno, Jalisco	Planning	Planning	Planning plant for Jetour	Planning	×	√ Tepeapulco & Ciudad Sahagún, Hidalgo; Planning 2nd plant	×
Production in other LATAM	Argentina	Brazil (SOP 2025)	Argentina	Brazil	Brazil (SOP 2024)	n/a	n/a	n/a

(Source: Ducker Carlisle)

Chinese investment strategies seen as a threat for US-based OEMs and production

In early 2021, the White House issued the "Executive Order on the American Supply Chain," promoting nearshore outsourcing. The "Inflation Reduction Act" from August 2022 secured the $7,500 tax rebate for electric vehicles, but it requires vehicle assembly in USMCA (following the rule for 75% of components to be produced in the region) with battery assembly, and raw material (minerals) sourced locally.

Eligibility must combine Year	$3,750 Share of critical minerals in EV batteries sourced from USMCA or countries with which the U.S. has a free trade agreement	$3,750 Share of battery components manufactured or assembled in USMCA
2023	50%	40%
2024	60%	50%
2025	60%	60%
2026	70%	70%
2027	80%	80%
2028	90%	80%
2029 and beyond	100%	80%

This creates a first barrier for Chinese OEMs to become eligible, as a part of the Chinese vehicles competitive advantage relies on the Chinese sourcing of their batteries and other key components. This constitutes a major hurdle for Chinese automakers and prevents them from a quick entry into the US market. As a consequence, BYD executive vice president Li Ke said in June 2023 that "the US market is not within our current consideration." Compared with the United States, she is more willing to discuss the growth plans of markets such as Mexico, Chile and Thailand.

BYD officially entered the Mexican passenger car market in March 2023, and subsequently launched models such as Dolphin and Seal into the market. Li Ke once said that the company is considering building a new factory in Mexico, but it will depend on market demand. "In principle, the cars we provide in Mexico will come from China, but if the demand is huge in the future, we will consider producing in Mexico." It illustrates the complexity of entering the North American market with SKDs. In the meantime, the United States has set an annual export quota of 2.6 million vehicles for Canada and Mexico (a 25% U.S. tariff if the export quota is exceeded) beyond the basics of the USMCA sourcing agreement. Therefore, Chinese OEMs willing to enter the US market would have to share these restricted volumes with leading brands such as Volkswagen, Honda, GM, Ford, Stellantis and Nissan.

Looking further ahead, the US and Mexican governments are expected to set up additional barriers for Chinese companies which generates a lot more uncertainty for them to fully enter the North American at large and the US market in particular. The US Congress may adjust the rules at any time if Chinese OEMs take a stand towards a stronger presence and competitiveness in the USMCA economic area. Li Bin, CEO of Chinese electric car company NIO, called on the US government to provide equal opportunities for Chinese electric car companies to enter the US market, stressing that automakers should not be involved in the political tensions between superpowers. Li Bin noted the current global political climate is very different from when the company was founded in 2015, after the COVID pandemic caused division and confrontation.

On February 29, US President Biden instructed the US Secretary of Commerce to investigate smart cars from China as a potential threat to national security. The US Department of Commerce focused on Chinese-developed software and electronic devices in cars such as Telematics Control Units. Following the investigation, the Biden administration announced new measures under section 301 of the Trade Act of 1974. It raised tariffs on Chinese built EVs to 100% and increased tariffs on selected metals (steel and aluminum) to 25%. The metal tariff targets potential transshipments of Chinese materials and components through Mexico. China has since threatened to retaliate with a 25% tariff on imported vehicles assembled in North America (and in Europe).

Thus far, Chinese OEMs such as GAC have unsuccessfully attempted to enter the US market. The new strategy is much more structured with a gradual entry through Mexico and benefitting from a locally based supply-chain with Chinese suppliers. The entry barriers are growing with tariffs and regulatory scrutiny on electronics and data management. The price of Chinese EV may become less attractive with time as they will also have to source some of their electronics from North American suppliers. Without the MSRP advantage, one can wonder how much effort Chinese OEMs will have to provide to enter the US market lacking brand image and dealer network. They will have to put emphasis on other qualities, particularly in terms of content, technology and user experience. Whatever their decision will be, Chinese automakers shouldn't expect a smooth ride into North America.

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