CHAPTER 4

MARKETING ENVIRONMENT FOR PALM OIL IN MEXICO

4.0 Current Marketing Situation

4.1 Market situation

Palm oil has the potential to be sold in the industrial market, reseller market and the government market as well. However, at the moment Malaysian palm oil exporters/producers do not seriously sell palm oil to Mexico. Palm oil were sold mostly to the resellers and industrial users through their agents in Singapore or Malaysia.

These resellers cum intermediaries are mostly the American-based trading houses like Conagra, Cargill, Louis Dreyfus and Pasternak. Itochu, the Japanese trading house, located in California (United States) also buys Malaysian palm oil and sell to the industrial buyers in Mexico. They buy oils and fats for the purpose of reselling at profit. For that reason they seek for the suppliers who can offer attractive price against the others.

The industrial users such as Andersen Clayton, the refiner and manufacturer of cooking and salad oils, margarine and shortening also buys Malaysian palm oil directly. This is a multi-national company (American-based) with huge capital, storage capacity of more than 10,000 tonnes of vegetable oil and other resources as well.

Many local refiners and manufacturers keep small stocks as the storage cost is very expensive especially after **CONASUPO** stopped channeling credits and subsidies to them. Therefore, most of them buy in small quantities with short reorder cycles. For that reason they buy from the trading houses. They also buy the least expensive oils and fats available, and then blend as appropriate in order to achieve the lowest cost product.

For the government market, it is becoming less attractive especially when the government opened trade to the business. The role of **CONASUPO**, a government agency which monitors imports of oils and fats has been reduced and the function is now taken by the private sectors especially the trading houses.

Under NAFTA, United States (U.S.) and Canadian suppliers will have 50% access to the Mexican government procurement market - including government controlled enterprises, up to 70% after an eight-year period and then lifting all restrictions after 10 years. [source: Exporters' Encyclopaedia,2000]. This present difficulties for Malaysian palm oil to penetrate the market as a "non-traditional supplier".

4.2 Product situation

Palm oil can be used in many food and non-food applications. In Mexico, palm oil is mainly used in blending with soft oils for most edible products such as cooking oil, margarine, shortening, filled milk and soap (blends with tallow). Palm oil/olein are also used for the industrial frying by organizations such as Bimbo, Sabritas and Gamesa.

With the tropical climate in the south and humid in the north and cold in the high lands, palm oil can replace other vegetable and animal oils and fats in a number of applications. However, the usage of palm oil in oils and fats application by the industrial users is still limited because many are still uncertain and not sure of the benefits of using palm oil as their ingredients.

In Mexico, for edible application most oils and fats are used in the production of salad/cooking oil (55%) and shortening (45%). Seed oils are normally used solely or in blends among them for salad/cooking oil while for shortening, they use lard, tallow or hydrogenated seeds oils exclusively or in blends.

Coconut oil, on the other hand, is consumed primarily by institutional food industry as ingredients in the shortening, candies and ice-cream, non-dairy milk and in laundry soaps.

In the consumer market, palm oil is never being sold as a consumer product because households are unaware of the feasibility of palm oil for daily consumption. Sunflower oil and safflower oil are widely used as cooking oils in this market.

They are sold under the Spanish names such as "Cartomo" and "Girasol". These oils have a positive image as healthy cooking oil among the Mexican people. Corn oil is highly perceived as premium brand/edible oil and marketed as a high-end product.

4.3 Pricing situation

In the Mexican oils and fats market, Malaysian palm oil was priced competitively with respect to sunflower seed and soybean oils from Argentina. In 2002, Malaysian palm oil was quoted at a discount of USD85 per tonne and USD44 to sunflower seed oil and soybean oil from Argentina.

However, total market demand for palm oil grew at a smaller rate compared to sunflower seed oil and rapeseed oil. This is probably due to the fact that palm oil is still new to most of the industrial users where the application is limited as compared to soybean oil, sunflower seed oil, coconut oil, rapeseed oil and tallow.

4.4 Competitive situation

There are about 14-16 oils and fats being produced, consumed and imported to Mexico. For imports, basically oils and fats can be sourced from the traditional and non-traditional suppliers. Traditional suppliers such as United States, Argentina, Brazil and the European countries are the major sources of soybean oil, sunflower seed oil, tallow and rapeseed oil.

The use of GSM-102, PL 480 credits, EEP, SOAP, COAP and CCC have had a major impact on the U.S share of the total market eventhough they are meant for the government buying. The use of SOAP and CCC for examples has made Mexico a major market for U.S. sunflower seed oil and tallow.

The use of these programs, along with the presence of major U.S industry groups in Mexico has provided the needed support for increasing sales of U.S vegetable oils in this market. Argentina, Brazil and European Union (EU) do subsidize their vegetable oils exports. Malaysia does not offer any credits arrangement to Mexico.

Several oilseed and product cooperator organizations are actively engaged in marketing activities of the wholesale vegetable oils trade in Mexico. Among them are the National Cotton Seed Products Association, the National Peanut Council of America, the National Sunflower Association and the American Soybean Association.

Only selected oil suppliers advertise on a regular basis, while even fewer differentiates between products. This occurs because the marginal cost of advertising is not worth the returns to suppliers [source: Agricultural Affairs Mexico Report, 1992].

In the palm oil market, Malaysia has to compete with Costa Rica, Indonesia, Colombia, Equador and other palm oil producing countries. Malaysian palm oil industry through its Promotion Council (MPOPC) and Research Institute (MPOB) have taken several steps in promoting Malaysian palm oil in Mexico to make the oil more acceptable to the Mexican.

4.5 Distribution situation

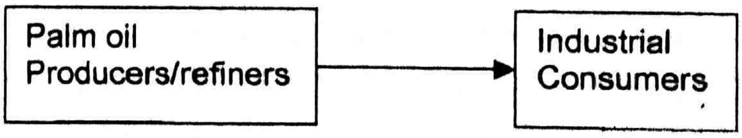
In pursuing for the market entry strategy most Malaysian palm oil refiners or producers are exporting directly to foreign intermediaries such as the American based trading houses for the Mexican oils and fats market.

Channel distribution for small industrial buyers in Mexico.

They are the private entities and very much important sources of supply for oils and fats especially to the small (Mexican) industrial users. They have the ability to break-bulk, giving credits, are equipped with storage, handling and transportation facilities and then sell the oil through their own sales forces.

For the major industrial buyers, they buy directly from Malaysia. No intermediaries involved in getting the supply of palm oil.

Channel distribution for major industrial buyers in Mexico.



Palm oil is only a small part of the oils and fats portfolio sold by these trading houses. They carry a large portion of soybean oil, sunflower-seed oil and other oils and fats from other countries in the world. Palm oil purchased is put in the same storage tanks where other oils and fats were stored.
Malaysian exporters/producers are only responsible for the shipment of palm oil from Malaysia to Mexico. All the marketing activities for the palm oil in Mexico are left to these import traders.

4.6 Foreign marketing environment – Mexico

The foreign marketing environment that consists of demographic/social/cultural, economic, political/legal, and technology/physical could present opportunities as well as threats to Malaysian palm oil in Mexico.

4.6.1 Demographic/Social/Cultural environment

The demographic trend of the last 30 years reflects a significant decrease in population growth. However, there is a decrease in mortality rate as the result of better medical, welfare and education services and to more extensive coverage of national health programs. In 2002, the population reached 101.8 million inhabitants.

Spanish is the official language in Mexico and English is the language most widely used in transaction with foreign countries. About 8% of the total were speakers of native languages. The states with the highest percentages of speakers of Indian languages are Yucatan, Oaxaca and Chiapas.

It is a young country and almost 80% of the population is under the age of 40, predominantly catholic (89.7%). About 71% of all Mexican live in urban zones as against 29% in rural areas. Today, 38% of the country 's population can be found in the states of Jalisca, Nuevo Leon, Puebla and the Federal District where

Mexico's four principal metropolitan centers are located. [source: Business Mexico, 2000].

Mexico still resembles a developing country. According to some recent studies, half of all Mexican cannot afford the nutritional minimum prescribed by the Food and Agricultural Organization (FAO) [source: Business Mexico, 1999]. About 10% of Mexico's current population is wealthy, 45% are middle class, and the rest are undeniable poor. On the other hand, almost every household has at least one television [source : Marketing Business, Dec.1999 - Jan. 2000].

In 1991, the estimated size of the Mexican labour force was 31.5 million of which two-thirds is male, less than 40% of the total population. This low participation rate reflects the fact that a large percentage of the population is under 15 years of age.

Mexico's workers earn low wages and according to the 2000 statistics, nearly 60% lower than Southeast Asia, 70% lower than Western Europe and 80% less than the United States .

Mexico has a literacy rate of about 90% and according to the1990 census, 88 of every 100 inhabitants over 15 years of age knew how to read and write. University graduates are somewhat more engineers per capita than does the United States (Harvard Business Review 2000).

However, there were still shortages of Mexican executives [source: Harvard Business Review, 1999]. Just as hiring local managers can form an important base of cultural expertise, provide access to established distribution networks and build on political and personal relationships that can make or break a company in Mexico.

Business in Mexico is conducted at a personal level. The establishment of relationship between buyers and sellers is as much important as establishing a business deal and this normally consumes a lot of time, energy and money. In many cases, business is conducted through the referrals.

Negotiating styles differs in certain parts of Mexico. The northern part of Mexico, due to proximity and a history of trade with the United States, are more used to American style of business. Mexican society on the whole puts a premium on politeness.

La Mordida or "the bite" as bribery is known in Mexico, and is practically a way of life. This is due to the lower pay they get and although the situation is improving and request for bribes are not as brazen as in the past. The emphasis that Mexican culture puts on politeness also contributes to some people 's reluctant to say "No" if they cannot fulfil the requirement. To the Mexican an outright "No" is considered rude [source: Importing from Mexico, 1991].

4.6.2 Political/legal environment

Most of Mexico's protectionist policy was set in place after World War II to bolster its domestic industry by instituting high tariff and other economic barriers to foreign products.

When Mexico was left with ballooning federal deficits, crushing foreign debts, triple-digit inflation, antiquated industries and escalating urban poverty in the early 80s, the government at that time under President de la Madrid, took a painful process of rebuilding the Mexican economy from state control to open market system.

Further reformation process has taken place when Mexico joint GATT in 1986 and the effort continued when Mexico was under president Carlos Salinas de

Gortari. "**Trust" mechanism** have been created to allow majority foreign participation in regulated industries, to open Mexico's capital market, and to extend the term for foreign ownership of property in the coastal and border regions.

Agricultural liberalization, possibly the most radical and far-reaching element of the reform package. A new agrarian reform act was passed in 1992 which allows "ejidal" communities to transfer ownership of their land or lease to private enterprises or corporate entities. The other major area of agricultural policy reform was the liberalization of agricultural markets; trade and price liberalization, reduction and elimination of input subsidies and reduction of state intervention.

Credit grants for agroindustry was expected to increase by 30% from 1992. The objective to channel the credit is to support the food processing industry resulting from the amendments to Article 27 of the Mexican constitution that have made it easier for farmers to enter into partnership with entrepreneurs.

Import tariffs was reduced to 20% (max) ad volarem from 100%. Generally all refined edible oils are subjected to 20% and crude at 10%, however there are some preferential of tariffs. Import from NAFTA countries are charged 18% and 9% for refined and crude oils respectively. Imports from Latin American Integration Association (ALADI) member countries are however duty free.

The government has also reduced non-tariff barriers by reducing license requirements to less than 20% of imports (at present, 192 of 11,835 are subject to prior import permits) and quotas on most imported products.

Apart from that, the Mexican government also provides Investment Incentive Programs such as Export Development Programs, Immediate Investment Depreciation, Facilities to Purchase Land in Some Federal States and Development Bank's Venture Capital Programs.

PERPUSTAKAAN UNIVERSITI MALAYA

AS11704748

In 1994, the government has substantially relaxed Mexico's once strict restrictions on foreign direct investment. In most economic activities in the country, foreign investors may own up to 100% of stocks in a company incorporated in Mexico. Activity like production cooperatives will be limited to a maximum 10% share. Further, Mexican companies established by foreign investors may own real estate in Mexico.
Corporate tax of Mexico is 34% which is higher than Malaysia of 28%.

The rate applicable to the value added tax is generally 10%. However, the sales of milk, dairy products, vegetable oils, shortening, palm, exporting goods and services are exempted. Dividend distribution is not subjected to paying the corresponding tax, provided dividends are taken from profits after having paid income taxes.

Payments related to royalties for technical assistance, patents, commercial brands and names are all subjected to a 15% tax. There are also state and municipal taxes where in 18 states, a special tax is imposed on payrolls and property.

The policy of the monetary authorities is to let the exchange rate float freely within a band (without the Central Bank's intervention). There is no restrictions on remittances abroad of profits, royalties, dividends and interest paid on loans or capital repatriation. Companies may open checking and deposit accounts in US dollars anywhere in the country, subject to a minimum opening amount defined by the commercial banks.

Other rules and regulations governing the business in Mexico are:-

a) Environmental law.

All new industrial projects, whether undertaken by domestic or foreign investors, are subjected to an environmental impact study before the construction phase. Compliance with environmental law is mandatory for all businesses engaged in activities that emit gases, odors, solid and liquid particles into the atmosphere.

b) Patents, Trademarks and Copyrights.

The Industrial Property Law and recent amendments to the Copyright Law provide additional safeguards for business operating in Mexico.

c) Competition policy

Federal anti-trust laws are contemplated in the Mexican constitution to prohibit unfair business practices in general.

d) Labour legislation

It states the maximum working hours per week, overtime compensations, vacation premiums, termination and retrenchment benefits, maximum test periods, the mandatory social benefits, and wage reviews which are established based on agreements regulated by the Federal Labour Law.

e) Immigration law

To facilitate the residence of foreign investors, officers and technicians in Mexico, the authorities in Mexican consulates abroad are authorized to issue the corresponding visas; "business visitor", "investor visitor" and "professional visitors" visas [source: Doing Business in Mexico, 2000].

Mexico's policy of deregulation is vital, as the secretary of state and industry, Jaime Serra Punche, writes in the 1994 World Economic Review, "As long as the economy remains over-regulated, it cannot reap the full benefits of trade liberalisation".

Mexico is still saddled with corruption, terrorism and drug trafficking.

4.6.3 Economic environment

Despite of tremendous economic reforms undertaken since the 80s, Mexico is now again facing financial crisis caused by lack of liquidity to pay their short-term debts. Too much dependence on the - *hot money* - for the country's development, mismanagement of its current account deficit and foreign trade deficit are the major attributes towards the crisis.

4.6.4 Technological /physical environment

Mexico currently, has a network of 242,000 kilometers of main and secondary roads and 26,400 kilometers of railroads. However, many east-west roads are especially poor which resulted in long delivery times and high logistic costs. Although, trucking costs have dropped about 50% since Mexican deregulation in 1989, freight rates remain about three times higher than in United States [source: Harvard Business Review, 1999].

It is also served by 82 airports as well as by 76 maritime ports. For oils and fats purposes, incoming vessels are conducted at Veracruz port only in Mexico where there are adequate facilities such as bulky installations for storage purposes and proper material handling facilities or else exporters can use Brownsville port in southern United States for that matter. Other ports which have the facilities to handle oils and fats cargo are Manzanila and Altamirano.

The communication systems are still poor. For example, letters from United States can take weeks to arrive while routine communications require the use of fax machine or express delivery service. In the telecommunication networks, even the country has made a substantial progress in the field of telecommunications in order to meet the needs of industry, commerce, science and education, telephone service is still inadequate and expensive.

Companies can experience long delays in acquiring dedicated line for computers communications and fax machines [source: Harvard Business Review, 1999].

The nation's needs for electrical energy are met mainly by hydroelectric and steam-powered plants. The electrical systems operates at 110 volts with frequency of 60Hz., comparable to the electrical standard throughout North America. Still, in several parts of Mexico, for example, in the state of Chiapas, the infrastructures are not being well developed as compared to the northern parts of the country.

4.7 Domestic marketing environment - Malaysia

The domestic marketing environments of Malaysia such as political/legal, economic and natural factors may affect the current performance of Malaysian palm oil exports to Mexico.

4.7.1 Political/legal environment

The government has been supporting the oil palm industry since 1950s and eventhough today, manufacturing sector shares a bigger contribution in the GNP; agricultural sector is somewhat of equal importance.

In facing the future challenges, palm oil industry is encouraged to further incorporate more downstream activities. According to Datuk Seri Dr. Lim Keng Yaik, "the plantation sector can rest assured that its effort to integrate agriculture and manufacturing activities, which is the future trend, will be fully complemented by the government" [source: Business Times, March 29, 1995].

As one of the source of revenues, the government has not imposed export duty on processed palm oil. The decision not to impose the export duty is to enable Malaysian palm oil to compete worldwide especially when selling to countries which are still imposing high import duties on Malaysian palm oil such as Mexico.

4.7.2 Economic environment

Malaysia's economic performance is among the robust developing countries which has successfully achieved growth by 4.2% in 2002 as compared to 0.4% in 1991 and is expected to achieve 4.5% for the year 2003.

Looking into foreign trade between Malaysia and Mexico, even though it is still small, there is an increasing trend for trades between the two countries. For 2002, trade is very much in Malaysia's favour as Malaysia's total exports to Mexico worth RM2.153 billion as compared to imports of RM0.514 million from Mexico [source: Monthly Statistical Bulletin , December, 2002].

4.7.3 Natural environment

The labour market, improve in 2002 with total employment rising 4% to 9.8 million from 9.5 million in 2001. The labour force, however, grew at a slower 3.0% from 4% previously.

On a sectoral basis, the manufacturing sector and the service sector registered growth of 4.1% in 2002. The agricultural sector grew only at 0.3 %. [source: Bank Negara Malaysia, Annual Report 2002]. Labour shortage problem especially in the plantation sector which could impede the planting works and affect the whole processes of supply limit the growth of the plantation sector.

Another problem faced by the industry is the limited land area for oil palm cultivation. Before this, the expansion of plantation area under oil palm was largely at the expense of rubber. Even though, Sarawak and Sabah have substantial land reserves, the cost of developing it is very expensive.