

Channel Market Strategies in the Mexican Water Segment (Part 1)

Channel market strategies are vital in all industries in all countries. However, if you are a foreign company trying to sell products into the Mexican water sector, they are even more important. As the previous article on government procurement mentions, Mexican law requires that all sales to Mexican government entities (federal, state, municipal, parastate) be carried out formally by a Mexican company. So, unless you have an office in Mexico, this means that selling to the Mexican government without a Mexican intermediary or a Mexican Corporation is technically illegal. If we divide the Mexican water sector into public and private opportunity areas, approximately half of the opportunities (public) cannot be sold direct or via a representative or agent. On the private sector side, no such barriers exist. However, questions of service, regulatory issues, credit, and payment make it so that selling direct in many cases is not optimal or even desired. Therefore, most US companies wanting to sell to the Mexican private sector start by selling indirectly through distributors, reps or agents, and Partners in the market.

Following are the most common channel options for a foreign company manufacturing water products or providing water services in the Mexican market.

Direct from abroad vs. Indirect sales via a local intermediary

As mentioned above, except in some rare exceptions, direct sales by a foreign company is not an option for sales to the Mexican public water sector at any level. Also, even if these legal restrictions were lifted, Mexican government officials would prefer dealing with Mexicans and Mexican companies. On the private sector side, first sales by a company to Mexico generally consist of reacting to a request from an end-user or reseller in the country, accepting an upfront payment, and shipping the product to Laredo or El Paso. While these types of sales might work without a Mexican intermediary, companies have to ask if many of those sales to the border repeat themselves or are of a size that is truly interesting to the company in the medium and long run.

Nonetheless, selling direct can be viable if not in some cases a necessary evil. If the value of the product and the size of the market and its potential are considerable, a foreign company might want to sell direct to meet pricing requirements or to avoid having to share margins, and it might have to do so if said products are unique to the market and cannot be serviced locally. However, in these cases, the company has to want to do this and it has to have employees with the time and cultural, language, and technical skills to make it work, something which many almost no small companies, few medium size companies, and not all large companies can count on.

While cutting costs and eliminating the middle man is important, that strategy in Mexico too often results in a considerable reduction in sales as well – not a tradeoff that a sound business will make. Likewise, the hidden costs associated with this move for most companies end up being more

expensive than sharing margins with an intermediary. Sales and service support, in-country logistics and inventory, regulatory issues, credit extension, and accounts receivable are a few of the more obvious areas that a foreign company may have problems addressing in a more cost effective manner than a local intermediary.

In the private water sector, the above issues are even more valid than for more general merchandise. B2B water product and equipment sales tend to have important installation and/or service components. However, the manufacturer can generally count on being able to teach its intermediaries to handle these situations.

Local Distributor

The most common and often the best intermediary option in the Mexican water sector is using a local distributor or distributors – selling to a Mexican company that buys, imports, and resells your product to the end-user.

Because Mexico was such a protectionist market prior to NAFTA, many Mexican companies were vertically integrated. They manufactured and sold their product in the market without having to share margins with intermediaries. Those manufacturers that used intermediaries almost exclusively relied on distributors. The buying and reselling of product at a profit is more of the traditional entrepreneurial mindset in Mexico. In part this was because of a lack of trusting manufacturers to pay commissions, the lenient bankruptcy rules in the country allowing small companies and individuals to take on the risk and reward of distribution vs. representation, and the need and ability to make larger margins as a distributor.

With the new government procurement national content regulations, if you try selling your product by itself through local distributors, you will not be able to sell your products in the majority of cases. As a result, signing a distributor to sell your product into the Mexican public water sector will, most of the time, be a waste of time. On the private sector side, distributors are the preferred way of selling at this time, both in general and in light of the underdeveloped rep and agent situation in the country. The advantage of working with a distributor is that they will (or should) hold stock in the country, they normally assist with marketing and after sales service, and most importantly, they take on the credit and payment issues. That being said, if your distributor sells a bunch of product with credit to non-creditworthy clients, both your company and your distributor will have to bear the payment problem burden.

When product is low in value (less than \$5,000 US), is a commodity, a replacement part, if stocking is required or broad market coverage is needed, then a distributor is generally the best option. However, if you need to control prices and margins to be competitive, if you feel the need to control branding and marketing, if you need your intermediary to not carry competitive product, and if you need for your intermediary to broaden its focus to cover your new lines and do some business development and not just be an order taker, then a distributor is probably not going to be your best option in the Mexican private water sector.

Local Rep or Agent

In a perfect Mexican world, where payments are fluid and stocking products locally is not required, everyone should want to work with a rep or agent – selling to a Mexican end-user by means of an

intermediary that finds and services the client and receives a commission when the client pays. A rep provides the best of both worlds: control over your pricing and marketing, service assistance, and someone locally with vested interest in seeing that you get paid. Also, reps tend to be more Business development orientated and not order takers like so many Mexican distributors can be. Reps will also generally work with fewer products and therefore afford your product the time and attention that you feel is necessary for success in the market while distributors might not even make an effort to sell your product if it does not fit nicely within its current channel and customer focus.

The good news is that with the push to avoid high, sometimes almost usury distributor mark-ups, there is a tendency for industrial clients to want to go direct, something which makes the rep/agent in greater demand. The bad news is that there is a dearth of reps in Mexico. Those that do exist are small companies or not companies at all, mostly ex-employees of companies that used these products who realized the potential for the product to be sourced from the vendor in a different, more efficient way. Wisconsin's Trade Office in Mexico is an active member of MANA (Manufacturers & Agents National Association) and has done studies for it, the most important rep association in the US, and determined how reps and rep agencies are few, extensively underdeveloped, and very hard to locate. Some distributors have tried creating a rep division inside of their operations, some in anticipation of these changes and others as a direct result of requests from US companies who want them to rep their product rather than distribute it. These efforts have had mixed results to date.

In the next edition of the Quarterly, we will discuss integrator, strategic alliance, and subsidiary office pros and cons as well the important issues of exclusivity and the usefulness and limitations of channel carrots and sticks in Mexico.