Operating in Mexico:

Effective cash and treasury management south of the Rio Grande

Before you decide to expand your business under the sunny skies of Mexico, you can save yourself some real headaches by taking a close look at the cash and treasury management services you'll need on the ground there and doing some advance planning to deal with them.

By Michele Royliston

IN THE PAST FEW YEARS, WE HAVE SEEN A SURGE IN THE NUMBER of Canadian companies interested in doing business in Mexico. Much of that interest is certainly attributable to the 1994 North American Free Trade Agreement, which is dismantling trade barriers and making it easier to do business in Mexico.

The Maquiladora zone near the U.S. border is another factor. Firms operating in the zone can import parts, assemble products and then export them, paying tax only on the value-added in Mexico. It has proven to be a real draw for many large U.S. and Canadian manufacturing plants. Canadian suppliers are locating in the zone to be as close as possible to their customers.

Mexican labour costs are as much as 80-per-cent lower than Canadian wage rates; the business climate is favourable, and Mexico is close to major American markets including California, Texas and Florida. Plus, the Mexican market is large and increasingly important in its own right, with 90 million people and a growing middle class.

It all adds up to a sunny business climate, one that is increasingly hard for many companies here to ignore. In fact, companies of all sizes are expressing interest and incorporating a Mexican presence into their business strategies. We are seeing Canadian companies exporting directly from Canada, establishing distribution facilities, acquiring Mexican companies or building their own plants in the country.

Operating in Mexico presents a number of challenges for treasurers and finance staff. To be successful with a Mexican venture, treasury staff must deal with the challenges of:

- the banking and business environment;
- managing funds in Mexico, and
- controlling Mexican interests from Canada

The banking and business environment: One of the surprises facing many Canadian firms after they establish a presence in Mexico is how much different the culture is as it relates to business and banking.

Language is the most obvious difference, and that alone presents some real challenges. Business is done in Spanish, and financial documents must be filed in that language. It's vitally important to have access to someone who speaks your language to assess your needs and help guide you through the process of establishing a banking relationship and services.

But language is only one of many differences — both subtle and not so subtle — in the way business and banking is done in Mexico. Most have a direct impact on cash and treasury management.

For instance, in Canada and the U.S., we refer to invoices as "receivables," and the onus is on the company that purchased your goods or services to pay.

In Mexico, invoices are referred to as "collectibles." It's up to the company selling the goods or services to collect the money. To do that, it must make it as easy as possible for the purchaser to pay. The more difficult it is to pay, the longer it takes the seller to collect.

Simply dropping a cheque in the mail isn't the way most invoices get paid in Mexico. In fact, the mail is notoriously unreliable. It takes a long time for a payment to make its way through the system to your desk. Even when it does, there's a good chance the envelope may have been opened and the cheque removed.

Although electronic banking capabilities are growing rapidly, many Mexican companies still have their clerks pay invoices in person at the bank of the company that issued them. Without an arrangement with a Mexican bank with a significant branch network, the difficulties are immediately apparent.

To facilitate payments, some Mexican banks offer a "bill presentment" system, through which a company sends details of its invoices sorted by creditor to its bank. A creditor can go to a branch of that bank, find out exactly how much is owed and make payments against specific invoices. These payments are immediately credited, and the information is made available online to the company issuing the invoice.

Adding to the list of cultural differences that can pose some real cash- and treasury-management challenges is that the vast majority of Mexican workers prefer to be paid in cash, a situation virtually unheard of here. Most Mexican workers don't have or want a bank account.

Paying in cash doesn't present much of a problem when you have a handful of employees, but when you have hundreds, or even thousands, of assembly-line workers, it can become a major hurdle. Some Mexican banks offer payroll services. They take a company's payroll register, put the appropriate amount of cash in pay envelopes together with pay stub, address it to the employee and deliver the cash payroll by armoured car to be distributed in the plant. Depending on the size of your payroll, the service offers some obvious and significant benefits.

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Last, but far from least, is cheque fraud. While the situation is improving, cheque fraud remains a major concern for Canadian companies of all sizes doing business in Mexico. For smaller companies operating in the country, a successfully executed fraud can be disastrous.

It has been common for the same cheque to be cashed more than once or for counterfeit cheques to be cashed. To combat such fraud, companies doing business in Mexico send cheque registers to their banks and have the banks confirm that the cheque presented is valid by comparing various fields in the cheque against the register.

Managing Your Funds in Mexico: It can also come as a surprise to some Canadian companies that most Mexican banks do not offer automatic zero-balance accounts. For companies with more than one Mexican location, it's an especially useful cash-management tool that minimizes parent-company funding requirements by making the most effective use of all revenues generated in Mexico.

Zero-balance accounts allow companies to use pesos generated by operations in one location to meet obligations in another. Only when the concentration account is in a negative position are funds required from Canada.

There are any number of examples of Canadian companies receiving urgent calls from one of their Mexican controllers requesting a fund transfer to meet payroll or some other obligation the next day. After the funds are transferred, head office often finds that more than enough funds were available in an account at another subsidiary.

Zero-balance accounts allow Canadian head-office staff to minimize funding requirements to Mexico, which in turn limits the parent company's foreign-exchange exposure.

Monitoring the concentration account provides a picture of the overall status of a company's funds in Mexico. With that information, head-office staff can more effectively move and use those funds, both in Mexico and in other operations around the world, to maximize returns.

Controlling your business from Canada: While the differences in culture and banking services can be substantially different than those in Canada, many of the top-tier Mexican banks are equal to Canada's in one area — their ability to provide electronic banking services.

This offers Canadian companies of all sizes two significant benefits: access to timely information and head-office control over funds in their Mexican accounts. Canadian head-office staff can walk into the office in the morning and know immediately what cheques were cleared through their Mexican accounts the night before.

Electronic banking systems also offer varying degrees of control. For example, some companies impose total head-office control on their Mexican accounts and approve every expenditure electronically. Most others are content with lesser degrees of control. Some companies want daily access to account status information, while others opt for something less.

Some companies limit risk by placing daily and monthly limits on the amounts that can be disbursed from a particular account. For example, you could specify that no more than 100,000 pesos a day, to a total of one million pesos a month, can be disbursed from a specific account, permitting subsidiary offices a degree of flexibility and autonomy while limiting a company's exposure and offering additional peace-of-mind.

Companies can also exercise their head-office control to repatriate funds in their Mexican accounts when they are needed, a major advantage especially for smaller companies doing business in Mexico.

A changing business culture: The business culture in Mexico has been changing. As a result of NAFTA, it is moving closer to Canadian and American ways of doing business. This is especially true in the area of electronic banking, where cash management services are as sophisticated as any in the world. Business strategy and not cash- and treasury-management considerations will be the primary factor in a company's decision to begin operating in Mexico.

That said, many Canadian companies don't worry about or even consider the cash-management challenges presented by very real differences in culture, business practices and banking services. It's only when the subsidiary has been established that the impact and the cost of those challenges become apparent. The choice of the right banking partner is the key to meeting many of those challenges.

Canadian and Mexican financial institutions are developing or have in place a variety of banking and cash-management arrangements for customers doing business in Mexico. For example, Scotiabank has developed an arrangement with our affiliate, Banco Inverlat, Mexico's fourth-largest full-service bank. Customers work with their Canadian account manager to assess their business needs and arrange their Mexican cash-management services. Because Inverlat has some 340 branches across the country, it can provide the services a Canadian company needs, from collection and cash concentration to payroll and cheque-protection services. Banco Inverlat is also a leader in the provision of electronic banking services, which allows customers to manage their Mexican operation locally or from a Canadian head office.

The bottom line? Making the right banking arrangements, the ones that will suit your specific needs, is a vital element in ensuring a successful venture in Mexico. If you're going to do business in Mexico, spend some time to find a banking partner who can meet your needs in Canada and on the ground in Mexico. You'll be happy you did.

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