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Mexico – From a Short Nearshoring Boom to US "Security-shoring"

Günther Maihold

With the reconfiguration of international supply chains, Mexico has gained importance as a location for new foreign investments. The country has been able to benefit from nearshoring, that is, the relocation of services or production processes closer to consumer markets. This is associated with lower logistics costs and often better management of supplier relationships. However, this boom in investments has abated due to various uncertainties – not least being Washington's threats to raise tariffs, which burdens the economic prospects associated with nearshoring. Mexican President Claudia Sheinbaum is attempting to counter this trend, but in view of the increasingly urgent demand by the United States for third countries to adopt an anti-Chinese course, Mexico is at risk of being caught in the trap of "security-shoring" and losing its autonomous room for manoeuvre. This is already forcing Mexico – as well as its economic partners who have invested there – to realign their production processes.

US President Donald Trump initially imposed tariffs of 25 per cent on Canadian and Mexican exports to the United States in early February based on the *International Emergency Economic Powers Act* (IEEPA), then exempted vehicles produced in Mexico and Canada that are delivered to the United States from the tariffs. Days later he postponed the implementation of the tariffs on almost all goods for four weeks until 2 April. On this "Liberation Day", Mexico was not — unlike countries worldwide — subject to a general tariff rate of 10 per cent. The exemption applies to all products that comply with the free trade agreement known as the United States — Mexico — Canada Agreement (USMCA). Goods beyond that are subject to different tariff rates.

The announcement of blanket tariffs on imported steel and aluminium by President Trump has had a wide range of effects. Above all, it fuels a climate of uncertainty among all economic actors, as they cannot rely on stable framework conditions in the medium term. Legally, Trump used an emergency order as the basis. Its activation was justified by referencing the growth in the smuggling of the designer drug fentanyl into the United States, and the persistently powerful role of organised crime in the neighbouring country. President Sheinbaum promised to deploy 10,000 soldiers to

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German Institute for International and Security Affairs

Mexico's northern border to stem the influx of drugs and undocumented migrants. In addition, 29 leaders in the drug trade have been arrested and extradited to the United States. However, these measures have not succeeded in reversing the imposed actions.

The disruptions associated with these uncertainties affect both trade and investments, which are of central importance to Mexico due to its favourable production conditions (especially low wages) and were the main reason that the country overtook China in 2023 as the most important trading partner of the United States.

The protectionism being pushed by Trump is having a major impact on Mexico's bilateral relations with the United States, and will continue to do so for the foreseeable future. Furthermore, the Trump administration has intertwined trade, migration, and security policy issues — a tactic that runs counter to the efforts of the Mexican government to keep these policy areas separate and negotiate them according to their respective logics. The USMCA, which was negotiated during the first Trump administration and came into force in July 2020 with Mexico and Canada as US partners, provided the appropriate framework for this. However, the future of this agreement, which is to be reviewed in 2026, is in question since unilateral tariff decrees have undermined its validity. The Mexican automotive industry is being hit particularly hard by the tariffs. Trade in motor vehicles accounts for 22 per cent of total goods traffic under the agreement and is thus considered the most critical sector. Of the 3.98 million vehicles produced in Mexico in 2024, 3.47 million were exported abroad, underlining Mexico's importance as a key hub for the sector.

Nearshoring is an economic opportunity for Mexico

Due to its strategic geographic location, its time zone, and the availability of labour, Mexico has become an increasingly attractive location for companies seeking to improve efficiency and reduce costs. Against the backdrop of the trend to relocate companies or segments of production — such as manufacturing stages or equipment configurations — from Asia to Mexico, the Mexican government hoped that these competitive advantages would attract significant amounts of new industry to the country. With the reconfiguration of international supply chains following the shift away from China, Mexico was expected to become the main beneficiary of new foreign investments. In 2023, the country achieved a record high US$36.06 billion in foreign direct investment (FDI). For the southern neighbour of the United States, the nearshoring boom thus represents a historic opportunity that may not return for decades. By relocating business processes to a nearby country, nearshoring offers numerous advantages such as geographic proximity, cultural alignment, and cost savings.

In Mexico, there is hope that the country can use the tailwind of the nearshoring trend to transition from being merely a production site to becoming an innovation hub. The ongoing trade conflict between the United States and China — and the tariff increases imposed by the Biden administration on imports from China — have been interpreted in Mexico as an additional incentive for companies to seek proximity to the US market. Even Chinese firms have decided to relocate operations to Mexico in order to continue exporting to the United States and thereby circumvent the high tariffs. Between 1 January 2023, and August 2024, more than 400 investment projects with a total volume of US$170 billion were announced; President Sheinbaum has since even mentioned a figure of US$200 billion. Nearshoring has become a new option for Mexico, as it is critical for the growth of certain strategic sectors (real estate, automotive, technology). The boom had already begun to take shape in 2022, when investment plans totalling more than US$9 billion were announced. A year later, carmaker Tesla revealed plans to build a new factory in Mexico, with projected costs of around US$5 billion.

But this nearshoring boom came to a sudden halt in 2023: Although Mexico registered the aforementioned record inflow of FDI in the same year, the share of new investments only reached the second-lowest level since 2006, the year when the Ministry of Economy began publishing investment data. The calculated US$4,817 billion accounted for just 13 per cent of total FDI in 2023. In the previous year, this figure had been US$18,147 billion, representing 50 per cent of all investments. As a result, the productivity, competitiveness, innovation, and employment boost that the government had hoped for failed to materialise. Finally, in July 2024, Elon Musk also put the announced construction of the Tesla factory on hold, so the expected signalling effect of that investment did not manifest either. Consequently, financial commitments in the steel and aluminium industries — which were intended to flow into car body production — were also called into question; other suppliers likewise stepped on the brakes.

The punitive tariffs from Washington, which are having cumulative effects particularly in the automotive sector, are cited as possible reasons why investors are postponing — or even entirely withdrawing — their previously announced investment commitments. Additional factors include the country's well-known deficits in energy and water supply, an opaque judicial reform that includes the direct election of judges by the population, inadequate law enforcement, and an unstable security situation throughout the country — issues that have not been resolved, despite recent successes in apprehending key cartel leaders and extraditing them to the United States. While some US carmakers such as GM, Ford, and Stellantis reportedly have unused capacity in the United States to marginally increase domestic production, the majority of corporations still view Mexico as indispensable for maintaining their product offerings on the US market. Their pressure was likely a key reason why the initially announced 25 per cent tariffs were suspended for one month.

Attempts to rescue the nearshoring effect

In Mexico, there is growing concern that the eagerly anticipated nearshoring bubble could burst. Declining figures for commercial property rentals seem to indicate that this is already happening. As a result, the Mexican president is making efforts to revive nearshoring. She aims to attract foreign investments totalling US$277 billion. Rhetorically, she is relying on a traditional line of argument: that the time has come for Mexico to jointly usher in a new phase of economic development. As the neighbour of the world's largest economy, the country is in a unique position to benefit from nearshoring — in the terminology of the Biden administration, "friendshoring" — in a world where the United States—China rivalry is reshaping investment decisions and supply chains. Yet this discourse does not reflect the new reality: The Trump administration seems to have no "friends", and its "Make America Great Again" objectives contradict such notions. In a time of rapid geopolitical and geoeconomic shifts and growing scepticism towards globalisation, Mexico can only benefit if internationally operating companies are able to count not only on optimised supply chains and lower operating costs, but also on stable framework conditions. Even if the effects of the US tariffs are temporary, the uncertainty may persist longer — especially if the United States and Mexico fail to reach a consensus on sensitive issues that are expected to be addressed in 2026 during the renegotiation of the trilateral USMCA.

These manifold uncertainties are already affecting Mexico's economic momentum. Even before President Trump's return to office, the International Monetary Fund (IMF) predicted that the Mexican economy would grow by only 1.5 per cent in 2024 and 1.3 per cent in 2025 — figures that are clearly below the Latin American average of 2.1 and 2.5 per cent, respectively. In April, the IMF prognosticated that Mexico's economy would contract by 0.3 per cent in 2025, a significant downward revision of 1.7 percentage points from its January forecast. In light of the unpredictability resulting from ongoing tariff and trade policy developments, the Organisation for Economic Co-operation and Development has revised its forecast for Mexico's growth down to 1.3 per cent in 2025 and 0.6 per cent in 2026. Nearshoring is in decline.

A frontal attack by Trump and the Republicans on Chinese production in Mexico could exact a further toll, especially if currency risks increase Mexico's debt service burden. Reduced investments and exports due to the uncertainty — especially in foreign trade (tariffs), the unsecure flow of remittances (due to the deportation of Mexican nationals from the United States and the impact of a remittance tax), and a decline in tourism (due to the threat of criminal violence) — could further diminish capital inflows into the country.

In response, at the beginning of the year, the Mexican president sought to give nearshoring a fresh impetus by launching a package of tax incentives to promote the establishment of foreign companies in Mexico. This extended a decree that is now set to remain in effect until the end of 2030. According to the decree, tax benefits will be granted in the form of immediate deductions of the purchase price of new fixed assets and additional deductions for expenses related to worker training. These benefits can be claimed both by companies already operating in Mexico and by those planning to set up operations there. The objective of extending these tax incentives, according to the decree, is to promote investment in Mexico and enhance corporate productivity. Added to this are tax relief measures — mainly reductions in fuel taxes, income tax, and value-added tax — that apply in the northern and southern border regions.

Plan México – a preventive programme

On 13 January 2025, President Sheinbaum — in a rare show of unity with representatives of the private sector — presented "Plan México" as a long-term framework for realigning the country, especially in light of increasingly complicated relations with the United States. The programme aims to take the wind out of the sails of sanctions against Mexico following the inauguration of Trump by making the country less dependent on Chinese imports and, at the same time, working to shield it more effectively from Trump's economic priorities. Initially, the plan was above all a call for calm — issued one week before President Trump's inauguration. Since then, the government — emboldened by its demonstrative alliance with the business sector — has endeavoured to chart a clear course that is guided by the maxim of preserving national sovereignty and characterised by order and prudence in anticipation of turbulent times ahead.

The plan aims to reduce dependency on China and increase the share of North American content in trade, in accordance with the rules of origin in the USMCA. Furthermore, it seeks to raise the domestic volume of products exported to the United States. To achieve this, the state wants to promote technological innovation within domestic industry while simultaneously providing targeted incentives across different regions by establishing so-called development hubs with industrial parks and research institutions.

Ultimately, the plan is a national industrialisation strategy with several objectives: to protect Mexican workers, ensure fair trade, promote more locally and regionally oriented production with higher value creation, and deepen regional integration. A key aim is to strengthen the competitiveness of domestic industry within the local and regional markets and to advance import substitution by expanding national value chains. This is intended both to create new jobs and to address regional imbalances in the country's economic development. Currently, just 4 of Mexico's 32 federal states account for nearly 40 per cent of the country's gross domestic product (GDP). This imbalance is to be addressed through an ambitious public investment programme in water and electricity supply. The same applies to road infrastructure, which is to be made safer in light of ongoing attacks by drug cartels. The overarching goal is to increase national input, quickly expand the domestic production platform, and boost investment. The fact that these plans were presented under the heading “Import Substitution” during the launch of Plan México makes it clear that imports from China are a specific target — especially those involving the supply of auto parts and accessories for Mexico’s automotive sector.

Among the plan’s 13 goals, the aspiration to elevate the country from the world’s twelfth-largest to the tenth-largest economy — surpassing Australia and South Korea — stands out. This is to be achieved primarily by raising the investment share of GDP to more than 25 per cent and creating 1.5 million new jobs by 2030. Particularly in the sectors for textiles, footwear, furniture, and toys, the aim is for 50 per cent of in-country demand and consumption to be met through domestic production. Overall, Mexico’s value-added share is to increase by 15 per cent. In public procurement as well, 50 per cent of expenditures are to be sourced from domestic production. These ambitious targets are complemented by corresponding benchmarks for education, the pharmaceutical sector, and tourism; further measures include regulatory simplification for businesses and financing opportunities for small and medium-sized enterprises.

The approach underlying the economic development plan also includes elements aimed at addressing criticism being voiced in Canada regarding Mexico serving as a backdoor for Chinese goods. For instance, Doug Ford, the Premier of Ontario, which is Canada’s largest province, proposed excluding Mexico from the USMCA. One of the core priorities of Plan México is the reshoring of products into Mexican production that were imported from abroad — especially China — over the past decades. If just 10 per cent of Chinese exports to North America were replaced by regional products, Mexico’s GDP would increase by 1.2 per cent, the United States’ by 0.8 per cent, and Canada’s by 0.2 per cent. It is evident that Washington, too, will demand a different approach towards China when the free trade agreement is up for review, in 2026 at the latest.

Despite the ambitious goals of Plan México, there are doubts regarding its implementation. One question is how the necessary capital will be mobilised in view of Mexico’s limited public finances, particularly given the expectation of declining investment interest from abroad. Another challenge is that the time horizons for the intended transformation of the national production platform may not align with the politically anticipated short-term steering effects, making it unlikely that there will be observable impacts in the near future.

From “friendshoring” to “security-shoring”

The Biden administration had framed its concept of geopolitical reordering under the motto of “friendshoring”. It recommended shifting supply chains away from China towards trusted countries. This was intended to continue ensuring free market access and reduce risks to the US economy as well as to closely aligned trading partners. By highlighting certain partners such as Mexico — due to their identification with US values — the concept of nearshoring was imbued with a strong normative dimension. This became evident as early as 2022, when the Biden administration launched its competition with China through three legislative measures: the Inflation Reduction Act, the CHIPS Act, and the Infrastructure Investment and Jobs Act. These measures initially focused on four global value chains: semiconductors, large batteries, critical minerals and metals, as well as pharmaceuticals and pharmaceutical chemicals.

Now, the second Trump administration has taken a more aggressive approach to supply chain policy, subordinating the United States’ international relations with

China to its own national security and domestic political interests. Nearshoring is thus losing its distinction as a seemingly neutral strategy for relocating production from Asia to Mexico; instead, Washington has placed national security interests above all else in its dealings with China. As a result, Mexico runs the risk of being caught between the grinding stones of the two great powers in its economic relations.

Mexican economist Enrique Dussel Peters therefore recommends using the term "security-shoring" to describe the strategy being practiced by the United States. This, he argues, better reflects the fact that Washington is pursuing its interests against China using a wide array of tools and measures. The systemic rivalry and confrontation between the United States and China mean that third countries must adopt specific measures to comply with growing US pressure to follow its lead. Third countries and regional blocs are thus being drawn into the specific measures that Washington is proposing — such as in the areas of trade and FDI — according to US national security considerations, without being able to exercise their own strategic options.

In this context, a Chinese company's investment in Mexico is no longer seen as a clever nearshoring move to gain access to the US market, but rather as a potential risk of concern in a costly geopolitical confrontation between superpowers. The United States is putting pressure on third countries to adopt US rules and instruments to limit engagement and cooperation with China — otherwise, there will be a price to pay, such as higher costs for access to the US market or even complete exclusion from it.

This exact policy from Washington is currently Mexico's greatest concern — one it seeks to prevent in these challenging times for global free trade. However, Mexico's efforts are currently being hampered by two developments: the tightening of the US "security-shoring" strategy, which is accompanied by a triangulation of trade policy between China, the United States, and Mexico; and a decline in FDI. By elevating trade and investment decisions in third countries to a matter of US national security, they are largely removed from national decision-making and bilateral relations. Mexico's efforts to maintain a consensual bilateral relationship with the United States thus are leading to a confrontation, which Mexico's president is trying to avoid.

A large portion of Mexico's economic policy is therefore placed from the outset into a triangular trade system between the United States, China, and itself, in which geopolitical considerations gain central importance. But the effects of US policy go far beyond this: The United States' efforts to decouple from China in recent years have undermined institutions and regulatory frameworks such as the World Trade Organization, along with the associated principles of reciprocity and most-favoured-nation treatment.

The US government has announced plans to establish a component-level procedure to certify the US content of auto parts, so that the 25 per cent tariff will apply only to the value of their non-US content. This means that auto parts compliant with the USMCA will remain exempt from tariffs until the US Secretary of Commerce — together with US Customs and Border Protection — introduces a procedure for applying tariffs to their non-US content.

Outlook: Mexico's economy and its international investment and trade partners at a turning point

If Mexico wants to maintain its position as the United States' most important trading partner beyond 2023, it will have to integrate fewer and fewer Chinese value-added components into its exports to the United States — otherwise, it risks facing tariffs under the Trump administration. Some of the measures included in President Sheinbaum's Plan México preemptively address these potential consequences of "security-shoring" in an effort to disarm such accusations from the US president before they arise. However, this adaptation comes at a high cost for the Mexican government. It must significantly increase public investment in the areas of energy generation, water supply, transport, and education. In doing so, the president is primarily relying on contributions from the private sector, which has at least verbally offered her its support.

Given Mexico's massive trade deficit with China (US$62.7 billion in 2023) — which is more than offset in value by its foreign trade surplus with the United States (US$152 billion in 2023) — potential trade restrictions by the US government could seriously jeopardise Mexico's established "business model". This explains President Sheinbaum's interest in replacing Chinese imports with domestic products to achieve greater independence from China. At the same time, this would also reduce the Mexican government's vulnerability to attacks from Washington within the framework of "security-shoring", even if the restructuring processes only yield results in the medium- to long term.

Substituting Chinese auto parts — which is particularly important for export goods in the automotive industry — with domestic products is likely possible only to a very limited extent, especially since many imports, particularly components for the automotive industry, operate through intra-company trade. Both President Sheinbaum and her predecessor, López Obrador, have repeatedly emphasised that Mexico does not wish to serve as a "springboard" for Chinese exports to the United States.

It remains uncertain as to whether the renewed interest in Mexico as a nearshoring location will prove sustainable, and whether the associated hopes — such as those voiced by international financial services provider J. P. Morgan in July 2023, when it declared a "New Mexican Moment" — will be fulfilled. Since that time, momentum has declined considerably, and Mexico is facing increasing pressure due to the security and trade interests of its northern neighbour. This could lead to the nearshoring expectations being quickly suffocated by the triangular logic of "security-shoring". International investors who have thus far taken advantage of Mexico's position as an extended workbench of the United States would also be affected.

President Sheinbaum's Plan México addresses some of the anticipated challenges, but its success depends on scarce public resources and the country's ongoing internal security issues. Only a sustainable strategy aimed at improving competitiveness can help the country seize the hoped-for "moment" and place Mexico on a new path to growth. This will hardly be achievable without new foreign investment. Therefore, in addition to the pressure exerted by the United States, the Mexican government must also do its homework if the country is to transition to resilient supply chains. The time to begin making those changes is now. Otherwise, the review of the USMCA in 2026 by the three North American countries will bring a difficult reconfiguration of trade relations.

For the German automotive industry — which relies heavily on Mexico for its US operations — these developments represent another significant blow. Although it moves in the slipstream of its American competitors and might benefit from their lobbying efforts, this would only be the case if the resulting exemptions are not limited to US-based firms. For Audi and Porsche, which have no production facilities in the United States, vehicle sales from their Mexican plants into the northern neighbouring country could be subject to massive price increases, and thereby suffer declining sales. BMW, which has been active in South Carolina and producing certain model series in a plant in San Luis Potosí since 2019, would see a portion of its US market offerings affected. For Volkswagen, the effect on certain product lines would be even more pronounced. Mercedes, too, would incur significant additional costs for truck models due to certain drive systems and components produced in Mexico.

Given the complexities of the respective supply chains, a short-term relocation of production facilities appears economically unviable. Much will therefore depend on a general regulatory solution that would need to be agreed upon in the course of the

USMCA review negotiations. Without such predictable foundations, stabilising Mexico's role in the network of international supply chains — especially in the strategic automotive sector — will hardly be successful and only lead to a decline in the volume of produced and exported vehicles in the future. Only if the three parties fail to find a negotiated solution will it be possible to gauge the full extent of the potential costs of "security-shoring" for economic actors.

This Comment reflects the author's views.

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SWP
Stiftung Wissenschaft und Politik
German Institute for International and Security Affairs

Ludwigkirchplatz 3—4
10719 Berlin
Telephone +49 30 880 07-0
Fax +49 30 880 07-100
www.swp-berlin.org
swp@swp-berlin.org

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