

Maquiladora industry

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In this paper I will discuss the history and practices of the Maquiladora industry. I will discuss its background, its problems, the benefits it offers to United States companies, and the impact the NAFTA has and will have on the industry. In addition, I will make a suggestion on a possible strategy the Maquiladoras can adopt in order to address the challenges brought on by the NAFTA, to ensure it remains a strong force in the future.

Mexican agricultural workers had been granted temporary work visas allowing them to work in the United States" agricultural industries through a program called the Bracero Program until 1965 when this program was terminated. As a result of this termination, the unemployment rate had exceeded 70% in certain border cities. In May of 1965 the Border Industrialization Program was established as a replacement for the Bracero program. It was later renamed the Maquiladora Program.

The program was established by the Mexican government to provide employment for Mexico" s rapidly growing population along its border with the United States. This program was utilized to keep Mexicans from entering the United States. The idea was that Mexican workers would be kept on the Mexican side of the border if they were given factory jobs on the Mexican side. The Maquiladora program also wanted to attract foreign manufacturing facilities, technology, and know-how by giving a permanent tax holiday to manufacturing companies that would set up " twin plants" on the Mexican side of the border.

In the beginning of the program, all foreign-owned operations had to be located within a 20-kilometer strip along the US-Mexican border. Since 1972

they can be located anywhere in Mexico. In 1996 there were around 2, 500 Maquiladoras - 35% of them were located in the interior states of Mexico. Last year there were over 3, 000 and more and more of these operations are being located outside of the border regions. Each of Mexico's 31 states has at least one Maquiladora.

Maquiladoras, also referred to as "in bond" or "twin" plants, are allowed to temporarily import into Mexico (free of tax) machinery, equipment, replacement parts, raw materials, and just about anything that was used in the assembly or manufacture of semi-finished or finished products. Once assembled or manufactured, the Maquila products must be exported unless special permission is obtained to sell a limited amount of output in the Mexican market. When these products are imported back to the United States, import duties are levied on the foreign value-added only. If Maquila products stay in Mexico, they are subject to applicable Mexican duties.

The largest issue surrounding the Maquiladora industry is the exploitation of cheap labor. The working conditions are often unsafe, workers are not compensated adequately for their labor, attempts to unionize are discouraged; and sexual discrimination and harassment are too common.

The conditions in and outside the Maquiladoras are terrible. Workers perform tasks such as welding without protective masks, leather gloves, or goggles (in many instances) and industrial accidents and toxic exposures are common. This, along with malnutrition caused by low salaries, produce skin illnesses, cancer, irregularities in menstruation, abortions, tumors, intoxication and birth of undernourished or disabled babies.

Of the employees, many are young girls and women ranging from the ages of 14 to 20. They work 6 days a week in 10-hour shifts. The average weekly salary for a Maquiladora worker is US\$35 - \$45 even though the average monthly rent for a house with public services such as running water and electricity is around \$200 a month.

For the most part, Maquiladoras are unorganized. In those that are organized, state-controlled unions represent the workers. Although some companies are unionized on paper, the unions, for the most part, function to reinforce management policies rather than for the benefit of workers. Then there are what are called "phantom" unions. These unions do not fight for the worker's rights. The workers do not even know them and have never seen their union leaders. When a conflict arises in a factory, management informs the worker that their unions have accepted these or those conditions. Not only are they not protected by existing unions, those that attempt to unionize and are often threatened or bribed by plant managers and the government.

In many companies, discrimination against and harassment of the female employees is very common. Female job applicants are required to produce urine samples to be used for pregnancy tests, while some have company doctors and nurses examine the applicants or ask confidential information concerning their contraceptive practices. This is done because pregnant women are refused employment. Sexual harassment is often the rule rather than the exception. Rapes occur frequently and few are reported because women fear being fired or blacklisted. Shame and humiliation also keep

them quiet. In Mexico, men and women are equal before the law, but the law does not recognize discrimination as a problem to be solved.

The Pollution Brought on by the Maquiladoras

The increased pollution, accompanied by the dumping of tons of hazardous wastes, poses a serious health threat to the residents of Mexico as well as the resident of the bordering US states. There are several canals that are "black" with chemical wastes that have been measured at levels that greatly exceed permissible standards. One factory was caught dumping drums of paint, solvents, and shellac into a drain. In other areas there are abandoned lead smelters and air full of soot and dust from brick-making ovens and smoldering tire dumps.

Main Advantages for the United States' Companies

For the United States companies this was a great advantage since Maquiladoras operate at very low costs in places where the currency is weaker than the dollar—such as Mexico. The less a currency is worth, the more relative value the dollar has. Since Mexico's peso is relatively weak, companies can trade their dollars for pesos with which they pay workers and expenses. The products they manufacture, however, are sold for dollars, increasing their profits by huge margins whenever the local currency falls. They could enhance competitiveness, reduce their costs, and maintain quality by placing their labor-intensive operations in the less developed Mexico, benefiting from the lower wage rates there.

For many US companies, manufacturing in Mexico has become necessary to battle overseas competition. Since many manufacturers are moving to "just-in-time" inventory systems, the quick delivery possible from Mexico's border towns offers a substantial advantage over Asian alternatives.

The NAFTA's Impact on the Maquiladora Industry

Traditionally, Maquiladoras offered foreign businesses several advantages over other forms of direct foreign investment. Since the signing of NAFTA, however, many of these advantages are either being phased-out or granted to all Mexican companies. The most significant advantages of operating as a Maquiladora include: 100% foreign investment, operation without ownership of assets, tax sheltering of cost centers, and 100% duty-drawback or waivers for temporary imports. Furthermore, the NAFTA attempted to address the labor exploitation and environmental problems associated with the Maquiladora industry.

One of the benefits of the Maquiladora program is 100% foreign investment of Mexican operations, which formerly was not allowed. However, Mexico's Foreign Investment Law has changed through the years (most significantly in 1989 and 1994)-full investment is now allowed in most business ventures.

Operation Without Ownership of Assets

Another advantage that Maquiladoras have is that they can receive production materials and capital goods as loans from their parent and client companies. As a result, most Maquiladoras have little or no inventory of fixed assets, eliminating the need to pay the Mexican asset tax of 2% of all assets.

In January 1995, the Mexican IRS reported that Maquiladoras would now have to factor the depreciation of "loaned" assets in price-transfer calculations, which is the first step toward phasing-out this advantage by 2001.

When Maquiladoras are structured as cost center (providing manufacturing services for a foreign parent) the foreign corporation has traditionally paid the Mexican company for operating costs plus negligible profit. By doing this they avoid Mexico's 34% corporate income tax, 10% mandatory profit sharing, and asset taxes. Now the Mexican IRS is changing the way Maquiladoras must declare assets. Over the next few years, Maquiladoras will be forced to raise their declared profit percentage to a rate that is comparable to that of two unrelated companies performing the same transaction at "arm's length". This is the type of transfer pricing procedure that is implemented by most trading blocks, like the EC. It will soon be effect throughout North America.

100% Duty-Drawback or Waivers for Temporary Imports

Maquiladoras have always allowed Mexican companies 100% duty drawback or waivers in imported components that are exported as final goods. Since 1994, this has provided many Maquiladora programs a way to use non-NAFTA materials within products without the need to pay the corresponding duties over those materials when importing or exporting goods to other NAFTA nations. On January 1, 2001, Maquiladoras that manufacture goods for export to NAFTA partner countries will no longer be allowed to take the

waiver. The waiver will still be available for goods that are going to non-NAFTA countries.

In 1995 the NAFTA's of Labor created the National Administrative Office (NAO) as well as the North American Agreement on Labor Cooperation (NAALC). Both were intended to stop labor abuses. The NOA was established to monitor labor complaints that NAFTA critics' voice regarding unfair labor practices. The NAO can recommend "ministerial consultations" as well as imposed heavy sanctions against Mexico. Unfortunately, the side agreements proved useless. The NOA cannot force Maquiladoras to allow unions-the most they can do is recommend "ministerial consultations." Sexual harassment and discrimination continues as well.

The NAFTA has also created side agreements covering the environment. One of them is the North American Development Bank (NAD Bank). Its purpose was to finance wastewater treatment projects along the border in the poorer communities. However, the most important criteria that needed to be met in order to receive funds were meeting certain market considerations. With this program NAFTA "encouraged" growth without regard for the environment through its practice of placing market consideration above environmental protection. Another is the Commission for Economic Cooperation (CEC). The CEC was established to investigate governmental non-enforcement of environmental laws. Unfortunately it has no power to enforce, they can only investigate-and they can't even do that until Mexico collects the data on the pollution for them.

Possible Strategy for the Maquiladora Industry

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As long as the Mexican currency is weaker than the US dollar I don't think that the changes are going to dramatically effect the flow of US companies to the south. However, the Maquiladora industry cannot count on this for continued growth. By the year 2001 the Maquiladora industry as we know it now will have significantly changed when the phasing out is complete.

Maquiladoras will no longer be "tax break" establishments; they will be just like other foreign investments. In order for them to fully compete in the near future they must become more efficient and leaner. The impact of globalization is forcing manufacturers to produce more rapidly and cheaply than ever before and to continuously improve. Because there will be no differentiation between the non-Maquiladora and Maquiladora industries I feel the inefficient producers will be wiped out. Therefore, Maquiladora employees will need better training, education, incentives as well improved working conditions and higher wages. Operations will also have to be streamlined in order to reap the benefits of economies of scale and scope.

In addition, Mexicans as well as US citizens will start to demand more accountability from the Mexican government and the Maquiladora industry. They need to be more responsible for their actions. What will the U.S. corporations do when human rights activists and environmentalists start lobbying and protesting on their US sites? Do they want to risk losing their shareholders to this type of negative attention?