Background Report on Mexican Furniture Industry

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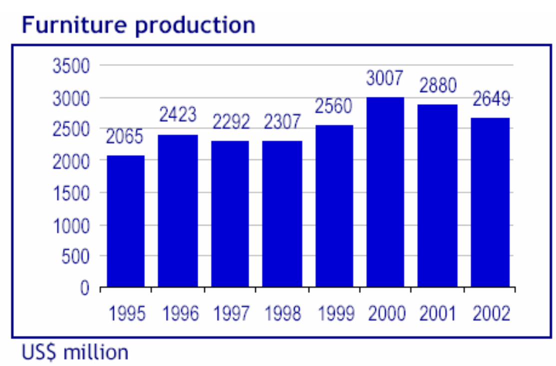
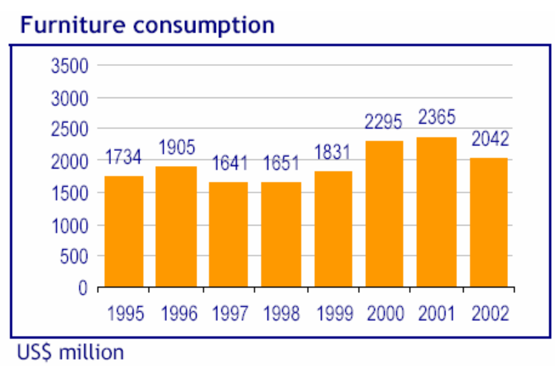
This report provides a background on the Mexican furniture industry. It relies partially on many statistics from a report compiled by the Italian firm CSIL Milano (CSIL Milano, 2004). Charts included here also come from this report. Many other statistics were obtained and computed by the author from other sources. This report, created using statistical information and further research into the industry, provides a background that will put into perspective the analysis of Mexican consumers and recommendations for action that will be provided in the second section of the study.

Broad Macroeconomic Situation

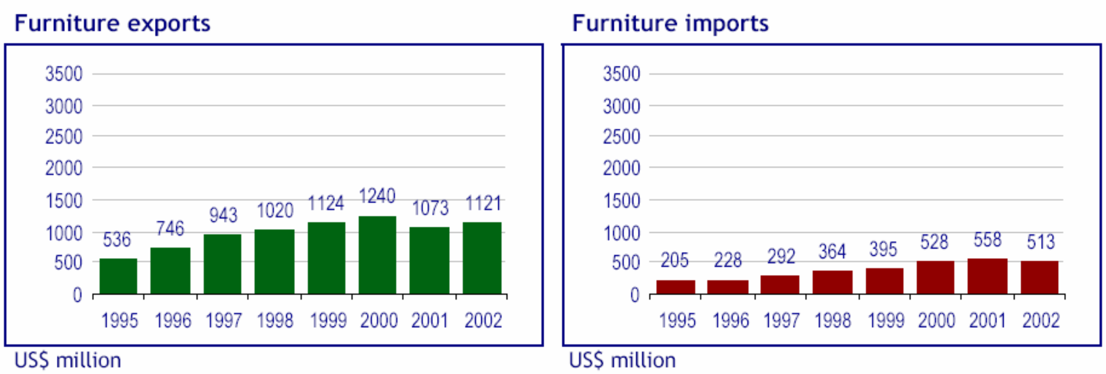
The first set of tables presents overall figures. Mexican production and consumption in recent years has displayed a general upward trend, but this effect is not monotonic. The downward trend in consumption in 2002 might be attributed to the difficult economic conditions in Mexico that began in 2001.





It is important to note that through 2002, exports had been a bright spot for Mexico. Roughly 42% of its production is exported, principally to the United States. These figures do include maquiladora operations, but those plants account for only 5% of establishments, suggesting a relatively minor role in exports (CSIL, Milano, 2004). It is noteworthy that in the seven years from 1995 through 2002, production has increased at an average annual rate of 3.6%, while exports have increased by 11.1% annually. This indicates a level of success on the part of Mexican industry in reaching external markets.

We do not yet have the data to ascertain whether this trend has continued, or whether Mexican exports have faced resistance as Chinese imports continue to rise. One data point indicates that exports were the same in 2004 as in 2002 (Zayas, 2005). The very strong dependence on the United States as a market for Mexican furniture (shown in the table below) could create a vulnerability should other nations improve access for their goods in the U.S. Even with this dependence, Mexico is the leading exporter to countries in Central and South America, according to CSIL Milano. With respect to imports into Mexico, the annual growth of 14.0% indicates increasing penetration of the home markets is occurring, a cause for some concern. One report indicated that manufacturers in Jalisco witnessed a 70% decline in sales to the United States (AII Data Processing Ltd). Such a number is high enough to warrant independent verification. Another source that signaled pessimism (Zayas, 2005) reported that 67% of Jalisco manufacturers saw their economic environment as adverse, with only 5% seeing it as favorable. These are clear warning signs for the industry. Near-term performance of this level would be inconsistent with the overall upward trend of Mexican exports. Preliminary World Bank statistics (World Bank, 2005) indicate that in 2004, exports of manufactured goods rose by 12.7%.



Tab. 1.1 Mexico. Main furniture trading partners

Destination of furniture exports		Origin of furniture imports	
United States	94.1%	United States	58.2%
Germany	1.4%	China	11.0%
Canada	1.2%	Italy	6.4%
Spain	0.5%	Spain	4.5%
United Kingdom	0.4%	Taiwan	4.3%

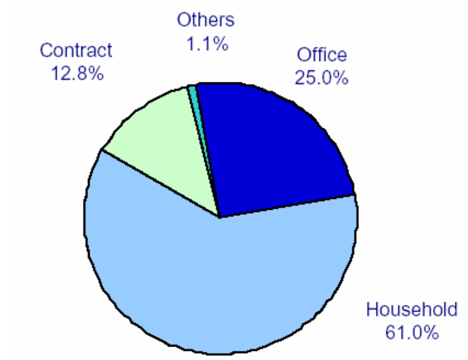
Source: CSIL

This export push of the Chinese furniture producers has created angst in the United States (Buckley, 2004) but also in Mexico: imports of Chinese furniture into Mexico have risen from $5.3 to $56.6 million in the years 1997 to 2002, an annual average increase of 40.2%. One report had imported of furniture into Mexico surging 78.7% during just the year 2003 (Data Process, 2004). Chinese overall furniture exports in the first half of 2005 rose at an annual rate of 32.5% (Comtex, 2005), suggesting continued export strength.

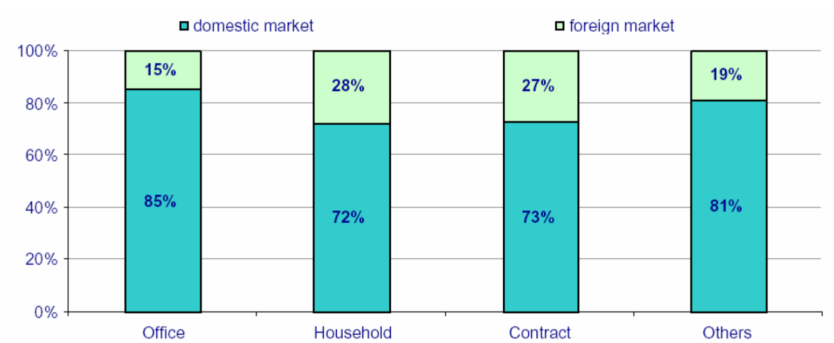
The Structure of Demand in Mexico

As illustrated above, demand has fluctuated somewhat in Mexico. The breakdown of types of furniture that are in demand is shown in the pie chart below. The bar chart below provides insight on the extent to which each of these markets has been developed for export. Since much office furniture is metal, this section of the market may be difficult to access for wood furniture manufacturers, but the other markets are theoretically accessible.

Furniture production by product
1998 Figures, by Value

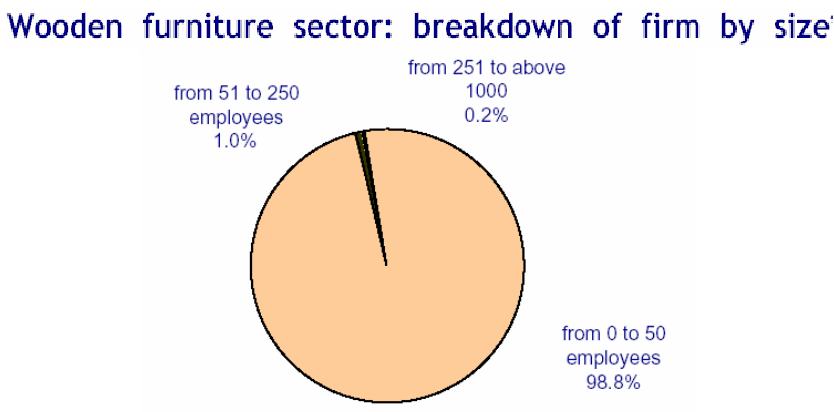


Furniture sales by market of destination
1998 Percentages, by Value



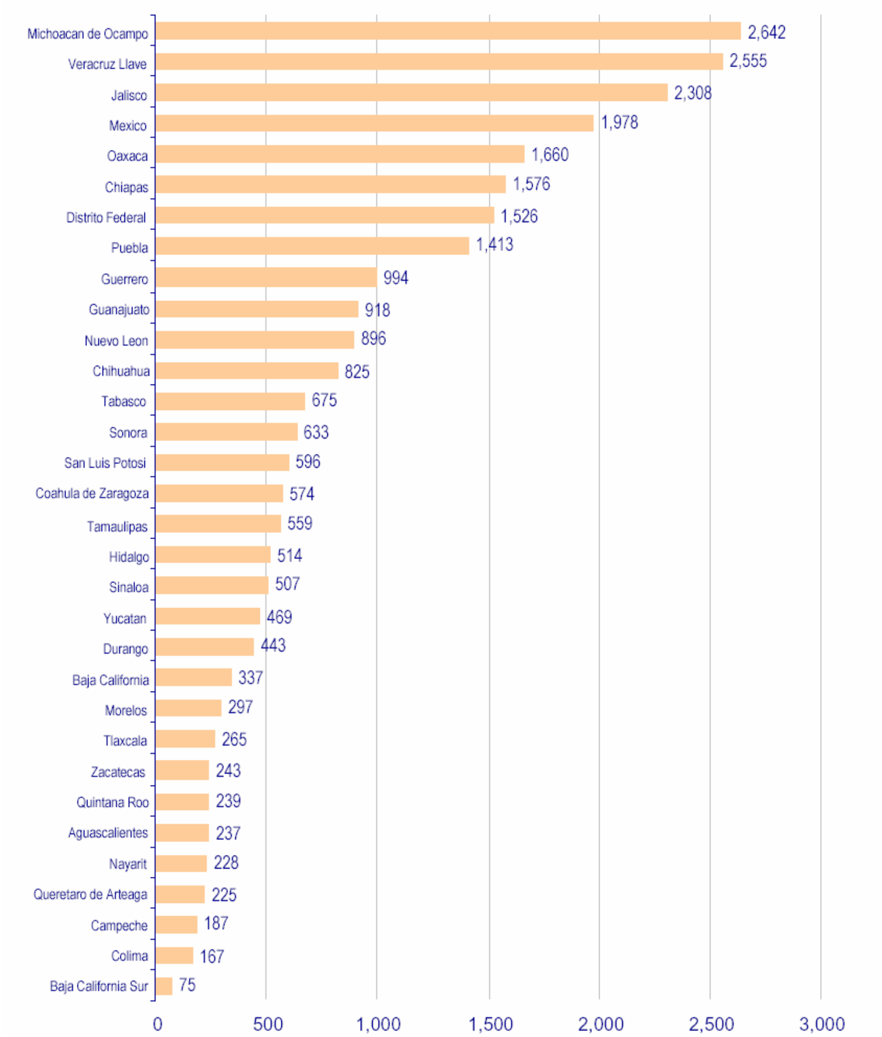
The Structure of the Industry – Manufacturing

Mexico's furniture manufacturing industry is highly fragmented, with 82,000 different establishments in existence as of 2002 (CSIL Milano, 2004). The chart below shows that the vast majority of companies have less than 50 employees. It is important to note that this chart illustrates the number of companies, not the level of sales by those companies. If the latter were to be used, the slices attributable to the larger companies would be significantly larger. But by any measure, the industry would still be categorized as fragmented. In this sense community unions and ejidos do not face overwhelming disadvantages in scale economies; their cost structure may be similar to industry norms.



The geographic location of manufacturing is similarly dispersed. Figures presented here come from the Census, to which companies with 50 or more employees and $175,000 in sales must report Looking at the number of companies, the following distribution emerges. The results show that of 25,761 such companies, the most in any one state is roughly 10%. This reflects Mexico's broad endowment of forests, and indicates a multitude of possible downstream buyers for certified lumber products.

Wooden furniture sector: number of companies by state



One clear problem for Mexican manufacturers is investment in the type of technology necessary to maintain their place domestically and especially, internationally. Zayas (2005), studying Jalisco manufacturers, found that 76% did not plan to invest in the near future, and of the 20% that did plan to invest, the average amount was only $11,030. Problems may also be due to prior investments; 19% of manufacturers reported problems with their existing technology. This is a very serious concern, given the strong tendency of the Chinese to invest in first-class manufacturing facilities. These plants also enjoy greater economies of scale, as there are only four or five furniture manufacturing plants in Mexico that can come close to the volume that can be produced in Chinese factories (Zayas: 2005:6)."

The Structure of the Industry – Retailing Channels

As is typical in many countries, furniture retailing industry is not concentrated, although at the retail end, large players such as Wal-Mart account for increasingly large amount of sales. With 400 Wal-Mart stores and 250 other stores that it owns, that company posted annual sales in Mexico of $11 billion (DSN Retailing Today, 2005). Though at present Wal-Mart sells primarily particle-board furniture, it could broaden its offerings in the future.

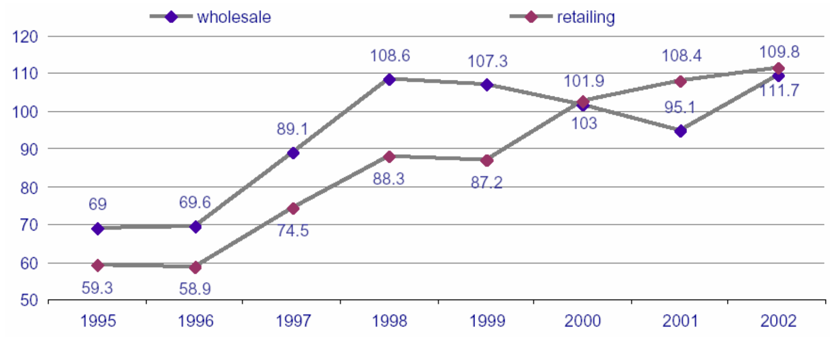
Using figures provided by CSIL Milano, it is possible to estimate market shares of other sellers of furniture. For example, two major department stores are El Puerto de Liverpool, and El Palacio de Hierro. While these stores likely receive a higher percentage of their sales from furniture, overall their market shares are lower. If 5%-10% of these company's sales are from furniture, their shares would be roughly 4 to 8% and 1 to 2%, respectively. Making similar assumptions about other retail players, it would appear, then, that the top ten retailers control from 10% to 20% of the Mexican market for furniture. Remaining sales are scattered among a large number of sellers, among which are dedicated furniture retailers.

These figures may understate concentration somewhat, for several reasons. Furniture tends to be a localized industry, so that in smaller population centers there may be less competition. Perhaps more importantly, furniture of varying quality does not compete directly. Overall, however, it is likely fair to say that the market for furniture in Mexico is competitive. Thus, wholesalers and retailers should not be able to pass through price increases, and the least expensive segment of sales is very competitive. This tendency is also driven by the arrival and penetration of low-priced Chinese imports to Mexico.

Despite the competition in the industry, however, prices have been on the rise through 2003, after which we do not have data. According to the Organization for Economic Cooperation and Development (2005), in the period from 2000 through the third quarter of 2005, consumer prices in Mexico rose at an annualize rate of 5.2%, with the trend for the last 12 months at 3.5%. In the three years for which we have both overall CPI data and furniture price data for Mexico (2000 through 2003), the overall CPI rose at 4.9% annually, while furniture prices rose at 6.7%. Given some of the more recent reports, which suggest a more difficult environment for furniture sales, it is difficult to expect that the trend of prices outpacing general inflation continued. On the other hand, the rise in the numbers of middle class Mexicans may account for greater purchases of more expensive furniture.

Thus, conditions appear to be better for furniture retailers than furniture manufacturers in Mexico. The following chart provides some historical background that is consistent with this view.

Index of annual furniture sales, 1995-2002* (1994=100)



Implications for Furniture Made from Certified Wood

This analysis suggests a quandary for producers of certified wood. On the one hand, the fact of certification could be the type of differentiation that permits certified furniture an added distinction in this competitive marketplace. Section 2 of this report will explore possibilities for price premiums associated with such a distinction. At the least, though, for the same price, it would seem that certification can be a “tie breaker.”

On the other hand, it may be difficult for certified furniture to move into the higher categories of retailing because it is often (though not exclusively) made of pine. Pine, although it has its own beauty (those with doubts can visit the website of Forestal Alfa, www.forestalalfa.com.mx), cannot compete with harder and therefore more desirable species such as cherry and oak.

Another issue that will have to be faced in creating markets for certified wood is the centrality of Wal-Mart in retailing in Mexico. Its status as a seller of furniture may well rise. Further, the company is continuing to open stores at a rapid pace (roughly 40 stores per year). But even if Wal-Mart did move to sell more wood furniture, its laser-like focus on costs would make it an unappetizing option for certified furniture. Another reason that this channel would be a potential problem for certified manufacturers is that certification is very unlikely to command a price premium at Wal-Mart. Finally, Wal-Mart is known to demand highly disciplined delivery schedules and other service. One pilot project between IKEA and the Pueblo Nuevo ejido (peopleandplanet.net, 2004) was terminated after problems of this variety. For mills that are used to serving local markets or who are just beginning to manufacture furniture, this will be a “tough sell.”

In the second section of this report on Certified Furniture and Mexico, we will explore further market entry and market enhancing possibilities for certified wood and other products. In this second section, we will report the results of a study that will help us to understand how Mexican consumers view certified wood.

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