

THE REPORT

San Luis Potosí 2017

OVERVIEW
EDUCATION
AGRICULTURE

INDUSTRY
REAL ESTATE
TOURISM

ECONOMY
AUTOMOTIVE
INTERVIEWS

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SAN LUIS POTOSÍ IS READY
QUALITY OF LIFE

In San Luis Potosí you can live well and live comfortably. The state's wide offering of work and leisure activities means it is the perfect place to live, work and play

■ **HIGH QUALITY OF LIFE**

San Luis Potosí is among the best states to live in with all the necessary **health** and **education** provision thanks to the ever-growing infrastructure that provides a high quality high coverage of services to the population.

From the urban areas to the suburbs there are different types of **housing** to suit every need and provide all residents with comfortable and high quality homes.

■ **CULTURE AND ENTERTAINMENT**

Mexico's **history** can be felt all over San Luis Potosí, its streets tell us stories of the most important moments of Mexico's past, moments that liberated and united their inhabitants. San Luis Potosí has a varied and vibrant **culture**, a state of festivals where we celebrate the stone that built our facades, the chocolate, enchiladas, wine and the rebozo, elements that are part of the life not only of the inhabitants of San Luis Potosí but all Mexicans.

■ **TOURISM**

San Luis Potosí is open to the eyes of the world. The state has strong infrastructure for the tourist industry and is an area that captivates and inspires visitors to return.

Magical towns, museums, open spaces, parks, hotels and recreational areas are just some of the attractions San Luis Potosí has to offer.



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Regional powerhouse

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San Luis Potosí's GDP was an estimated \$17.13bn in 2016, averaging around 4.4% annual growth in 2010-16. The workforce has also expanded, with the economically active population standing at 1.19m in 2016, or 42.7% of the total. In 2015 the state's economy expanded by 5.4% compared to 2.6% growth at the national level. The automotive segment forms nearly a quarter of the state's manufacturing industry, compared to just 18% of Mexico's manufacturing sector. Although its economic activities are mainly focused on the automotive industry, other segments such as chemicals, food, tobacco and textiles play a key supporting role.



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A key area of potential

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Some 2.75m ha of San Luis Potosí's 6.1m-ha surface area are potential agricultural areas, with around 1.85m ha currently under cultivation. Nearly 225,000 people in the state work in agricultural activities. In the 12 months to September 2016 agricultural production volumes fell, but the value of agricultural output increased by 36% to \$882.4m.





The state is widely known for its biodiversity and rich cultural history

Unique, global, connected

A vibrant and dynamic region looks to the future

For geographic and strategic reasons, San Luis Potosí and the rest of the country's central region had an important part to play in the nation's fight for independence from Spain.

PRE-COLONIAL HISTORY: San Luis Potosí has a rich colonial history dating back long before the arrival of the first Spanish colonial expeditions in 1518. The land marked a crossroads between different cultural regions – Aridoamerica and Mesoamerica – and was home to a number of tribes, such as the Otomi and Chichimeca, for millennia. Like many of the ethnic groups in the region, their religion and culture was characterised by the worship of the sun and the moon, with the noticeable development of culture and society appearing during the first millennium CE; the construction of large settlements and temples were common at this time.

It is claimed the name San Luis Potosí derives from France's king Louis IX, who also happens to be the city's patron saint. The suffix Potosí was added to signify the area's great mineral riches with hopes that it could match the famous mines of Potosí in Bolivia. With the discovery of the mines by Spanish settlers in 1592, they became the focal point of area's economy during the colonial period, alongside the gradual growth of agriculture in the form of cattle ranches and expansive *haciendas* that are still scattered throughout the countryside today. The region's economic importance was further cemented in the 16th century by the construction of the *Camino Real de Tierra Adentro* – the royal road of the interior land – which connected the city with Zacatecas and what is now New Mexico to the north, and Querétaro and Mexico City to the south. Today, this 500-year-old road remains an important trading route and is popularly known as the NAFTA (North American Free Trade Agreement) Corridor.

FROM INDEPENDENCE TO REVOLUTION: For geographic and strategic reasons, San Luis Potosí and the rest of the country's central region had an important part to play in the nation's fight against the Spaniards, which culminated in the declaration of war on September 16, 1810 – now Mexico's Independence

Day. The war lasted for slightly less than 11 years, with the country declaring independence in 1821 as a republic with a federal constitution based on the US model established four decades earlier.

Yet, 40 years later, San Luis Potosí, like the rest of Mexico, experienced some years of political instability, marked by the invasion of the French in 1862 and the establishment by President Benito Juárez of the state's fourth-largest city, Matehuala, as its capital in 1863-64. This was followed by the short-lived monarchy of Maximilian I in 1864-67, with San Luis Potosí serving as a key royal stronghold until late in 1866, the same year the city connected its first telegraph line to Mexico City. This politically volatile era was followed by the country's first prolonged period of peace; dubbed the *porfiriato* after the liberal army general Porfirio Díaz, who ruled during the period. Although often criticised as a dictator, many also see him as the very first truly globalised Mexican leader who understood the importance of building infrastructure and attracting foreign direct investment (FDI) as ways to boost economic growth.

Díaz's rule came to an end in 1910 with a nationwide outburst of violence resulting in a period of rule by a series of popular leaders such as Pancho Villa, Emiliano Zapata and army general Álvaro Obregón, which eventually culminated in a new social order derived from a new constitution signed in 1917.

THE 20TH CENTURY: For the remainder of the 20th century, Mexico was essentially a one party state with the Institutional Revolutionary Party (Partido Revolucionario Institucional, PRI) ruled the country for over seven decades. This period includes what is referred to as Mexico's *milagro económico* (economic miracle), which saw over 40 years of sustained economic growth and the development of the country's oil industry, accompanied by investment in education, health and transport, as well as energy infrastructure. The fall in oil prices in the 1980s combined

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with rising inflation led to a regional debt crisis and Mexico unwilling to meet its international payment agreements. Under these circumstances the country became more open to reform, thanks in part to president Carlos Salinas de Gortari (1988-94), who in 1993 signed Mexico up to the treaty that would irreversibly change its economic course. NAFTA came into force on January 1, 1994. Since then, states like San Luis Potosí have, in just two decades, been part of what has become a transition from one of the world's most closed economies to one of its most open, with 12 free trade agreements providing tariff-free access to 46 countries.

CULTURE & HERITAGE: Compared to a national average of 83%, some 89% of the inhabitants of San Luis Potosí identify as Catholic, and the state hosts a variety of festivals involving feasts, songs and processions that occur throughout the year. Some examples include the gastronomically rich Feast of San Miguel Arcángel held on September 29 and the Purísima Concepción running from December 1 to 8, a pyrotechnic extravaganza accompanied by dances and scores of musical instruments. Away from religious festivals, the state hosts a variety of events related to arts and culture, with the International Exhibition of Folklore and Traditional Arts and the International Festival of Contemporary Dance being just two of the most popular examples.

Potosinos, as they are widely known, are particularly proud of their food, characterised by its hearty dishes such as *enchiladas potosinas* (stuffed corn tortillas) and *colonche*, an alcoholic drink made from the red fruit that grow on the nopal cactus, especially popular in the north of the state.

GEOGRAPHY & CLIMATE: With its 58 municipalities – representing 3.12% of Mexico's territory – situated on the Tropic of Cancer, the surface area of the state of San Luis Potosí is 61,137 sq km, and it is blessed with a wide array of biodiversity from the famous *Huasteca*, a veritable rainforest, to dry, arid flatlands in the north of the state, just a few hundred kilometres from the US border. Nearly 73.5% of its territory is classified as arid or semi-arid, with the exception of the coastal region, which has a humid to semi-humid climate. Overall, the climate of the region has an average temperature of 21° C and an average annual rainfall of 950 mm. This climatic variance leads to impressive biodiversity in flora and fauna. The state boasts large stretches of ferns, moss, rosewood, banana and papaya, as well as large populations of deer, foxes and wild boars.

POPULATION: According to the National Institute of Statistics and Geography, in 2015 San Luis Potosí had a population of 2.7m, where 48.5% of the population is female and 51.5% is male, and 64% of inhabitants live in urban areas, a figure slightly below the national average. One significant economic advantage of the state is its relatively young population: 54% of people are under the age of 30, with a life expectancy of 77.5 years for women and 72 years for men. Approximately 89% of the population can trace its roots



Major transport links connect San Luis Potosí to the US border, which lies a few hundred km to the north

back to various European countries, the majority from Spain, many of whom settled in Mexico during the Spanish Civil War in the 1930s. A noteworthy demographic characteristic more typical of Mexico's southern states, San Luis Potosí has a sizeable indigenous population, which comprises 10.7% of the population, with Náhuatl, Huasteco, Pame and Otomi being the principal groups that live in the state's rural areas. This means that approximately 10% of the state's population are able to speak an indigenous language other than Spanish. In terms of cultural integration, efforts are being made by the state administration to implement integration programmes in the form of indigenous universities. Due to its relative isolation and proximity to the US, it is one of the states with the most significant migration rates north of the border.

POLITICS: San Luis Potosí is one of Mexico's 32 federal entities, which consist of 31 states and Mexico City. The current state administration is led by Juan Manuel Carreras, who took office in September 2015 for a six-year term on an anti-corruption mandate promising a transparent, responsive administration, enacting measures to avoid conflicts of interest. In his opening address Carreras emphasised the importance of investing in both economic and social policy as a way of reducing poverty and fostering inclusive development in the state, regardless of status or geographic location. At the helm of the state's economy is Gustavo Puente Orozco, secretary of economic development, a key player in attracting the state's impressive FDI flows increasingly stem from the Asia-Pacific region. The state sends three representatives to the country's 128-seat senate and 10 to the 500-seat *Cámara de Diputados* (Chamber of Deputies), Mexico's lower chamber.

URBAN CENTRES: San Luis Potosí's capital of the same name is by far the state's largest urban centre with a population of 824,229 people, exhibiting an

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Renewable energy sources such as solar and wind are increasingly being added to the generation mix

average annual growth of 1.33% over the decade. Unsurprisingly, it is both the main engine of growth and the key recipient of infrastructure spending in utilities, transport, health and education. According to Puente, the eight municipalities of the Centro metropolitan region account for 84.1% of the state's GDP and the vast majority of its infrastructure. It has the state's only international airport, its sole state university, the majority of its health care services and its only rapid transit system in the pipeline – a rapid bus system, known as the metrobus.

In spite of the developmental imbalance evident throughout the state's history, often seen as its main development challenge, other urban areas are also attracting key investments. Soledad de Graciano Sánchez is the state's second-largest urban area, is essentially a suburb of the capital just 8 km away from its centre. Unsurprisingly, the city's development is set on a similar path as the capital, fostering its growth mainly through manufacturing and industrial parks. Ciudad Valles, the third-largest city with 177,022 inhabitants, lies on the eastern flanks of the state, with horticulture and cattle ranching being the principal sources of income alongside the production of sugar cane.

The city's income is growing from ecotourism, as it is considered the capital of the famous Huasteca region, an area known for its impressive biodiversity and waterfalls. The state's fourth-largest city, Matehuala, is now booming, expanding in specific areas such as textiles, food, mechanics and electronics, as well as traditional agriculture.

HOUSING: According to Puente, it is a developmental priority to construct more housing close to the industrial zones to cater to rapid urbanisation in the capital's suburbs. Plans are being drawn up for a *Ciudad Satélite* (Satellite City), the Colinas Industrial Park some 16 km outside the city. Other projects such as *Ciudad Madera* (Wood City) and Villa de Reyes aim

to house workers from the plants of multinationals such as General Motors, BMW and Goodyear. The combined effort of these plans aims to reduce the current housing deficit, which sits at around 11,000 homes. In March 2017, in celebration of World Water Day, the mayor of San Luis Potosí announced that all homes in the capital city now have access to clean drinking water, a remarkable achievement given the lack of access in the rest of the country and the years of underinvestment in state utilities.

SECURITY: Often a key factor for foreign investors when choosing a location in Mexico, the issue of safety and security is of comparatively minimal concern in San Luis Potosí, especially considering that many states to the north and south struggle with their own security situations. In spite of this, Carreras announced in 2016 that more would be spent on protecting citizens and businesses with greater coordination among municipal, state and federal levels of government.

ENVIRONMENT: Due to its high levels of biodiversity, the state has three key areas protected by law by the state government: Sierra de Álvarez, Sierra la Mojonera and Sierra del Abra Tanchipa. However, given its mining history, the region still attracts significant interest from companies looking to extract its rich natural resources in zinc, copper, lead, gold, silver, mercury, fluorite, zeolite and arsenic. In some instances this had led to conflicts, with one particular incident involving First Majestic Silver and its use of cyanide and open-pit mining in and around the UNESCO World Heritage sites in the state. Many of these areas are sacred to indigenous groups such as the Huichol peoples. Wirikuta Mountain was acquired by First Majestic in 2010. In the end, a compromise was reached, but the case highlights the potential for clashes between a rapidly developing state and its pre-Hispanic cultural heritage.

However, the new administration emphasises its social obligation to live within its means, with the construction of solar farms being made a priority over recent years to give a viable green alternative to supply the state's growing energy demands.

ECONOMIC BREAKDOWN: While San Luis Potosí's first economic activity was based largely around mining, which began in the late 16th century, today its economic activities are heavily focused on the automotive industry, with other manufacturing segments such as the chemical industry, food and beverages, tobacco and textiles all playing an important supporting role. The tertiary sector comes first, contributing 51.9% to state real GDP, which involve 54.2% of the state's economically active population. The primary sector's contribution to real GDP is just 3.7%, although 19% of the workforce is reliant on the sector for their income.

STRUCTURAL REFORMS: Arguably the most defining transition of the Mexican and state economies has taken place during the current administration of President Enrique Peña Nieto (2012-18). Alongside other mainstream political parties, several key

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structural reforms were implemented involving the radical transformation of sectors such as telecommunications, education and, arguably most important, energy. The latter is of particular relevance to San Luis Potosí, whose favourable geographic location at the centre of the country lends itself to serve as a convenient distribution hub for surrounding states. There are calls to extend Mexico's fuel reserves from a mere 48 hours to a matter of weeks – the US, by comparison, has three months of reserves in the form of the Strategic Petroleum Reserve. Mexico lacks a similar system, and some propose that San Luis Potosí could be the ideal location for comparable reserves in the country. This provides real opportunities for private sector operators wishing to enter into storage of fuel, something that could become a highly lucrative sector in the years to come.

WORKFORCE: A key structural issue for Mexico is the formalisation of the economy. As a state, San Luis Potosí performs better on financial inclusion measures than the national average, with a quickly expanding and economically active population. Recent figures from the Mexican Social Security Institute show that in the first two months of 2017, 10,621 jobs were created, the fastest monthly expansion since November 2004.

Looking at the wider picture, such growth can also be seen as a two-sided coin: the very fact that a record number of jobs has been created is likely thanks to the confidence of foreign investors in the quality of the state's labour force, and is highly correlated with the \$688.9m in FDI flowing to the state over the last six months to March 2017. This point illustrates a key objective of the current administration: investing in education and social programmes to bring more workers into the formal sphere, and in turn create more services for the growing and economically active population.

The guiding idea is that these services will lead to a more productive workforce with higher levels of well-being over the long term. According to Puente, there are also efforts to include more women in the workforce, with many involved in setting up small and medium-sized enterprises. The local government is encouraging such activities, with a fund of MXN 700m (\$42.2m) being made available, and some 20,000 currently seeking aid (see analysis).

EDUCATION: The average duration of schooling in San Luis Potosí is 7.7 years, which is below the national average of 8.1 years. The state has a literacy rate of 93.5%, and 6.5% – many of whom are from older generations – have no formal education.

There are a number of higher education institutions in the state, many of them technical institutes such as the Instituto Tecnológico de San Luis Potosí and the Universidad Politécnica de San Luis Potosí. With 35,000 students, the state's Autonomous University of San Luis Potosí (Universidad Autónoma de San Luis Potosí, UASLP) is the most established of the state's higher educational institutions, with a wide offering of advanced programmes.



The state is emerging as a leading centre for high-tech research and development activities

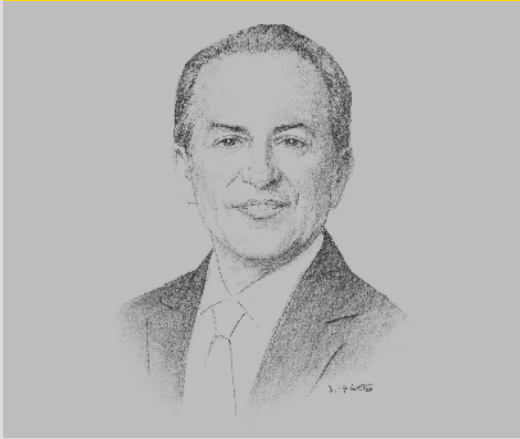
RESEARCH & DEVELOPMENT: Even before the election of US President Donald Trump, commentators speculated on the next steps Mexico should be taking to move up global value chains. In the 1990s Mexico was known as the *maquiladora* of the US, so named for the factories operating close to the border. Yet it is now a world-renowned producer of high-tech products, from aircraft parts to vehicles. In order to develop further and diversify its offering, the country needs to mature its manufacturing processes and, crucially, put more money into developing innovating practices and products that allow the country to climb even higher through global value chains. The state government understands this overall situation and is on a path to increase its research and development (R&D) efforts, forging more solid links between industry and academia, in an effort to make it a more attractive investment destination, not only for manufacturing processes, but more advanced R&D practices.

This work is being undertaken mainly by the UASLP, which is conducting research into material fibres, nano-materials, mining, engineering, health and biomedicine, greenhouse agriculture, chemicals and renewable energy generation (see analysis). It is estimated that the UASLP is responsible for 67% of all research in the state and contributes to the national R&D ecosystem by providing 477 researchers to the National Researchers System.

DOING BUSINESS: In 2016 the World Bank ranked the city of San Luis Potosí as the eighth-best city to do business throughout the whole of Mexico; the year before it was voted by KPMG as the fourth-best city for investment in the country. These reports not just cited the individual attractiveness of San Luis, but also emphasised its geographical context in the midst a four-state ecosystem – known as the *Bajío* region – with complementary manufacturing, commercial, business travel and residential possibilities.

A key structural issue for Mexico is the formalisation of the economy. As a state, San Luis Potosí performs better on financial inclusion measures than the national average, with a quickly expanding and economically active population.

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Juan Manuel Carreras

Local growth

Juan Manuel Carreras, Governor of San Luis Potosí, on the economic and academic advantages of the state

What are the main economic strengths of San Luis Potosí, and what are the economic and social priorities of the state over the long term?

CARRERAS: Although our economy originally started as a mining state, in the 21st century we transformed ourselves into a highly sophisticated manufacturer of steel, chemical products, foodstuffs, home appliances and vehicles. The growth of these key industries not only has positive economic implications, but has the ability to lift people out of poverty and share in the prosperity. While investment, employment and income are objectives of the government, strengthening the educational sector should continue to be a priority.

More professionalisation ultimately leads to a formalisation of the economy, which has a direct effect on the development of a whole range of other sectors. With more formal employees comes more necessity to develop and invest in social security services, which are essential to maintaining and improving the health and well-being of the country. Finally, it is important that we always consider the environment while enjoying economic and social development, and make a concerted effort to live within our means for the benefit of all.

How are links between universities and industry being improved to match the state's growth and ensure a necessary supply of human capital?

CARRERAS: The government plans to establish a new, bilingual technological university to expand and strengthen links between industry and academia, specifically focused on manufacturing. The use of dual education in universities is an essential tool in widening students' perspectives by linking up with companies and learning technical practices first hand.

It is also important for the indigenous population, who need to be given the opportunity to study in higher education establishments and feel a benefit from the growth of the state. As such, programmes at the Universidad Intercultural de San Luis Potosí act as crucial

tools in combating and reducing social exclusion, as well as providing an equal educational opportunity for the state's substantial rural population.

How is the location of the state being leveraged to provide better economic and social development for businesses and individuals?

CARRERAS: At the city level, the capital and other large urban centres are experiencing high growth, with real estate, construction and service development all springing up on the fringes of cities. Business tourism is also benefitting from the vast expansion of facilities being offered in these areas. In the case of the capital, the strategic importance of the city centre is being complemented by growing suburbs, and the government is incorporating seven municipalities to form a larger, more integrated urban zone with more government-backed services as a result. This more effectively structured centralisation means authorities are better able to provide essential social programmes, such as childcare centres, which in turn increases the economic contribution of women to the state. In return for economic growth, there has to be tangible social and economic benefits for the people. For the first time in many years, industrial development is occurring outside the capital. The state's fourth largest city, Matehuala, is booming and attracting significant investment infrastructure. This is finally starting to address the state's historical spatial development imbalance.

At the national level, our strategic geographical location in the centre of the country is crucial for links with neighbouring states that are also experiencing high growth levels. Additionally, Saltillo in Coahuila and Monterrey in Nuevo León – and other cities in Tamaulipas – are crucial trading partners in the well-developed north-east region. We are also part of the booming Bajío region in the centre of the country, which is one of the most important platforms for developing Mexico's manufacturing capability in global value chains.



The region's population has risen from 2.41m in 2005 to 2.72m in 2015

Regional powerhouse

Industrial growth is set to continue in the region

San Luis Potosí initially found wealth as a mining town after gold and silver were discovered in the area in 1592. Indeed, its name derives partly from Potosí, the Bolivian town that had the reputation as the richest city in the world thanks to its silver deposits. The state's mining boom never quite took off like its namesake's, but the central Mexican state has always had characteristics that make it a natural centre for industry. Just 415 km from the capital Mexico City, 505 km from Monterrey and 370 km from Guadalajara, it is as central as it can be relative to the economic centres of the country.

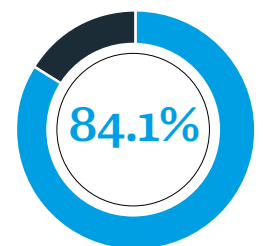
For more than a century this strategic location allowed the city to be a rail hub; and although passenger trains are now confined to the railway museum in the capital's historic centre, the current railway network makes San Luis Potosí a highly connected region in Mexico for cargo. Kansas City Southern's Mexican subsidiary operates routes directly from the industrial zone to the eastern US, as well as the eastern and Pacific coasts of Mexico. Today, San Luis Potosí is known as a crucial part of the Bajío region alongside Querétaro, Guanajuato and Aguascalientes. The area has become a powerhouse for Mexico's manufacturing industry, and in particular a centre for automobile manufacturing.

ECONOMY: The emergence of the Bajío industrial corridor has allowed GDP in the states that comprise it to grow well above the national average in recent years. State GDP has been at least one percentage point, in most cases more than two, above national GDP for every year since the 2009 recession with the exception of 2013 and 2014. San Luis Potosí's GDP increased from MXN211.3bn (\$12.7bn) in 2009 to an estimated MXN284.5bn (\$17.1bn) in 2016 on a constant price basis, averaging around 4.4% annual growth in 2010-16. Mexico's national GDP growth, meanwhile, averaged 3.1%. Recently, the gap between national and regional growth has become wider, with the state's GDP growing at double the rate of Mexico's. In 2015 the state's economy expanded by 5.4% compared to 2.6%

growth at the national level, putting it in fifth place out of 32 states in terms of GDP growth. Fellow Bajío states Querétaro and Guanajuato were the first and third fastest growing in Mexico that year, respectively. Official state figures for 2016 are still not available, but San Luis Potosí is again expected to more than double the nation's rate of growth, with 2.3% forecast for Mexico and 4.6% for the state. This has seen San Luis Potosí increase its share of national GDP from 1.77% in 2003 to 1.98% in 2015, according to the most recent official data available from National Institute of Statistics and Geography. The workforce, too, has expanded with the economically active population in San Luis Potosí rising from 1.04m in 2011 to 1.19m in 2016, or 42.7% of the total population, according to estimates from the Secretariat of Economic Development (Secretaría de Desarrollo Económico, SEDECO). Economic activity remains firmly centred in the Centro region, where the capital city and most industrial areas are located. The Centro region accounts for 84.1% of state GDP despite being home to just over half the population, which has grown from 2.41m in 2005 to 2.72m as of the last census in 2015. Migration from other states to the industrial zone is partly responsible for the increase.

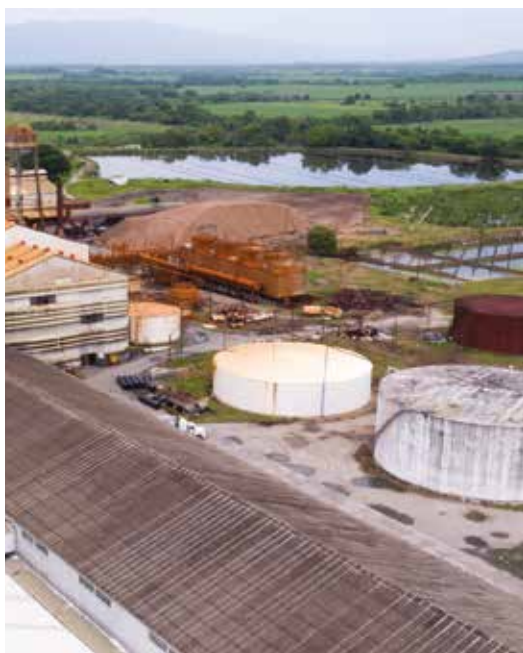
INVESTMENT: The nature of how foreign direct investment (FDI) is made, and how levels are measured, means states rarely see linear annual growth; indeed, in 2016 San Luis Potosí received just \$838.4m of FDI – around 47.3% of the amount registered in 2015. But the industrial boom has brought far larger inflows in recent years. With \$1.77bn of FDI inflows, 2013 was a record year for the state, and though the number dropped to \$980.1m in 2014, in 2015 San Luis Potosí attracted \$1.62bn of investment – putting it sixth in the country despite being the 18th largest economy out of 32 states. Additionally, exports have witnessed consistent growth, having more than tripled in US dollar terms since 2009. Volumes have grown every year since then to hit \$10.47bn in 2016, according to SEDECO estimates.

The Centro region accounts for



of state GDP despite being home to just over half the population

San Luis Potosí's GDP increased from \$12.7bn in 2009 to an estimated \$17.1bn in 2016 on a constant price basis, averaging around 4.4% annual growth in 2010-16.



There are 20 industrial parks located in San Luis Potosí

In November 2016 San Luis Potosí's airport began work on a \$24.1m expansion to double capacity from 450,000 passengers per year to more than 1m by the fourth quarter of 2018.

Approximately \$11.44bn of that is estimated to have come from the manufacturing sector.

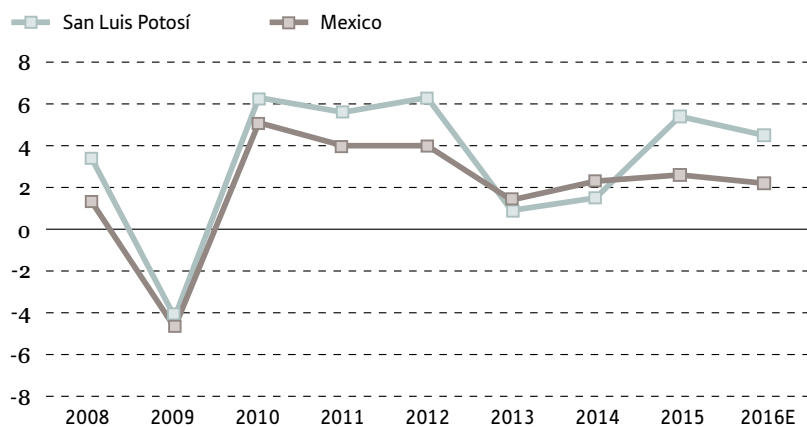
AUTOMOTIVE BOOM: Indeed, some 78.8% of Mexico's GDP is generated within a 500-km radius of the state capital, giving companies based in the area access to 73m potential customers. The arrival of General Motors, which opened a plant in San Luis Potosí in 2006, led to a significant expansion in automotive manufacturing; the number of companies involved in the industry increased from 93 in 2008 to around 218 in 2016 (see analysis). In 2016 BMW began construction of a \$1bn manufacturing plant in the Logistik industrial park in Villa de Reyes, where the company will begin manufacturing its 3 Series in 2019. Around 35% of the 2500 automotive providers in Mexico are based within 300 km of San Luis Potosí's capital, according to Gustavo Puente, secretary of economic development in San Luis Potosí. This has helped the automotive segment form around a quarter of the state's manufacturing industry, compared to just 18% of Mexico's overall manufacturing sector.

DIVERSIFIED INDUSTRY: Yet the state's economy is not all about cars. As in the past, mining continues to be a key industry, although in October 2016 the sector accounted for just 1.2% of the jobs in the state affiliated with the social security system – a way of measuring formal employment. San Luis Potosí is home to the largest fluorite reserves in the world with significant deposits of bentonite and cadmium. In total the sector received \$102m in FDI in 2016. More traditional industries include food, where Mexico-headquartered multinational Grupo Bimbo celebrated the 25-year anniversary of its San Luis Potosí plant, which employed more than 1200 people in 2016. Mexican-owned Mabe, which produces home appliances from its plant in San Luis Potosí, will celebrate 30 years in the city in 2017. Bimbo is one of the largest players in an electrical appliances and accessories industry that employs more than 10,000 people in the state – the third most of any manufacturing sector behind food and transport.

INFRASTRUCTURE GROWTH: San Luis Potosí has a comprehensive state-funded infrastructure network. With the future of the North American Free Trade Agreement (NAFTA) unclear, San Luis Potosí is still in a position to retain the advantages of being on what is known today as the NAFTA corridor. The Carretera 57 highway, which runs from Piedras Negras on the US border to Mexico City, passes through several of the state's 20 industrial parks that were placed strategically along the main road. Anticipating further increases in traffic along industrial roads, the state government has begun work on the road to Querétaro. President Enrique Peña Nieto's visit to the state in late February underlined the route's strategic importance to the country, and as he instructed the nation's minister of communications and transport, Gerardo Ruiz Esparza, to seek ways of reducing congestion. In November 2016 the state's airport operator began work on a MXN400m (\$24.1m) expansion to double capacity from 450,000 passengers per year to more than 1m. The project is set to be completed by end-2018. "Over the last five years Luis Potosí's airport has experienced an average annual growth rate of 16%. The new added capacity will allow it to increase capacity to 1.2m passengers a year," Marco Antonio Camarena, regional administrator of San Luis Potosí's airport, told OBG. In addition, the state's industrial parks offer added facilities for companies locating in the area. Most notable are the World Trade Centre industrial park, which acts as its own Customs office; and Mexico's first free trade zone, from which Kansas City Southern railway operates an intermodal transport hub. This puts San Luis Potosí firmly in the NAFTA corridor both by road and rail (see analysis).

SAFE BET: There are many factors that contribute to stability in the region. The state is relatively isolated from the organised crime that persists in certain areas of the country. Members of the business community and state government are encouraging investors to focus on San Luis Potosí's stable labour environment, as there has not been a strike in the state for 14 years. There is also consistency in the weather, with a dry to semi-dry climate and an average temperature of 21°C.

GDP growth of San Luis Potosí vs Mexico, 2008-16E (%)



Source: INEGI, SEDECO

Juan Manuel Carreras, governor of San Luis Potosí, has made attracting investment a priority by implementing business-friendly practices since late 2015 and appointing administrators with experience in the private sector, such as Gustavo Puente, who served as the president of the San Luis Potosí branch of the National Chamber of Industry (Cámara Nacional de la Industria de Transformación, CANACINTRA). According to SEDECO, the relationship between state authorities and local, national and international businesses is one that is conducive to prosperity. The World Bank's "Doing Business 2016" report put San Luis Potosí in eighth position overall out of Mexico's 32 states.

EDUCATION: The stable business environment is complemented by local government efforts to provide the education needed to make the state a continued place for investment. Close collaboration among the government, private sector and educational institutions is actively encouraged. There are more than 92 technical schools and universities, and major investors like BMW are collaborating with educators to provide apprenticeships via a dual education system (see analysis).

TOURISM: The recent sharp increase in business travellers has provided ample room for the hotel industry to expand in the state's capital city. With government efforts to capitalise on the increase in the number of non-business tourists, investments are being made in the region's infrastructure and diverse ecosystems. Additionally, due to San Luis Potosí's relatively unexplored natural areas, adventure and nature tourism are set to expand (see analysis).

AGRICULTURE: Carreras has made decentralising the economic activity of San Luis Potosí away from the capital one of the administration's priorities, and the huge potential in agriculture is attracting investment both from abroad and elsewhere in Mexico. Thanks to investment in protected agriculture, it is one of the top-three tomato producers in the country, and it is also a top producer of chilli, oranges and sugar cane.

Making the most of a dry climate, plentiful sunshine and energy infrastructure to expand the reach of greenhouses is one way the state may look to boost formal employment in rural areas. The state has invested MXN107m (\$6.45m) in the modernisation of irrigation technology in an effort to make agriculture more productive and profitable, and the current administration is aiming to modernise 15,000 ha of land in the short term. These efforts, among others, are aimed at formalising labour and improving the quality of life in the countryside. According to San Luis Potosí's Secretariat of Agricultural Development and Water Resources, 43.8% of the businesses or people operating in the sector are subsistence farmers, meaning their primary focus is on growing enough food to feed themselves and their families, leaving little or none for surplus trade.

A CHANGING MARKET: The auto industry experienced a minor setback in January 2017, with US auto manufacturer Ford cancelling its proposed \$1.6bn investment in a new plant in San Luis Potosí. This and the political rhetoric coming from the newly elected US administration have stakeholders in the US and

Mexico questioning the future of NAFTA and trade between the two countries. However, BMW, which is building a \$1bn plant set to begin operations in 2019, immediately reaffirmed its commitment to investment in the region, as did other industrial companies with operations in the state. "BMW makes its investments based on the long term, and there is no reason for us to change our plans for a project of this size," Carlos Gutiérrez, head of government relations and external affairs at BMW in Mexico, told OBG. "We are aware that there may be changes in the external environment, but we are building a production plant to serve the whole world," he added. Additional key investment projects have been signed since, signalling resilience and stability in the manufacturing industry. In January 2017 US-owned transport group Kansas City Southern teamed up with Watco Companies and World Trade Centre (WTC) Industrial to facilitate and expand the export of liquid fuels from the US to Mexico (see analysis). According to José Luis Contreras, COO of Grupo Valoran, parent company of WTC Industrial, "this joint venture is a sign of confidence and there is an optimism around now that wasn't here in January 2017".

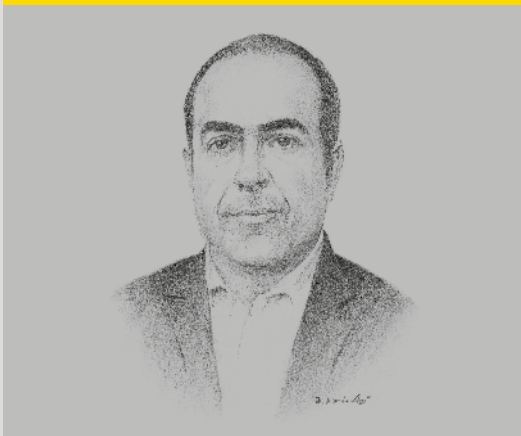
FREE PUBLICITY: Furthermore, in the wake of Ford's decision, San Luis Potosí experienced a period of relative world media attention. "In some ways, Ford's departure can be an opportunity for San Luis Potosí," Paulina del Valle, director-general of the Mexican Business Council for Trade, Investment and Technology in San Luis Potosí, told OBG. "We are becoming known throughout the world, and other companies can now come and take advantage of the strategic and logistical location of the state," she added.

Although any changes in Mexico's trade relationship with the US – and thus the impact on industry in San Luis Potosí – are far from defined, the notion of having to operate in a new environment is accelerating the process of diversifying to new markets. "For a long time in Mexico we have made the mistake of always looking north," Raúl Martínez Jiménez, president of San Luis Potosí branch of CANACINTRA, told OBG. "Now we may not be able to export to the US as much as before, but in San Luis Potosí we have everything we need to reach many other countries." Indeed, industries are building on existing relationships with Europe, Asia and other parts of Latin America. Although state exports, as in the rest of Mexico, go overwhelmingly to the US, San Luis Potosí has something of a head start when it comes to receiving investment from non-US sources. Since the 2000 free trade agreement with the EU, around 40% of Mexico's FDI has come from Europe; in San Luis Potosí that number is around 50%. Furthermore, the number of Japanese companies present in the state has risen from three in 2009 to 46 in the span of eight years.

OUTLOOK: While the uncertainty that has been ushered in with the new US administration may have lowered expectations in the short term, there are several encouraging signs that industrial growth is set to continue apace in the region, and central players in San Luis Potosí's private sector are therefore expecting the state to remain a top destination for investment.

The state has invested \$6.45m in the modernisation of irrigation technology in an effort to make agriculture more productive and profitable, and the current administration is aiming to modernise 15,000 ha of land in the short term.

Since the 2000 free trade agreement between Mexico and the EU, around 40% of Mexico's foreign direct investment has come from Europe; in San Luis Potosí that number is closer to 50%.



Gustavo Puente Orozco

Location, location, location

Gustavo Puente Orozco, Secretary of Economic Development, State of San Luis Potosí, on the expansion of the state's economy

What markets besides the US is San Luis Potosí looking at to maximise its trade potential?

PUENTE: For obvious structural and geographic reasons, the Mexican and US markets are intrinsically linked together. This is not necessarily a disadvantage, as the North American Free Trade Agreement still exists, and Mexico is still the largest trade partner of a number of states. Having said that, increased interaction with other key global markets in Europe and diversification towards Asia is essential to maintain the strong growth San Luis Potosí has experienced over recent years.

The EU ambassador to Mexico recently visited the state and underlined the importance of our relationship with the world's largest trading bloc. Nearly 40% of Mexico's foreign direct investment (FDI) comes from Europe, with this number reaching 51.6% in San Luis Potosí, whereas 41.7% of investment comes from the US. However, looking at growth areas since the turn of the new century, the results are clear: investment and trade from Asia, especially from China, Japan and South Korea, has grown significantly from almost nothing in 2000. Eight years ago there were three Japanese companies in the state, and now there are 55, and it is the same story all over the Bajío region.

In what ways can San Luis Potosí's central location be leveraged to bolster its economy?

PUENTE: Looking at the national picture, San Luis Potosí stands out as one of the top-seven growth regions in the country and consistently posts economic GDP growth well above the national average. In 2016 the state registered 4.6% GDP growth and received \$658.9m in foreign investment in the manufacturing sector in the last five months alone, creating 7980 new jobs. This figure can always be improved; in spite of clear challenges, the state is expecting to reach at least \$1bn in FDI inflows in 2017. Looking at the breakdown of industries, San Luis Potosí's key growth sector is the automotive industry, which represents around 25.7%

of the state's GDP. In Mexico there are 250 original equipment manufacturers, 30% of which are located within 300 km of each other. The proximity of the value chain is enticing to firms looking to move to the state. Taking advantage of its location, the state has become a logistics centre for a variety of industries. Rail operator Kansas City Southern's presence demonstrates this and is a big draw to industry, especially due to the presence of the World Trade Centre Industrial Park, which acts as an entry point for refined energy products arriving from the US by train. In other areas the state remains strong, especially in mining. San Luis Potosí is one of the most important producers of gold, silver, copper and zinc. In terms of manufacturing, we are a large producer of food products and domestic appliances, but most importantly all of the above-mentioned industries have a strong focus on research and development. This builds on work done by other institutions in neighbouring states such as Querétaro, which follows the vocational dual system of education pioneered in Germany.

How is infrastructure being prioritised to ensure it facilitates the state's growth?

PUENTE: The state government is implementing various new projects to bolster the infrastructure of the state over the long term. A \$4bn investment in the upgrade of the Querétaro-San Luis Potosí road using the new public-private partnership model approved by the federal government is just one example.

From an international angle, the expansion of the airport is crucial. In 2013 it had 261,699 arrivals and now has 504,313 annually, almost doubling over three years thanks to business and leisure travellers. In 2016 a new MXN400m (\$24.1m) investment was initiated that will take 20 months and bring the capacity up to 1.2m arrivals. Capacity is being added, and the development of new routes connecting Toluca with Santa Fé, Los Angeles and San Francisco is being studied; these routes will connect us to travellers coming from Asia.



A main highway passes through several of the state's industrial parks

The centre of industry

Major projects under way to keep the sector expanding

Of all the places vying to be industrial and logistical hubs, San Luis Potosí perhaps lays the best claim to being in the middle of everything. Geographically, it is more or less equidistant between Mexico's three most important economic cities: Mexico City, Monterrey and Guadalajara. "Its location is the main reason why national courier and cargo company Estafeta chose San Luis Potosí's airport as its headquarters," Raúl Martínez Jiménez, president of the San Luis Potosí branch of the National Chamber of Industry, told OBG. "We are right in the centre of Mexico, making us a logistical focus of the country." San Luis Potosí is located on the vertebral column of Mexico and is intersected by the Carretera 57 – the main highway that runs from US border town Piedras Negras to Mexico City. The highway passes through several of the state's 20 industrial parks, providing easy access for both workers and drivers. The Kansas City Southern de México (KCSM) terminal at the World Trade Centre (WTC) industrial park provide further connections to the US market.

ENERGISING GROWTH: KCSM's presence in the state has allowed San Luis Potosí to take centre stage in Mexico's energy distribution. Grupo Valoran, a well-known, regional business that built Mexico's first multi-storey cement manufacturing facility in the 1970s, has taken the lead role in making the most of the country's 2013 energy reform. The group, which owns WTC Industrial, officially announced in January 2017 that it had signed on to a joint venture with KCSM and the US transport group Watco Companies to facilitate and expand the export of liquid fuels from the US to Mexico.

The Central Mexican Terminal (Terminal del Centro de México, TCM) is forecast to be completed by the second quarter of 2017, and comprises a liquid fuels train terminal to be located inside the free trade zone (FTZ) in the WTC industrial park, just south of the state capital, requiring an initial investment of \$45m. A statement from the parties involved said the joint venture was a direct result of energy reform legislation aimed

at opening the country's energy markets to foreign and private investment. KCSM will utilise the FTZ in the WTC industrial park to supply the TCM with hydrocarbons from Texas, where it will link with 26 other refineries. According to Allan Roach, senior vice-president of network strategy for Watco, the proximity to KCSM's existing terminal will ensure quick cycle times of customer rail cars, while the location in Mexico's largest FTZ will provide an economic advantage to rail shippers.

NEW GENERATION: This is not the only way that investors are looking to meet anticipated increases in energy demand. Another of Grupo Valoran's subsidiaries, Ranman Energy, entered into a joint venture with Canadian firm ATCO to build a power plant in the WTC park planned to provide up to 20 MWh of electricity to tenants of the industrial park by December 2017. The project is designed to be highly scalable, with the possibility of additional capacity as new tenants take up operations in the park. Valoran plans to take further advantage of the new energy reforms to build Mexico's first isolated electric power plant, which means the electricity generated by the plant will not necessarily be transmitted via the national transmission network or general distribution networks. The plant will begin with a capacity of 65 MW, with the potential to grow to 400 MW, nearly half of the 900 MW of energy consumed by the entire state of San Luis Potosí.

"Not only will we be able to alleviate energy scarcity, which is what the energy reform was designed to do, but we will also be able to offer competitive rates – with the number set by the Federal Electricity Commission as the maximum," Michele Porriño, director at WTC Industrial, told OBG. "Energy is a limiting factor in production, so we are seeing an opportunity to resolve this problem," he added.

Electricity production is generating significant interest at neighbouring industrial parks as well. "There is important work to be done, as although it is said there is plenty of capacity, the issue lies with transmission

San Luis Potosí is more or less equidistant from Mexico's three most important economic cities: Mexico City, Monterrey and Guadalajara.

Mexico's first isolated electric power plant will be built in San Luis Potosí, beginning with a capacity of 65 MW and the potential to grow to 400 MW, nearly half of the 900-MW consumption of the state.



The government is working to upgrade the state's road system and transportation infrastructure

A leading auto manufacturing plant is being supplied with 100% carbon dioxide-free electricity, powered by on-site solar generators.

and the network of distribution lines," Bernardo López Ortega, general director of Logistik industrial park, told OBG. "Energy reform is going to be beneficial for everyone," he added. Founded in 2003, Logistik is the biggest industrial site in Mexico, and counts the state's two original equipment manufacturers (OEMs) – BMW and GM – and L'Oréal and Continental among its tenants. It has an internal power substation but is looking to bring on another energy provider to give clients choice.

RENEWING EFFORTS: San Luis Potosí's climate offers additional advantages to manufacturing and industrial groups that settle in the state. BMW, for instance, says its plant will be its most resource-efficient production location worldwide once operations begin in 2019. This is in part thanks to the plant being supplied with 100% carbon dioxide-free electricity, powered by on-site solar generators. Swedish-Swiss industrial technology company ASEA Brown Boveri (ABB) installed 4000 photovoltaic cells at its San Luis Potosí campus that produce 1200 KWh – or 60% of the plant's electricity needs. ABB, which itself develops solar energy technology, uses the panels as a live platform to display the potential of the company's clean energy products to clients.

FREEING TRADE: Long before recent energy plans, the FTZ in the WTC industrial park was already one of San Luis Potosí's most significant attractions. The zone was the first of its kind in Mexico and it remains the only one in the Bajío region. It allows clients to avoid physical inspection at the point of entry, preserve original seals from providers, enjoy faster crossings and defer taxes until products are released into the Mexican market – if at all.

Within the San Luis Potosí FTZ, a 100-ha intermodal terminal was established by KCSM in 2002. Moving around 450,000 containers per annum, the terminal links the state not just with the US at Laredo, Texas and other Mexican cities, but also with ports on either side of the country. Altamira on the Gulf of Mexico connects the country to ports on the East Coast of the US and

Europe, while Lázaro Cárdenas on the Pacific coast connects it with ports across Asia.

The terminal in San Luis Potosí is used by companies based in neighbouring states as well, receiving containers from Honda, for example, which has plants in Jalisco and Guanajuato. According to Gustavo Puente, secretary of economic development in San Luis Potosí, this crucial logistical role is played not just for companies operating within the state, but also for those elsewhere in Central Mexico. KCSM is therefore one of the state's most significant attractions, and a strategic ally.

INDUSTRIAL PERKS: The readily available infrastructure of San Luis Potosí's 20 industrial parks is undoubtedly a vital ingredient in attracting foreign companies. "The state government has a very good vision for the orderly development of the region and is making large investments in infrastructure. Industrial parks do not just ensure that giant companies such as BMW find the services they need; they also allow their suppliers to operate nearby," Carlos Gutiérrez, head of government relations and external affairs at BMW in Mexico, told OBG. "Water, electricity, rail and a number of other infrastructural aspects are crucial, because they mean that some of our suppliers have found conditions accommodating and will appreciate our efforts, and this all bodes well for the future," he added. Another contributing factor to why BMW chose the area is the suitability of the terrain for a construction project of such magnitude in nature. "In some areas of the park the land has a resistance of up to 100-120 tonnes per sq metre," López told OBG. "That means companies that build here can spend less on the foundations," he added. **TRANSPORT WORKS:** Undoubtedly the most urgent challenge that the business community sees for San Luis Potosí's development as an industrial hub is one of mobility. However, the government is responding to these concerns. "Key areas that still need attention are road infrastructure and the transport system, especially given the volume of traffic that the roads are going to be seeing in the near future," Gutiérrez told OBG.



Industrial parks are one of the state's most significant attractions

Free trade zones allow clients to avoid physical inspection at the point of entry, preserve original seals from providers, enjoy faster crossings and defer taxes until products are released into the Mexican market – if at all.

“However, the government is working on this and is taking the opportunity to upgrade the infrastructure. An investment of this scale obviously means that the collaboration of the government is very important, and we have found that they are very willing to listen,” he added. Indeed, as reported, work is being undertaken to widen the Carretera 57 to Querétaro with the encouragement of President Enrique Peña Nieto. However, additional pressing steps need to be taken to solve traffic problems. “Here we are talking about mobility policies, but what we first need to work on is immobility policy,” Ramiro Robledo, secretary of communications and transport of San Luis Potosí, told OBG. “We can take steps so that people do not have to make so many journeys – whether that’s as simple as encouraging online bill payments, or thinking about working remotely,” he added. By mid-2018 the city of San Luis Potosí should have a bus system close in calibre to the ones running on the industrial complexes. The first stage of the metrobus, a preferential lane system with capacity to carry 40,000 passengers per day, will be completed and go from near the city centre to Villa de Pozos at the start of the industrial zone. “Despite challenges in managing the transition of existing transport operators to a 21st-century regulatory regime, there is a willingness among most transporters to agree to the new rules,” Robledo told OBG. Another development in revamping the transport system is a bid to promote sustainable practices and reduce emissions. San Luis Potosí announced in August 2016 that the urban public transport systems would be switching over from petrol to natural gas, though the timeline for the changeover had yet to be announced at the time of publishing. A number of taxis and the metrobus system have already started using natural gas fuel, not only for environmental reasons, but also to save money; a litre of natural gas is around half the cost of traditional petrol.

SPREADING WINGS: In order to better deal with the growing numbers of business travellers and tourists to the area, a major transport expansion project has been started at the Ponciano Arriaga International Airport (PAIA) airport. The existing airport infrastructure, located some 16 km from the city centre and 48 km from the Logistik and WTC industrial parks, may soon become unable to provide for a region that has developed into a centre for industrial investment. Passenger numbers have almost doubled in just three years, rising from 262,000 in 2013 to 504,000 in 2016, falling short of the advertised capacity of 450,000 per year. Seeing the potential and necessity of expansion, the private sector airport operator Grupo Aeroportuario del Centro Norte (OMA) began work on a MXN400m (\$24.1m) investment in November 2016. OMA operates the San Luis Potosí airport alongside 12 others in Mexico. By the end of 2018, the PAIA will be more than three times its current size, with the terminal building growing from 4111 sq metres to 12,800 sq metres, and capacity will more than double to around 1.2m passengers per year.

Mexico City is the only other airport in the country undergoing such a transformation. “Our airport is the port of entry for most foreigners when they arrive in



Ponciano Arriaga International Airport's capacity will double by 2018

San Luis Potosí, so it is very important it reflects the city's growing importance,” Marco Antonio Camarena, regional administrator of the PAIA, told OBG. “For 2017 uncertainty surrounding US President Donald Trump's policy towards Mexico may push passenger growth slightly below the double-digit figures of recent years, but the investment comes with the expectation that business will continue to boom,” he added.

MORE CONNECTIONS: San Luis Potosí already has direct international flights to Dallas and Houston, and is looking to open new routes in the coming years. Airlines are evaluating the possibility of adding flights to Los Angeles to improve connections with Asia, as well as with Detroit given the continued dominance of the automotive sector in the Mexican state. Additionally, in recent years the airport has added tourist routes to other parts of Mexico in a bid to encourage tourism in the region. Since December 2013 Cancún has been approximately 2.5 hours away thanks to a direct route from airline company Volaris, while Querétaro-based TAR Aerolíneas began operating flights to Puerto Vallarta on the Pacific coast in October 2015.

TEAM GAME: By definition, being a hub implies being the centre of a joint effort, and although healthy competition exists between the states in the Bajío region, San Luis Potosí's industrial community is very much aware that what is good for neighbouring states is good for the state itself. Industrial hubs are not self-contained entities, and often companies work across parks in different cities. That KCSM works with other companies based in other industrial hubs is a good example, as are the auto parts companies that supply the OEMs based elsewhere in the Bajío region.

“We host providers of Mazda, Honda and Nissan, for example,” López told OBG. “Obviously, it would be beneficial for everyone to base themselves in San Luis Potosí, but the success of other states such as Querétaro, Aguascalientes, Guanajuato, and Jalisco also benefits San Luis Potosí. The future is still bright,” he added.

By mid-2018 the first stage of the metrobus, a preferential lane system with capacity to carry 40,000 passengers per day, will be completed.

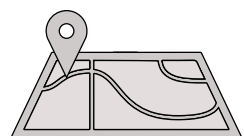
Due to increasing arrivals of business travellers and tourists, passenger numbers at the Ponciano Arriaga airport have almost doubled in just three years, rising from 262,000 in 2013 to 504,000 in 2016.



Several international firms are investing in the state's auto sector

Competitive advantage

The auto industry in San Luis Potosí is planning for long-term growth and all contingencies



35%

of Mexico's auto and auto parts producers are located within 300 km of the state's capital

San Luis Potosí's automotive industry could hardly have asked for a worse start to 2017, but the state's strengths have not changed, and optimism returned in a matter of weeks. Ford Motor's withdrawal from San Luis Potosí in January 2017 meant the cancellation of a \$1.6bn investment and the loss of up to 2800 jobs. However, it was several years from opening its doors when it pulled out, and both San Luis Potosí and the surrounding Bajío region already hold pivotal positions as providers of vehicles globally. In some ways, by withdrawing so early, Ford lessened the blow.

INVESTMENT FLOWS: Some 35% of the 2500 automotive suppliers in Mexico are based within 300 km of San Luis Potosí's capital, according Gustavo Puente, secretary of economic development in San Luis Potosí. "Even without Ford, San Luis Potosí remains a major provider for the automotive industry," Raúl Martínez Jiménez, president of the San Luis Potosí branch of the National Chamber of Industry, told OBG. "Our state is in a strong position and well placed to open up to the world." Some companies in the sector, such as Robert Bosch and Cummins, have been in San Luis Potosí since long before the North American Free Trade Agreement, with the former arriving in the mid-1970s and the latter in 1980. Robert Bosch continues to invest in its local operations, with the announcement in October 2016 of an \$80m plan to add 25,000 sq metres to its existing plant, bringing the total number of employees to 2700. The investment includes a new engineering centre focused on petrol systems.

There is also a new BMW plant, where construction is progressing well and generating high expectations for the company, according Carlos Gutiérrez, BMW México's head of government and external affairs. The German original equipment manufacturer (OEM) will produce the 3 Series there, assembling up to 150,000 units annually beginning in 2019. Puente told OBG that at least 10 more suppliers could arrive in San Luis Potosí over the next two years as a result of BMW's

investment. Meanwhile, tyre manufacturer Good-year remains firm with its \$550m investment in a new factory that will produce 6m tyres and create up to 1000 jobs. The plant is set to open by the end of 2017.

New investment also continues to be made. Most recently, Chinese company Ningbo Asiaway Machinery said in March 2017 that it would install a new plant in the state, according to Puente. Ningbo is a specialist producer of aluminium and zinc components for the automotive segment. In addition, in early January 2017, just as Ford was cancelling its investment in the state, Japanese plastic auto parts maker Nidec Sankyo announced plans for a \$15m factory there, and in February 2017 German auto interiors firm Benecke-Kaliko said it was going ahead with a MXN400m (\$24.1m) investment to expand its existing plant in the region.

CLUSTER EMERGENCE: Collaboration between the public and private sectors in developing the automotive industry in San Luis Potosí became concrete in 2015 with the establishment of the Automotive Cluster of San Luis Potosí. The cluster aims to create a public policy for the sector that outlasts political administrations. With the goal of "strengthening the orderly, harmonious and sustainable growth" of the sector, the cluster has formalised the link between the government, the private sector and educational institutions. Héctor Soto, director-general of the Automotive Cluster of San Luis Potosí, which already has 42 members, told OBG the aim is to build bridges between industry, the government and academia to find solutions to common problems and, in the medium term, undertake high-impact projects. There are already examples of tangible results. Soto told OBG that when General Motors identified the need for a training programme in lean manufacturing – a method used to eliminate waste – the cluster went into the company's installations, carried out a review and helped implement improvements. Where clusters can really come into their own is with longer-term

The Automotive Cluster of San Luis Potosí makes official existing ties between local and federal government, the private sector and educational institutions to enhance efficiency and human resources.

projects. Soto highlighted ongoing work with the Tangamanga University and Universidad Potosina to create a degree programme specific to automotive engineering. “Projects like this will not bear fruit for a few years, but rather are part of a longer-term strategy,” he told OBG. For the cluster itself, the next challenge is to incorporate Japanese firms.

JAPANESE COOPERATION: There is one area where San Luis Potosí’s cluster is taking a leading role. It is coordinating a project, set to launch in July 2017, through which the Japanese International Cooperation Agency will send experts to Mexico for five years. They will educate local providers and try to incorporate them into the supply chains of OEMs and tier-1 firms in the Bajío region. “We will be working with small and medium-sized enterprises from the top level, trying to change the mindset,” Soto told OBG. The first step of the project will be to identify suppliers, and then discover companies’ needs. Although the initial programme will focus on Japanese firms, it aims to create the skills and knowledge that should strengthen the local supply. “There are huge opportunities on a national level to increase the local content,” he added.

SUPPLY CHAIN OPPORTUNITIES: Another benefit of the cluster is its ability to tackle issues that are a problem for the Mexican industry more generally. According to Soto, as tier-1 providers tend to swarm around the famous brands, around 50-60% of the parts used by OEMs are produced locally. Yet, as you move down the scale, tier-1 manufacturers tend to use local suppliers for just 15-30% of their materials. Indeed, a December 2016 report prepared by the Automotive Cluster of San Luis Potosí showed that although seven tier-1 providers and 11 tier-2 players were already members, there are 26 potential tier-1 members, but just nine potential tier-2 associates and two tier-3 providers. Looking to tackle this problem, the cluster has formed a tier-2 subcommittee. “It is good practice and a great opportunity to encourage tier-1 companies to buy from local tier-2 and tier-3 providers, rather than import,” Soto told OBG.

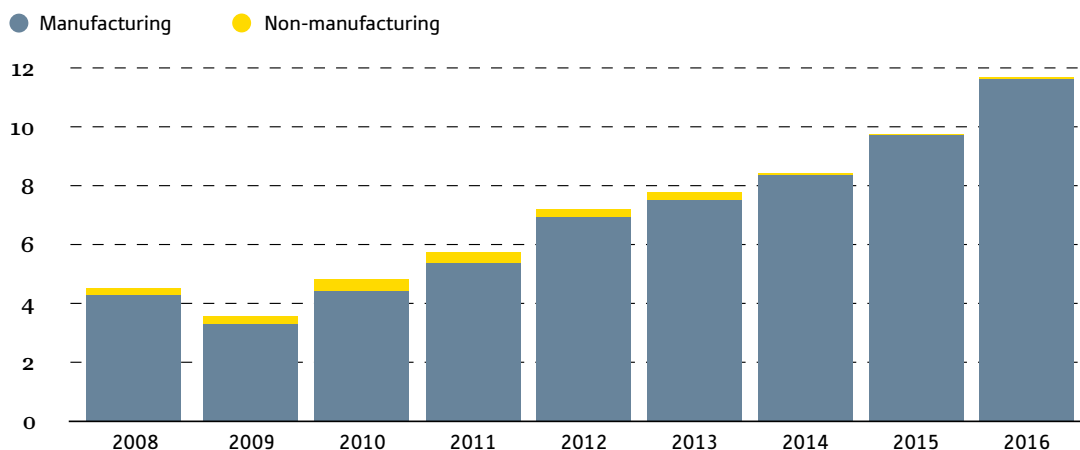


Mexico is looking to attract foreign knowledge and technology transfer through alliances and co-investment

National trade and investment promotion agency ProMéxico argues that tier-2 and 3 providers have a great opportunity in the country, and the group has been promoting links between these kinds of suppliers and OEMs and tier-1 providers through seminars and business meetings. Yet, this requires higher-quality processes, too. ProMéxico points to the example of Eastern Europe as a region that has been able to take the path to highly specialised manufacturing processes. “The strategy is focused on tier-2 and 3 providers dedicated to processing materials that, due to their specialisation and quality, add value to the national product,” according to ProMéxico’s 2016 automotive report, “The Mexican Automotive Industry: Current Situation, Challenges and Opportunities”. Therefore, ProMéxico is also looking to attract foreign companies to this segment of the supply chain, via alliances or co-investments, so they can transfer their knowledge and technology to Mexican companies.

50-60%
of the parts used by original equipment manufacturers are produced locally

Exports from San Luis Potosí, 2008-16 (\$ bn)



Source: INEGI



The state is looking to increase private sector contributions to education

Innovate to educate

Industry and academia team up to train next generation of workers

In the last quarter of 2016 San Luis Potosí recorded the lowest-ever unemployment level for the state and the fourth-lowest level in Mexico at 1.97%. As of January 2017 approximately 400,000 people were employed in the formal labour market.

The boom in automotive jobs has been an important factor in bringing unemployment down in San Luis Potosí. In the last quarter of 2016 the state recorded the lowest ever unemployment level for the state and the fourth-lowest level in Mexico at 1.97%. As of January 2017 approximately 400,000 people were employed in the formal labour market. According to the Secretariat of Economic Development (Secretaría de Desarrollo Económico, SEDECO), as of October 2016 some 37.3% of workers in San Luis Potosí incorporated into the social security system were employed in industry, while 15.2% were employed in commerce. The automotive industry is a major player in both of these areas. Dräxlmeier Group, the German automotive components supplier, for example, is the largest employer in the entire state, supporting more than 5000 workers.

What makes the state so attractive for manufacturing is its well-trained workforce. "If more US companies decide to leave, not only will they find a more expensive workforce, but they will also be missing out on qualified and well-trained Mexican workers," Raúl Martínez Jiménez, president of the San Luis Potosí branch of the National Chamber of Industry (Cámara Nacional de la Industria de Transformación, CANACINTRA), told OBG. "In San Luis Potosí the public and private sector have both invested a lot in education and training, and we are now seeing the fruits of our labour."

JOINT EFFORT: The collaboration and interaction among educational institutions, the state government and companies that have chosen to invest in the region has been crucial to San Luis Potosí's development.

While these companies praise the level of workers found in the state, they are also aware that they need to be proactive to ensure they get the best out of the local population. BMW, whose new plant is positioned to create 1500 new jobs, began training 25 local mechatronics engineers in 2015 by collaborating with the Technological University of San Luis Potosí (Universidad Tecnológica de San Luis Potosí, UTSLP). BMW has since

launched similar programmes with local technical colleges looking to train production mechanics and automotive mechatronics experts. Encouraging this kind of dual education is one of the current administration's objectives under its science and technology plan for the state, with Goodyear, Continental and Bosch among those with programmes in the state. "Training the local workforce is a joint endeavour with local educational institutions, and we are seeing great potential," Carlos Gutiérrez, head of government relations and external affairs at BMW in Mexico, told OBG. "Our collaboration with universities like UTSLP includes bringing experts from other plants around the world to share their knowledge, and encouraging workers from this plant go to train in other facilities. The idea is to be able to make the most of the technical experience we have," he added. BMW's Munich and Spartanburg plants are helping to set up the factory in Mexico. Japanese car-maker Toyota also picked San Luis Potosí as the base for its Centre of Technical Training in 2008, even though its new factory will be built in Guanajuato.

RESPONDING TO DEMAND: Educational institutions have shown themselves to be flexible and able to develop according to the demands of industries based in the region. The Centro Educativo, Grupo Cedva, effectively began as a mechanic school but has developed into what it describes as a professional working institution. The group now offers three-year technological baccalaureates, three technical degrees, and an automotive mechanical engineering degree at its San Luis Potosí branch. According to Annel Romero Velasco, director of engineering and baccalaureate programmes at Cedva, the centre is now incorporating an automotive engineering course at the *técnico superior universitario* level – an intermediary level between baccalaureate and a fully certified engineer. "Our courses often respond to what the market is demanding of us," she told OBG. Cedva's experience in the sector is such that the institution is collaborating with BMW in

As of October 2016 some 37.3% of workers in San Luis Potosí incorporated into the social security system were employed in industry, while 15.2% were employed in commerce.

designing a course. “Our new course is part of an agreement we have with BMW, and we are finding that this is at the level that equipment manufacturers are looking for at the moment,” she added. Local institutions and multinationals have become partners in ensuring each other’s expectations are delivered. “We have to be very efficient to ensure not just that companies find a workforce here that matches the profiles they need, but also that the local people are able to find the jobs they want thanks to these opportunities”, Manuel Lozano, secretary of labour for San Luis Potosí, told OBG.

INVESTING IN THE FUTURE: The dual education system also provides opportunities for the young population in the state. “They know they have an guaranteed job at the end of their studies, and when they start working they can in some cases double their family’s income,” Martínez told OBG. “Young people in San Luis Potosí now are not just looking to migrate north for opportunities, they understand that studying gives them more job options here,” he added. With international firms arriving, language skills are also becoming more important; the state has responded by opening a bilingual university. According to Romero Velasco, this flexibility also encompasses training women, who are traditionally under-represented in the industry, to work with automotive companies. Based on industry requests, Cedva offers 50% scholarships grants to female students. “Companies want to balance out their staff and are asking us to train more women,”

Romero Velasco told OBG. “While this could present a cultural challenge, international companies like BMW are specifically asking for this.”

FROM INDUSTRY TO R&D: More than just training for jobs, San Luis Potosí’s universities are in a position to gain relevance as research centres. The Centre of Analysis for Research and Innovation, a Mexican think tank, ranked San Luis Potosí eighth of 32 states for public and private investment in science, technology and innovation. One of these is the Potosíno Centre of Scientific Investigation and Technology (Instituto Potosíno de Investigación Científica y Tecnológica, IPICYT), which provides scientific analysis for industries in the region. Alejandro Ricardo Femat Flores, director-general of IPICYT, told OBG that the institute is “convinced that knowledge, technology and innovation support profitable businesses that can transform society.”

In March 2017 Juan Manuel Carreras, governor of San Luis Potosí, announced the creation of the State System of Science and Technology, which he sees as a step towards increasing private sector contributions to and involvement in research and technology. “The Bajío region’s position as an area of high production capacity is an opportunity for San Luis Potosí to become a centre for research and investigation through the right investments and strategic interaction,” Femat Flores told OBG. Several companies have already begun this process, which bodes well for potential research and development centres and their staying power.

San Luis Potosí is ranked

8th

among the 32 Mexican states for public and private investment in science, technology and innovation

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Agricultural production value was up 36% y-o-y at end-September 2016

A key area of potential

Officials look for ways to streamline and add value to agriculture

Approximately 2.75m ha of San Luis Potosí's 6.1m-ha surface area are potential agricultural areas, with around 1.85m ha currently being cultivated.

Agriculture may never be able to compete with the manufacturing industry as a proportion of GDP, simply due to the relative volumes involved, but this does not detract from the importance of the sector in San Luis Potosí's economic development.

Some 2.75m ha of San Luis Potosí's 6.1m-ha surface area are potential agricultural areas, with around 1.85m ha currently being cultivated. Moreover, the Ministry of Agriculture, Livestock, Rural Development, Fisheries and Food (Secretaría de Agricultura, Ganadería, Desarrollo Rural, Pesca y Alimentación, SAGARPA) estimates that around 225,000 people in the state work in agricultural activities, with more than 35% of the state's population estimated to be reliant on the sector. According to the Secretariat for Economic Development, this is despite just 4.7% of the state's GDP coming from the primary sector.

As of the third quarter of 2016, only 7.5% of agriculture jobs were registered with the social security system, meaning the vast majority of rural jobs – generally self-employed producers of coffee, citrus fruits or cattle – in San Luis Potosí are informal. "Our challenge is to make the value of agricultural production in San Luis Potosí grow, and thus generate more respectable jobs," Alejandro Cambeses, secretary of agricultural development and water resources, told OBG. "We must establish more areas of protected agriculture, look for new markets away from the US and Canada, and show our potential to and incentivise the arrival of agro-industrial companies," he added.

CAPITALISING ON CAPACITY: San Luis Potosí maintains a leading position in Mexico in the production of agricultural products. It ranks third in soy beans, tomato, sugar cane and orange production in Mexico, fourth in chilli, fifth in beef, and sixth in beans and goats. According to Gastón Santos-Ward, the state delegate for SAGARPA, investment in different areas has led to increased production in San Luis Potosí of certain products that were nowhere near as important in the

state beforehand. To capitalise on this new capacity, San Luis Potosí must look to add value to its products, something the new administration has already started.

In the 12 months to September 2016 agricultural production volumes were down to 11.91m tonnes – below the state government's target – but the value of production increased by 36% to MXN14.64bn (\$882.4m). Volumes fell because of a 60,000-ha reduction in harvested area, but the value increased thanks to more commercially valuable products, such as dried chilli from Villa de Ramos. Cambeses told OBG that San Luis Potosí's existing production capacity alone is attractive for potential companies, but adds that the state's location – just like in the automotive sector – makes it an ideal choice.

Some potential added-value opportunities involve the product itself; Cambeses highlights using soy beans to make milk or flour, or taking the region's high quality tomatoes to produce paste or sauce, for example. Furthermore, Cambeses told OBG that an international company is in discussions about a potential project to use San Luis Potosí's vast sugar cane production, which reached 5.4m tonnes between October 2015 and September 2016, to make ethanol, and thus provide a renewable energy source in rural areas.

PROTECTED AGRICULTURE: Investment in the cultivating process is providing further opportunities. Tomato production has increased significantly in the state due to a wave of greenhouse construction.

SAGARPA estimates that each hectare of protected agriculture generates eight, better-paid jobs. San Luis Potosí officially has 901 ha of protected agriculture; however, surveys being carried out by the Secretariat of Agricultural Development and Water Resources (Secretaría de Desarrollo Agropecuario y Recursos Hidráulicos, SEDARH) estimate the actual number is closer to 1400 ha. "The building of greenhouses is turning the state into a powerhouse for tomatoes," Santos-Ward told OBG. The potential in San Luis Potosí

San Luis Potosí ranks third in Mexico for the production of soy beans, tomato, sugar cane and oranges; fourth in chilli; fifth in beef; and sixth in beans and goats.

for protected agriculture, which allows for the adjustment of environmental conditions to suit different plants, is aided by strong infrastructure – four gas pipelines traverse the state – and a dry climate in the north, where a majority of the greenhouses are based.

“Protected agriculture allows for high productivity, better quality and therefore higher prices,” Cambeses told OBG. He is aiming to establish 50 ha of protected agriculture for each of the remaining five years of his term. As an added benefit, the new developments in the more remote Altiplano region are helping to stem migration from the countryside into the city. “It brings agriculture jobs to the people without requiring them to move homes,” he added.

San Luis Potosí is also using greenhouses to diversify its product base. Strawberries, for example, had previously not been a farmed commodity in the state. Yet production is beginning to take root thanks to a MXN4.6m (\$277,200) investment, of which MXN900,000 (\$54,200) has come from the state government, MXN2.03m (\$120,700) from the producers themselves and MXN1.67m (\$100,700) from private sector financing and investment.

IMPROVED IRRIGATION: Another area of technology the state government has identified as a priority for adding value to products is modern irrigation, a process that helps to look after groundwater, reduce usage and make production more efficient. In San Luis Potosí irrigation is benefitting sugar cane, chilli and tomato producers, among others. “We have been growing in this area but can grow faster,” said Santos-Ward. When the current administration took office in September 2015, there were 51,384 ha of land in the state that could count on modern irrigation technology. The government is targeting a further 21,000 during its six-year period, and by end-2016 had already added 6408 ha, according to SAGARPA.

CONTRACT FARMING: Large companies are also finding opportunities in San Luis Potosí through contract farming, where Grupo Modelo, the Anheuser-Busch InBev-owned brewer, has come to an agreement to buy malt barley from 900 different producers in Villa de Arriaga. The government supported the MXN33.7m (\$2m) investment by planting 9650 ha of barley with MXN9.6m (\$578,600) of financial support in 2016, and will look to invest a further MXN13.7m (\$825,700) in 2017 to bring the number of farmers to 1400.

For the beer maker, the model allows it to reduce costs by cutting down on imports of malt, which is by far the most costly ingredient in the alcoholic drink. For the producers, it guarantees not just a buyer, but also a price – at MXN4500 (\$271) per tonne. The investment is set to significantly repay the state, with production estimated to have totalled MXN34.74m (\$2.1m) in 2016. Similar models are being followed with vegetable oil company Tron Hermanos, which is buying sunflowers from 300 different producers in the region.

MEAT PRODUCTION: San Luis Potosí is also an important provider of meat – both beef and goat. At the larger end of the scale, meat company Grupo Gusi opened an abattoir and packaging facility in the



The state of San Luis Potosí is an important provider of meat – both beef and goat

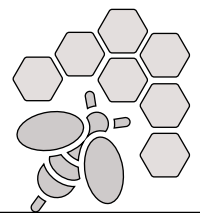
Huasteca region, with a federally certified plant that has capacity to process up to 2400 cattle per day.

However, many cattle and goat farmers are small, individual producers making subsistence incomes from their produce, as is the case for 43.8% of businesses and individuals working in agriculture in the state. Therefore, attempts are being made to bring smaller producers together and eliminate, or at least reduce, the role of intermediaries between buyers and sellers, who in some cases are earning much more than the farmer, according to Santos-Ward.

HELPING SMALL FARMERS: One such programme being carried out to support goat farmers brings buyers and sellers together at markets, or allows small producers access to larger companies. “At the moment, around 20% of the agricultural industry is highly competitive, with access to credit, exports and technology,” Santos-Ward told OBG. “Therefore, one of the biggest areas of potential for the state is in bringing together small producers so they can achieve better prices, eliminate intermediaries and become more competitive.” In the case of goat farmers, this is not only directly improving their profits – which according to Santos-Ward are up by around 40% – but is in turn also allowing smaller producers to have additional cash for investments, thereby increasing productivity.

Bringing small farmers together has also worked well with honey producers in the state, according to Cambeses. “We have helped them multiply volumes by several times, eliminated intermediaries and organised producers together to enable them to reach better-paying markets,” he told OBG. Now around 90% of the honey produced in San Luis Potosí is exported to Germany, Cambeses added. Finding new markets is a key area of potential for the state. “Sometimes I feel we are very good at agricultural production, but not so strong when it comes to selling,” Santos-Ward told OBG. “That is why we are making efforts to reach new markets with events and promotions such as food shows.”

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90%

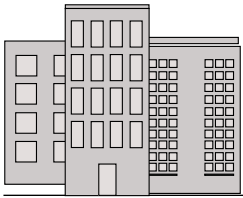
of the honey produced in San Luis Potosí is exported to Germany



High GDP and population growth are set to boost the real estate sector

Looking upward

Challenges and opportunities in construction and development



There is a current deficit of

11,000

homes in and around the state's capital city

With GDP growth above the national average, an expanding population and new immigration from abroad, San Luis Potosí's real estate sector looks set to expand. This will be further encouraged by the deficit of 11,000 homes in and around the capital city, according to Mauricio Ramírez, general director of the State Housing Institute of San Luis Potosí (Instituto de Vivienda del Estado de San Luis Potosí, INVIES).

Yet bureaucratic bottlenecks are presenting challenges to much-needed investment in the area, due mainly to the slowdown in construction permit issuances, as the municipal authorities prepare the Central Population Plan, which will lay down new regulations on the use of land for the capital city. Construction activity in new housing transactions, for example, fell from 16,000 in 2015 to 11,000 a year later. Although the Municipal Planning Institute is right to fix poor practices in legislation, delays in launching the plan have left the industry at a standstill, Ramírez told OBG.

According to Manuel Leal, secretary of the San Luis Potosí branch of the Mexican Association of Real Estate Professionals (Asociación Mexicana de Profesionales Inmobiliarios, AMPI), this is having a negative effect on investment in the city. "This leaves developers with their hands tied, unsure of whether new projects will be profitable or not," he told OBG.

RIPE FOR INVESTMENT: When the plan is finally resolved, however, the city has the conditions to be a strong investment destination. Starting in 2018, real estate group Thor Urbana is preparing to build a series of new developments in the state, including corporate offices, two hotels, a shopping centre and 400 apartments for a total investment of approximately MXN11bn (\$663m). Leal sees Thor Urbana's project as similar to those in the modern high-rise business district of Mexico City, and notes it will be the first development of this style in San Luis Potosí.

SKY IS THE LIMIT: Without government authorisation for new residential areas, AMPI and other developers

are looking upward. According to Ramírez, including a minimum storey limit in certain areas will encourage verticality. San Luis Potosí has cemented its status as a major automotive production centre, but it has some way to go in terms of real estate. "A lot of construction, infrastructure, mobility and services projects are being stopped because they are viewed as too ambitious for this state," Leal told OBG. "Perhaps in order to attract large-scale construction projects, the state needs to think bigger and start to believe that San Luis Potosí can be a strong economic power," he added.

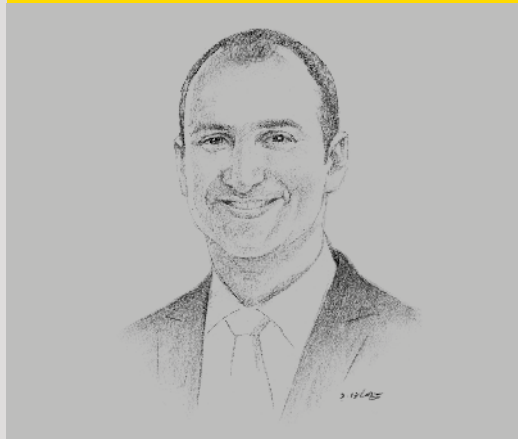
Indeed, according to Jimmy Arakanji, founder and co-CEO of Thor Urbana, when announcing investment plans, San Luis Potosí has too often looked over by developers compared to other cities in the country such as Querétaro and León.

METROPOLITAN RING: Yet even before the capital's plan is available, there will be opportunities for expansion in mixed industrial and residential developments. The *Ciudad Satélite* (Satellite City), for example, is being developed around the Colinas Industrial Park some 16 km outside the city. The area now has 6000 houses and plans to build an additional 30,000. Around 40% of those who work at Colinas are estimated to live in the adjacent residential complex, according to INVIES.

A similar project is under way in Villa de Reyes which houses employees of BMW, GM and Goodyear near the World Trade Centre and Logistik industrial parks. *Ciudad Madera* (Wood City) will be just three minutes from GM's plant and include schools, a hotel, restaurants, sports complexes, medical services and shopping areas to accompany the 8000 residential lots, with an initial investment of MXN2.5bn (\$150.7m).

These kinds of projects help to provide alternative development attractions, according to Ramírez. "It is an opportune moment to consider San Luis Potosí's growth," he told OBG. "The state has potential because of how well it is distributed. The conditions are ideal for real estate investment and development," he added.

The *Ciudad Satélite* is being developed around the Colinas Industrial Park some 16 km outside the capital city. The area now has 6000 houses, and around 40% of those who work at Colinas are estimated to live in the residential complex.



Vicente Rangel Mancilla

Unexpected outcomes

Vicente Rangel Mancilla, CEO, Grupo Valoran; and CEO, Grupo Ranman, on the potential for expanding global trade

What does the implementation of energy reform mean for investment in downstream activities?

RANGEL: Energy reform has been well thought out, and it is a necessity for the country's development, although it could have been communicated to businesses and the general public in a better fashion. The challenge is to implement it in a more rapid way, because people have invested a lot of money in the reform, and they want to see their investments matched by a speedier implementation. That being said, considering the daunting task of the reform, the progress so far has been impressive. In geographic terms, the central region of the country benefits most from storage and distribution. Recently, the rail company, Kansas City Southern, along with Grupo Valoran and energy logistics firm Watco, signed a joint venture to transport refined energy products directly from Texas to the World Trade Centre in San Luis Potosí, cementing San Luis Potosí's reputation as a strategic, central distribution point for the rest of the Bajío region and beyond. Mexico's total fuel reserves stand at around 48 hours, but as the government is obliged to increase this, there are huge opportunities for investors in privately operated storage facilities. So it makes sense that an increase in the need to store the country's most important commodity reserves should mean they are stored in a geographically strategic location in the centre of the country such as San Luis Potosí.

What infrastructure measures should be implemented to help grow the regional economy?

RANGEL: San Luis Potosí is an ideal location not just for the transport of hydrocarbons, but also for a wide variety of products. Studies show it is an ideal place to transport products to the Gulf of Mexico and the Pacific Ocean. The governor is developing a new infrastructure strategy that marks a turning point for the industrial zone of San Luis Potosí, which covers 5000 ha. The current road network is insufficient to support its strong growth. To support this infrastructure plan, the state

needs to focus on other areas, such as its electricity capacity. Until now the Federal Electricity Commission has neglected its role of providing sufficient energy; we hope the energy reforms and the involvement of the private sector will move this forward, and we also have the first distributive generation power plant in the country under the new energy reform in order to push the growth of San Luis Potosí. Mexico also has an economic productivity issue, and it has nothing to do with the market or macroeconomic conditions. Rather, it is about the mindset of workers, who lack the beliefs of their counterparts in more developed markets. With the current situation in the US, companies need to address this issue by incentivising their workers and encouraging them to do supplemental training, which will give them soft skills needed to add value to their employment, and drive them and their productivity.

How will the changing commercial relationship with the US affect the investment dynamic?

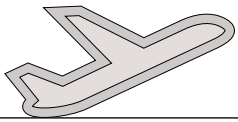
RANGEL: The changing relationship with the US and the hostility of the current administration towards the Mexican economy could produce some unexpectedly positive outcomes. It will help us improve our levels of productivity, and give a collective mental boost to the country for workers and businesses. However, the country needs to create new opportunities for itself. Mexico has free trade agreements with 46 countries, and on a macroeconomic scale we need to use that advantage to forge relationships with new markets. Until now we have not made the most of it, but this is a golden opportunity. We also need to diversify our economic offering to make us a more attractive market. In Asia, especially in leading markets such as Japan, there is more interest than ever to do business with and invest in Mexico. Even in the US, many companies in California and Texas that have strong trading relationships with Mexico are fighting elements of the current administration's policy to protect bilateral trade interests.



The administration is looking to capitalise on remote areas of the state

Work and play

State enjoys rising caché for business travellers and adventure tourists alike



Around
75%

of passengers who use the San Luis Potosí airport are business travellers

San Luis Potosí is perhaps not as popular as the tourist destinations of Oaxaca or Cancún; however, its profile is on the rise. While the historic centre of the state's capital city is an attraction in itself, it is the more remote areas where the current administration is seeking to capitalise on the potential in adventure tourism.

From the ghost town of Real de Catorce in the northern plateau region, to the rainforest, rivers, waterfalls and indigenous cultures of the Huasteca region in the south-east, the state is home to diverse potential attractions. Tourism, therefore, can provide an opportunity to diversify economic activity away from San Luis Potosí's central region, which accounts for just over half the population but 84.1% of GDP.

BUSINESS DESTINATION: For the first 11 months of 2016 the state recorded a hotel occupancy rate of 69% – the highest among 70 of Mexico's inland cities. Those in highest demand were four- and five-star hotels, suggesting the prominence of business travellers. Indeed, a press release from the governor's office credited the 123 conferences and conventions for the 1.39m visitors that San Luis Potosí received in the 12 months to September 2016 – a 10% increase year-on-year. According to Marco Antonio Camarena, regional administrator of San Luis Potosí's airport, around 75% of passengers who use the airport are business travellers, with the remaining 25% consisting of leisure travellers or locals. According to Juan Manuel Carreras, governor of San Luis Potosí, the continuing increase in business travellers is driving the arrival of more hotels, with more than 30 under construction as of November 2016. In June 2016 the US-owned Staybridge Suites opened its first hotel in the city, catering to those coming to spend extended time working at the state's various foreign-owned industrial plants.

That does not mean, however, that business travel and leisure tourism are entirely separate phenomena. Bernardo López, general director of Logistik industrial park, told OBG that the quality of life and the nearby

leisure options were one of the attractions that encourage foreign companies to move to San Luis Potosí. The French, Germans and North Americans, for example, that own and run craft brew pubs in the old centre add to a sense of safety and contribute in building a thriving nightlife. Not everywhere in Mexico can offer this to visiting workers. Moreover, "industrial growth is an opportunity to promote local tourist attractions and make the sector more important", Artur Esper Sulaiman, secretary of tourism for San Luis Potosí, told OBG. "For the moment just 15% of tourists in the state come from foreign countries, and the administration would like to increase that," he added.

UNTAPPED BEAUTY: One way to do this is by displaying regional attractions at trade fairs and expos. San Luis Potosí hosted the Adventure Travel Trade Association's AdventureNEXT trade fair 2016 – the first time the expo was held in Latin America. The state also participated in the Chicago Travel & Adventure Show and The Boston Globe Travel Show earlier this year. "We have multiple nature and adventure locales, and we believe we can become one of the leading destinations for this kind of tourism in Mexico and worldwide," Carreras told OBG. "Given the remote nature of some of San Luis Potosí's greatest destinations, however, the government needs to ensure we are making the necessary investments in infrastructure to increase visitors to the region," he added.

Investment will not focus solely on transport, however. As in other sectors, tourism growth requires the state to develop education programmes for workers, something that the Carreras administration has outlined in its six-year plan for the sector. "Mexico's *Pueblos Mágicos* (Magic Villages) programme is bringing funds to the state," Manuel Lozano, secretary of labour for San Luis Potosí, told OBG. "Through the federal programme, MXN2.5m (\$150,700) has been invested in training tourism-related businesses in the state's two Pueblos Mágicos – Real de Catorce and Xilitla."



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GDP growth for 2016 was expected to ease slightly to around 2.1%

Upbeat forecast

Investor sentiment strong despite regional political changes

Foreign direct investment remained strong in 2016, continuing a trend that has seen inflows reach historic highs of \$33bn per year on average since 2014.

Improving employment figures and the strong performance of a number of key sectors were offset by slower growth and uncertainty over the impact of the US President Donald Trump's administration on the economy, which is set to be a major theme in 2017.

While GDP growth for the year was expected to ease slightly to around 2.1% from 2.5% in 2015, according to the IMF, investor sentiment remained strong, buoyed by the government's decision to begin implementing an ambitious programme of structural reforms. However, the US election result in November 2016 sent ripples through the economy, driving down the peso and raising the prospect of ratings downgrades in the new year.

UNCERTAIN TIMES: Early December 2016 saw Fitch follow in the footsteps of fellow ratings agencies Moody's and Standard & Poor's by revising its outlook for the Mexican economy from stable to negative.

The agency cited particular concerns that the US could reduce Mexico's tariff-free access to its neighbour's market by making changes to the North American Free Trade Agreement (NAFTA).

"Attempts to renegotiate NAFTA or hinder the outsourcing of activity from the US to Mexico could prove to be disruptive for the Mexican manufacturing export sector and adversely impact employment, investment – including foreign direct investment – and the country's growth," Fitch cautioned. At present, 80% of Mexico's total exports are purchased by the US.

All three agencies said they expected Mexico's rating to be reviewed in 2017, on the back of uncertainty related to growth and the potential impact of the incoming US administration on the country's economy.

Mexico is already feeling the weight of concerns over policy realignments north of the border. Pricing on credit default swaps has risen 11% since the US election and is threatening to push up overseas borrowing costs further still.

SOLID FOUNDATIONS: However, while question marks continue to hang over future US-Mexico trading

relations going into 2017, industry players remained broadly upbeat. Some point out that NAFTA was due an overhaul, while others note that changes to the agreement could spur Mexico into building stronger trade relations with other countries.

"If [NAFTA] is modernised, I am certain that would help the country to develop even further," Carlos Rojo, CEO of Grupo Financiero Interacciones, told OBG. "However, looking ahead, in the unlikely event that President Trump chooses to void it altogether, I believe that Mexico could, instead, focus its efforts on fostering stronger trade relations with other countries, while also bolstering the internal economy."

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Many of the country's key indicators also looked sound towards the end of 2016. Unemployment had fallen to 3.6% by the end of October, according to data issued by the National Statistics Institute in November, marking its lowest level in nine years.

Inflation, too, remained relatively stable in 2016. The consumer price index had risen 3.31% year-on-year as of November, having edged up from 2.61% at the beginning of the year. In its latest global outlook report, the IMF said it expected consumer prices to increase by 3.3%, before cooling slightly in 2018 to 3%.

At least some of the change in prices was caused by a drop in the peso's buying power: the local currency depreciated by around 12% following the US election and was trading at just over 20 pesos to the dollar in mid-November.

The Bank of Mexico raised its key rate by 50 basis points to 5.75% in mid-December, in what marked its fifth hike of 2016. The central bank has now raised its rate by 275 basis points since the US's initial rate increase, implemented in December 2015. A weaker peso will add to Mexico's import bill and is likely to contribute to higher costs and inflation in the new year.



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