SPECIAL SUPPLEMENT

LATIN AMERICAN LOGISTICS

# A New World Venture

As rising fuel costs and lengthening supply lines give businesses further pause assessing total landed logistics costs and proximity to market, Latin America finds itself squarely in the middle of an emerging logistics land swap. Thanks to the pioneering efforts of visionary 3PLs, U.S. companies are prospecting sites in Mexico, Brazil, and elsewhere as they explore new sourcing and selling opportunities.

# Brazil Stakes Its Claim

## Shifting trade winds, strong domestic industries, and the presence of leading 3PLs have positioned Brazil in the middle of a global trade rush.

With so much attention directed toward the Asia-Pacific theater, and U.S. businesses bent on digging deeper into countries such as China in search of less-expensive labor, Latin American markets have largely remained untapped. Mexico notwithstanding, countries such as Brazil have been discreetly, albeit progressively, developing transportation infrastructure, absorbing intellectual capital and best practices, and creating a business climate that is rapidly attracting foreign interest from businesses and logistics providers alike.

Latin America is far from a new venture for U.S. industry. Henry Ford's foray into Brazil's rubber-rich Amazonian market and the ill-fated development of "Fordlandia" in the 1920s foreshadowed the automobile's inevitable importance to the region's economic prospects.

Today, the automotive sector is among Brazil's top export industries and the country's emerging role as one of the world's

leading ethanol and flexible-fuel vehicle producers bodes well for continued growth. In less overt ways, the development of the automotive industry, corollary demand for logistics and supply chain execution capabilities, and the swift migration of U.S. 3PLs to the region have helped reinforce a nascent transportation and logistics network that is beginning to pay major dividends for regional economic growth.

Ryder System first made inroads into Mexico, Brazil, and Argentina in 1995, notes Gene Sevilla, vice president and managing director of Ryder, Latin America. The Miami-based 3PL started selling into the Mexico market and its cross-border business organically evolved. Its expansion into Brazil and Argentina has largely been through strategic acquisitions, and Ryder entered Chile two years ago with an existing customer.

### Ryder in Latin America:

**ARGENTINA:**
724 employees
600 vehicles (17% owned, 83% dedicated)
200 carriers under contract
11 locations*

**BRAZIL:**
1,100 employees
1,000 vehicles (60% owned, 40% dedicated)
600 carriers under contract
12 locations*

**CHILE:**
5 locations*

**MEXICO:**
1,800 employees
1,000 vehicle fleet (60% owned, 40% dedicated)
145 carriers under contract
26 locations*

*including crossdock, warehouse, maintenance facilities

"Mexico was a greenfield effort, beginning with automotive and consumer products," Sevilla says. Its economy has been greatly helped by the North American Free Trade Agreement (NAFTA), evidenced by an upswing in manufacturing integration, international traffic, internal consumption, and general business growth. "NAFTA has been the wind under Mexico's wings," he observes.

South America, by contrast, has not enjoyed the benefit of a contiguous border or liberalized free trade and, consequently, is still internally market driven and focused. Brazil, however, is beginning to reap the benefits of social and economic reform and increasing domestic consumption, and this growth is spilling out beyond the continent.

South America's slower growth has been a windfall in terms of sustainable development. Political and economic protectionism over the past few years have helped stabilize fiscal management and strengthen domestic industries. In the face of a weakening U.S. market and an otherwise thriving global economy, Latin America at large and Brazil in particular are positioned to capitalize on a potential economic development bonanza.

"More people are buying consumer product goods in Brazil, including three million vehicles a year, many of which are manufactured in-country," says Sevilla. "Automobile producers are also exporting product to other South American countries as well as Mexico and China."

Strong government leadership has curbed once-rampant graft and is encouraging private investment. A more secure financial footing, controlled inflation, and greater public/private collaboration are further indications that Brazil's

traditionally domestic-driven economy can sustain and grow commodity and specialized export trade.

"For exports, Brazil remains a low-cost producer of commodities. It has resources and can produce inexpensively," says Sevilla. "Despite infrastructure concerns, Brazil can export cheaply and is becoming more efficient at achieving scale with manufactured goods."

But the infrastructure gaps are glaring, and inland transportation needs improvement to support warehousing networks as in Mexico and the United States. The cargo transportation network in Brazil depends heavily on trucking, with 62 percent of freight moving on roads, followed by rail (20 percent) and inland waterways (13 percent), says Adolfo Pimentel Filho, director of business development, Ryder Brazil.

"There are some efforts toward privatizing roads. Brazilian authorities are aware that they need to make strong investments in local infrastructure – especially transportation – to support short- and long-term growth plans," he says.

Mauricélio Gomes Faria, general manager of logistics, Latin America for Fiat Auto in Brazil, perceives road transportation as the foremost challenge and opportunity for business growth in the region. The South American arm of the Italian automobile company manufactures components and assembles vehicles in Brazil and Argentina.

Fiat Auto in Brazil has partnered with Ryder to handle international transportation management for Iveco-Fiat Group's truck and commercial vehicle division in Argentina and Brazil, and the Fiat Group's automobile business in Brazil and Mexico.

Growing consumerism, market competitiveness, and progressive technology investment have made Brazil attractive to Fiat despite bureaucracy and infrastructure issues. The value of working with Ryder is evident in its "ability to react to new transportation demands," says Gomes Faria.

While the broader difficulties of managing local transportation and warehousing, and linking these domestic components to global supply and demand chains are readily apparent, they have yet to dam the tide of foreign speculation. In fact, these obstacles have created demand for the type of responsiveness that third-party logistics companies can provide, hastening the pace of manufacturing and logistics outsourcing growth in the region.

As 3PLs continue to expand their presence throughout Latin America, they are also leveraging experience and service capabilities to attract U.S. and foreign businesses outside of the already entrenched automobile sector.

Ryder, which began working with automotive titans, has also developed local partnerships with leading consumer goods companies. Much of what it has acquired and developed in terms of cultural knowledge and value-added logistics services for the auto industry are transferable to other verticals.

On the transportation side, automotive companies' sophistication and focus on inbound and just-in-time require optimal routes for delivery to manufacturing plants. It's easy to predict demand, but any disruptions, such as transport delays, can greatly impact operations. These challenges necessarily impact local distribution.

"The automotive supply chain is contingent on network design and efficiencies gained or lost through warehousing and distribution strategies such as crossdocking. This level of sophistication is not available working solely with local partners," Sevilla shares.

In the consumer products sector, the network between local manufacturing plant and final consumer is considerably more arbitrary – businesses are less attuned to shifts in demand, and don't know what will be sold where. These companies require greater flexibility and scalability.

As interest in Latin American grows, the task of integrating local transportation and distribution links with global supply chains will define the evolving role of the 3PL – and give current outsourcing prospects a strike of certitude as foreign businesses explore new avenues for growth.

## BRAZIL

**GDP (OFFICIAL EXCHANGE RATE): 1.3 trillion**

**EXPORTS: $159 billion** (transport equipment, iron ore, soybeans, footwear, coffee, autos)

**IMPORTS: $116 billion** (machinery, electrical and transport equipment, chemical products, oil, automotive parts, electronics)

**EXPORT TO U.S.: 17.8%**

**IMPORT FROM U.S.: 16.2%**

**2006 U.S. FDI: $33 billion**

Brazil's historically dominant commodity trades, notably in the agricultural and mining sectors, have played a major role in the development of the country's port infrastructure, which to date touts four ports – Tubarao, Itaqui, Santos, and Sepetiba – among the world's top 50 in terms of cargo volume.

As Latin America's largest economy continues to consume, and maturing domestic industries pave the way for emerging global import/export trade, airfreight traffic to and from Latin America is projected to grow at a steady clip. São Paulo/Guarulhos-Governor André Franco Montoro International Airport, which currently ranks 37th in the world and tops in Latin America in terms of air cargo tonnage, is positioned to play a major role in Brazil's long-term economic growth.

Sources: Airports Council International, CIA World Factbook, American Association of Port Authorities, and U.S. Dept. of Commerce Bureau of Economic Analysis

# Expert Advice

## In a recent conversation with *Inbound Logistics*, Latin America guru Marcio Stewart shares his insight on the region's growing prospects.

**IL: Mexico and the United States' economic ties are well-documented with NAFTA trade. South America has had less success with the Free Trade Area of the Americas (FTAA) negotiations. How has the fruition and failure of these respective trade agreements impacted economic development in Mexico and Brazil?**

**MS:** While NAFTA improved Mexico's entire logistics system, Brazil never went through this type of catalytic experience. Consequently, Mexico's logistics efficiencies are closer to the United States' than Brazil's capabilities. Whereas the cost of logistics as a percentage of GDP is around nine percent in the United States, in Brazil it's approximately 13 percent, while Mexico lies somewhere between the two.

Protectionism always produces a smaller, less-efficient market, where customers pay higher prices for inferior goods. Brazil has come to realize this and is gradually opening up its market selectively.

**IL: Are Latin American governments working with the private sector to subsidize transportation and warehouse infrastructure development and attract foreign direct investment?**

**MS:** The Mexican government is aggressively promoting public-private partnerships to build up its infrastructure – which is attracting interest from the United States and elsewhere.

For example, last April, Chinese Ambassador Yin Hegmin visited the State of Sonora to discuss potential investment in the Port of Guaymas. According to local authorities, its preferential location close to the United States and improved logistics systems enable goods to reach the United States with greater speed.

Mexico and China already have burgeoning trade in grains, minerals, and fisheries. China is looking to improve its access not only to the Mexican market, but to the United States through Mexico. Worried about bottlenecks in Los Angeles, China is seeking supplementary conduits.

Leonel Godoy Rangel, governor of the state of Michoacán, met with Carlos Slim – the richest man in the world, according to *Fortune* Magazine – to discuss infrastructure investments. The state presented two different projects to the Grupo Carso, owned by Slim. One deals with the state's plan for highways, the other for its airport.

Slim also might be interested in several projects, including an infrastructure expansion at the Port of Lazaro Cardenas.

**IL: In terms of transportation infrastructure, how are Mexico and Brazil getting up to speed in developing networks that can accommodate growing freight transportation needs?**

**MS:** Mexico is very proactive with its infrastructure development. The government will invest US $8 billion in its railway system, and use some of this money to improve railway connections between the United States and Mexico in the border areas of Nuevo Laredo and Tamaulipas.

Mexico is also looking at creating multimodal complexes beyond the 66 already in existence. The objective is to have 124 facilities up and running by 2012. The corridors between the port of Salinas Cruz and Manzanillo will be upgraded to improve logistics output to Asia.

From a maritime perspective, Mexico is accepting bids to construct specialized container terminals at the ports of Manzanillo and Lazaro Cardenas.

In Brazil, improvements also focus on facilitating major trade lanes. To accommodate demand for ore from Vale Mining Company's Carajas mine, the country will invest US $7 billion in rail and port facilities within the next four years; $4 billion to upgrade its rail network; and $3 billion to construct a new port in Ponta da Madeira to expand export capabilities from northern Brazil. This will allow Vale to double its yearly exports through these facilities to 200 million tons by 2012.

Recently, Petrobras, the Maggi group, and the Amazon state government jointly constructed a $125-million private container port in the Amazon at Porto Velho, where barges take containers to the coastal port at Itacoatiara.

Despite these improvements, Brazil, Mexico, and Latin America in general, are far behind developed countries in terms of road, rail, waterway, and air infrastructure.

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*Marcio Stewart runs AGI, a logistics market research company, and heads a collaborative group of Latin American logistics experts that contribute to www.latinamericanlogistics.org*

# Pilot Pen Notes the Write Way to Outsource

## To distribute its quality writing instruments in Mexico, Pilot Corporation of America relies on its 3PL not just for storage and transportation, but also a competitive edge.

Trumbull, Conn.-based Pilot Corporation of America, the U.S. subsidiary of Tokyo, Japan-based Pilot Pen, has maintained a U.S. operation since 1970. The company is authorized by its parent company to sell in the United States and in Mexico. Since 2000, Pilot Pen Mexico, a Guadalajara-based business unit of Pilot Corporation of America, has been purchasing products made at the U.S. company's manufacturing and distribution facility in Jacksonville, Fla., and arranging for their distribution in Mexico.

"We sell pens to Pilot Pen Mexico, which then sells the pens and makes its own profit," says Juan Estrella, director of supply chain for Pilot Corporation of America.

Pilot Pen does business in Mexico without dedicating major corporate assets to the market by relying on Miami-based 3PL Ryder to distribute its Florida-made goods south of the border.

The full line of Pilot Pen writing instruments spans 12 different categories, including a variety of pens and pencils, creative markers, highlighters, and a mixed bag of supplies including refills, lead, and erasers.

Only a limited portion of the Pilot Pen line is distributed in Mexico. For example, "we don't carry No. 2 pencils. We sell mainly refillable pens and markers," Estrella explains.

Equally focused is Pilot Pen's geographic concentration in Mexico. While it directs distribution operations throughout Mexico, the company's primary market is the capital, Mexico City. Other major markets for Pilot Pen products include Guadalajara and Monterrey.

The pen manufacturer contracts with Ryder to select Mexican ground transportation carriers and to provide additional operational support. Ryder is particularly careful about screening, selecting, and monitoring Mexican motor freight carriers

serving Mexico City. Pilot Pen depends on motor freight carriers "that can consistently deliver to Mexico City within a certain time window," Estrella says.

Pilot Pen began its relationship with Ryder in Mexico four years ago. The company had relied on another logistics company to handle product distribution in Mexico until it filed for Chapter 11. Ryder took over the lease on an inventory-handling facility in Guadalajara, signing new contracts with most of the former customers who moved merchandise through the facility, including Pilot Pen Mexico.

The transition to Ryder went smoothly. "We didn't want to diminish customer service," Estrella notes. "That's always the scary part of a transition, wondering how long you are going to be down. We weren't down at all."

In making the transition to Ryder, Pilot Pen protected the short-term stability of its operations and the long-term viability of its distribution cost structure in Mexico. Ryder maintained smooth shipping to key markets and integrated its management information system with Pilot Pen's at minimal business disruption.

Ryder handles order processing, customer service functions, inventory storage and management, and shipment tracking for Pilot Pen in Mexico. In addition, Ryder provides services related to importing U.S.-made Pilot Pen goods in Mexico. "We have our own import broker," Estrella explains, "but Ryder does the follow-up." This includes ensuring that extra import documents are provided, if necessary, and that import duties are paid promptly so products quickly clear Mexican customs processing.

All Pilot Pen products sold in Mexico pass through Ryder's warehousing and distribution facility in Guadalajara, where security is a top priority. "There's no pilfering in Ryder's facility; it does a good job securing the inventory," Estrella notes.

## WORKING AS ONE

Maintaining open lines of communication helps the partners keep things running smoothly. Pilot Pen and Ryder employees hold weekly meetings to fine-tune the distribution of Pilot Pen products in Mexico. Ryder works so closely with Pilot Pen in Mexico that customers tend to see them as one company. The Ryder manager who supervises its facility in Guadalajara, for example, responds to calls from Pilot Pen customers as if he were a Pilot Pen employee. "He answers the phone, 'Pilot Pen,'" Estrella says.

Ensuring order execution is critical to keeping major customers and attracting new ones in Mexico. "When Pilot went into Mexico, we guaranteed our service, as we always do," Estrella notes. "Our culture is: we're going to get the merchandise there, wherever the customer wants it."

This dependability has been crucial in dealing with larger retailers. Office Depot, one of Pilot Pen's largest customers in Mexico, insists on timely order execution, which Ryder has delivered.

With Ryder at its side, Pilot Pen hopes to capture the business of another U.S.-based retailer in Mexico: Wal-Mart. "We've been approaching Wal-Mart for a few years, and recently got some positive feedback," Estrella says.

Pilot Pen may have nowhere to go but up in Mexico, given its short five-year presence in the market. "We're still in the infancy stage there," Estrella notes.

Holding down distribution costs in Mexico is critical to accelerating its growth, so Pilot Pen works closely with Ryder to develop efficient ways to do business.

## MEXICO

**GDP (OFFICIAL EXCHANGE RATE): $886 billion**

**EXPORTS: $268 billion** (manufactured goods, oil and oil products, silver, fruits, vegetables, coffee, and cotton)

**IMPORTS: $279 billion** (metalworking machines, steel mill products, agricultural machinery, electrical equipment, car parts for assembly, repair parts for motor vehicles, aircraft, and aircraft parts)

**EXPORT TO U.S.: 85%**

**IMPORT FROM U.S.: 51%**

**2006 U.S. FDI: $85 billion**

Mexico's own meteoric rise as a back-door distribution hub for the United States' capacity-choked West Coast facilities is mirrored in the expected growth of the Pacific port of Lázaro Cárdenas. Hutchison Port Holdings, which operates the single-berth port that began operations in 2003, has big plans for the up-and-coming container facility. With phase one of redevelopment complete, future plans will expand the complex to four berths, with a continuous quay length of nearly 5,000 feet, and increase container throughput to more than two million TEUs a year.

Sources: Airports Council International, CIA World Factbook, American Association of Port Authorities, and U.S. Dept. of Commerce Bureau of Economic Analysis

One potentially money-saving idea under consideration would let Ryder handle Pilot Pen order-taking in Mexico. Currently, Pilot Pen Mexico inputs customer orders into its own IBM server, an AS400 system, and the orders are then transmitted in a transfer protocol designed specifically for Ryder's management information system. The partners may combine their systems to boost efficiency.

As Pilot Pen has become more comfortable working with Ryder, the pen manufacturer has begun to consider funneling customer orders in Mexico directly to Ryder. That step would free Pilot Pen to devote more internal attention to other operations. And that's exactly the kind of freedom a good partner provides.

# Latin American Beat

News and Trends Shaping a New World Order

**Benetton and Sears Mexico** have signed an agreement to expand United Colours of Benetton (UCB) in Mexico, extending the brand's presence with a total of 250 points of sale in both Sears Mexico department stores and new stores by 2010. Under the agreement, points of sale offering UCB fashion and accessories collections for women, men, and children will open in Sears department stores across Mexico. With the additional opening of 50 new UCB stores, Benetton Group will reach a total of 250 retail outlets in just three years, decisively expanding its presence in the country. Furthermore, Benetton is locating new offices in Miami to serve as regional headquarters, and monitor the market and identify business opportunities in the Americas. The Miami branch will also establish a sourcing hub to serve the whole area, distributing, among other things, collections designed specifically for the region.

In an effort to tap growing global consumer markets and scale back growth in the United States, **Starbucks** recently opened its first store in Argentina. The Seattle-based chain plans to debut as many as four stores in Argentina by year's end. Starbucks already has coffee shops in seven Latin American countries including neighboring Chile and Brazil.

**Lakeland Industries**, a Ronkonkoma, N.Y.-based protective apparel company has completed the acquisition of Brazilian protective apparel supplier Qualytextil S.A. in an effort to sell directly into the country. Qualytextil markets products directly to major state-owned companies and agencies and the main oil and chemical companies in Brazil. As the latest addition to Lakeland's expanding international presence, Qualytextil's regional Brazilian operations, including manufacturing, sales and marketing, warehousing, and distribution, benefit from state-provided tax incentives, favorable labor rates, and proximity to economical transportation for garment distribution throughout Brazil and into neighboring countries.

Responding to strong demand from European and Latin American airfreight customers, **Panalpina** has launched a new service called Palmair. Using the Miami gateway, the Swiss forwarder offers a direct transshipment concept for destinations in Latin America in cooperation with its long-standing partner Centurion Air Cargo and a sub-contractual agreement with Cargolux. The two companies have established a link between Latin American connections, their European road feeder network, and Cargolux's Luxembourg hub. This setup gives Panalpina total control of the cargo flow from origin to destination. The service covers Bogotá, Medellin, Barranquilla (Columbia), Caracas (Venezuela), Lima (Peru), and Manaus (Brazil), among others.

**Temasek**, Singapore's state investment company, is targeting Latin America and the fast-growing economies of Brazil and Mexico in its latest phase of global expansion. The group, which holds stakes in both Merrill Lynch and Barclays, has targeted the Latin American region because of its long-term potential and attractive investment prospects. With more than 75 percent of its current investments based in Singapore and Asia, Temasek has switched its attention to the West as the credit crunch offers more opportunities for sovereign wealth funds.

**Ford Motor Company** announced its new Ford Fiesta small car and a sporty European hatchback model for North America sales would be produced at the company's Mexico City plant beginning in early 2010. Transformation of the Cuautitlan assembly plant near Mexico City begins this year as the facility transitions from its current production of F-Series pickups for the Mexican market to small cars for all of North America. Ford's Chihuahua Engine Plant, which builds I-4 engines, will also expand to assemble diesel engines for light- and medium-duty trucks in global markets. And, through a joint venture with German transmission manufacturer Getrag, Ford will set up a transmission plant in Guanajuato to support various products.

**Australia and Chile** have negotiated a free trade agreement (FTA), covering all agricultural products including Chile's most sensitive commodity, sugar. Government authorities expect to sign the FTA in late summer with the legislation to enter into action Jan. 1, 2009, pending ratification. Under the agreement, all existing trade will be liberalized by 2015. Two-way trade between Australia and Chile is currently more than $850 million annually and Australia has invested US $3 billion in Chile. This is Australia's first FTA with a Latin American country and augurs further trade growth between the two regions.