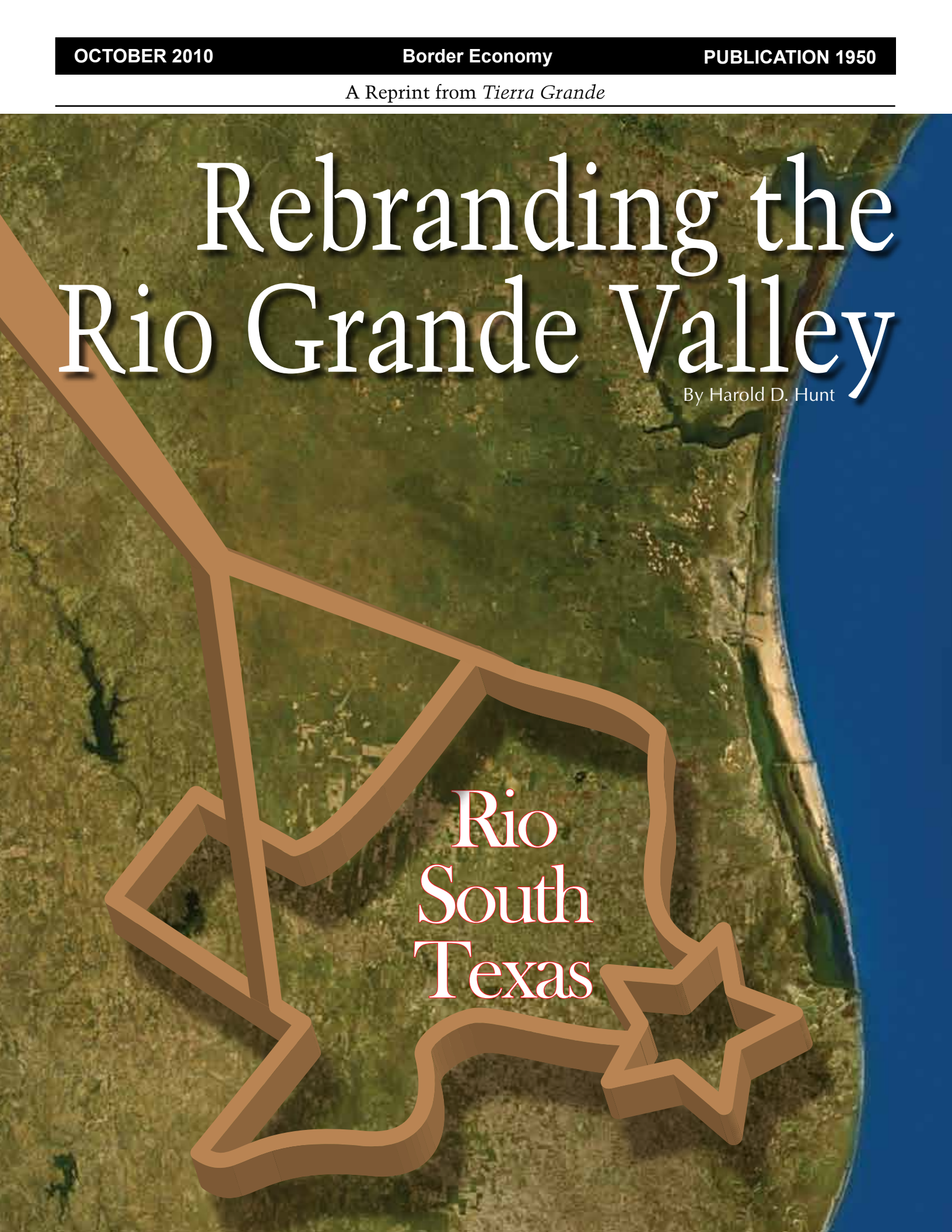


Rebranding the Rio Grande Valley

By Harold D. Hunt



Rio
South
Texas

During the last decade, China pushed past the Mexican maquiladoras to become the leader in supplying all manner of manufactured goods to the United States. But skillful gamesmanship and a bit of luck may deal the Rio Grande Valley a winning hand in the coming years. That bodes well for the local economy and the region's commercial real estate markets.

The China Syndrome

Mexican manufacturing plants located in the border cities of Reynosa and Matamoros have been a driving force in the Valley's economy for more than three decades. As the manufacturing base became established on the Mexico side, the Valley increasingly benefited from the warehousing, transportation and other service-related jobs supporting the shipment of goods into U.S. markets.

Proximity has always been a major advantage for Mexican maquiladoras. Their location near the U.S. border has facilitated speedy, efficient delivery of finished products to American consumers.

Between 1995 and 2000, the North American Free Trade Agreement helped triple the volume of products assembled or manufactured in Mexican maquiladoras and exported to the United States. But the maquiladora model was challenged in 2001 when China became a member of the World Trade Organization.

The ensuing removal of U.S. trade barriers with China triggered an exodus of many major U.S. companies from Mexico. The thought was that cheaper Chinese labor could be profitably substituted for Mexico's superior proximity. The result was fewer trade-related jobs in the Valley.

The dream of bigger profits did not always match the reality, according to Dr. Barry Lawrence, professor of industrial distribution at Texas A&M University. Lawrence asserts that many firms did not consider the total cost of doing business in China, instead focusing primarily on labor costs.

"Labor won, but for all the wrong reasons," says Lawrence.

In the end, labor often was not significantly cheaper after factoring in all cost components, including the cost to find bilingual people to train a Chinese workforce, and significant employee turnover.

More recently, labor unrest has become a serious

problem. Average wages in China have risen by more than 50 percent since 2005, up about 15 percent per year just since 2008. Whether or not China revalues its currency, labor demands will continue to act as a de facto currency revaluation, working against the country's competitiveness for the foreseeable future.

Couple all of these concerns with unpredictable transportation costs, the challenge of managing more complex and

variable inventory levels, frequent theft of intellectual property rights, Chinese government bureaucracy and the cost to shuttle executives to the plants, and the original maquiladora model has renewed appeal.

In February 2010, AlixPartners Business Consultants analyzed a variety of products and compared their manufacturing costs in the United States with those in 12 lower-cost countries. Results revealed that Mexico is the world's lowest-cost component manufacturer. KPMG's recent report, *Competitive Alternative 2010*, ranked Mexico as the world's most cost-competitive location among developed nations in all industry sectors.

Valley's Response: Rio South Texas

As China's allure has slipped, the Rio Grande Valley has come up with a new plan for the future. Twenty-six different interest groups and municipalities on both sides of the U.S.-Mexico border have teamed up to market the four southernmost counties and northeastern Mexico as one region known as "Rio South Texas."

The 90-mile-long by 60-mile-wide area (see map) is home to about 3.5 million people on both sides of the border. By the year 2040, that population is expected to double to seven million.

Rio South Texas was created to showcase the area's critical mass of labor and consumers to attract private sector investment, economic diversification and business expansions. When the Mexican population is included, Rio South Texas represents the 23rd largest population base in the United States and the third largest in Texas after Houston and Dallas-Fort Worth.

The region has staked out a new logistical paradigm, marketing itself as the "Third Coast," a major distribution hub for North America. The Third Coast is a reference to the Port of Brownsville, which complements the Mexican Pacific Coast

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ports of Lazaro Cardenas and Manzanillo and the Mexican Gulf Coast ports of Altamira, Tampico and Veracruz.

The goal is to funnel manufactured components produced in Mexico and other countries through Rio South Texas. Finished products can then be delivered faster and more efficiently via a single distribution center on the American side of the border.

"In the Third Coast logistical model, shipments arriving at Mexican ports are moved by truck or rail into Rio South Texas,



AUTO PARTS are among the many items manufactured in Mexico's maquiladoras, then warehoused and shipped from U.S. distribution centers in South Texas to buyers throughout the country.

where they are combined with products produced in maquilas in Reynosa and Matamoros, then shipped directly to a U.S. customer," says Keith Patridge, president-CEO of the McAllen Economic Development Council.

Forging Ahead with Infrastructure

A number of new infrastructure projects are in the works for the region, enhancing its competitive edge. The North Rail Project is designed to remove all Union Pacific mainline switching out of the City of Harlingen, resulting in fewer traffic delays.

West of Brownsville, construction has begun on the first new railroad bridge across the Rio Grande in more than 100 years. Union Pacific on the U.S. side and Kansas City de Mexico (Kansas City Southern's Mexican subsidiary) on the Mexico side will operate the bridge jointly. Kansas City de Mexico offers freight rail service from the Port of Lazaro Cardenas to Matamoros.

The bridge's total cost will be about \$100 million according to Cameron County Regional Mobility Authority Chairman and commercial real estate broker David Alex. Twenty-five crossings in downtown Brownsville and 15 in downtown Matamoros will be eliminated with the completion of the rail bridge, dramatically improving rail efficiency and safety, according to Alex.

Mexico is also constructing a 400-acre intermodal yard west of Matamoros that is scheduled to be completed in two to three years, coinciding with completion of the railroad bridge. Financing is already in place to turn the existing rail right-of-way through downtown Brownsville into a tolled internal parkway.

Tolls will be used to support a number of future road projects in Cameron County. Alex says that TxDOT funds are

extremely limited, and the county does not have time to wait until they become available. The region has received \$120 million in federal funds, much of which will be used for infrastructure development.

Other proposed toll projects include a West Loop and East Loop to divert freight traffic crossing the border away from downtown Brownsville. The East Loop will provide direct access to the Port of Brownsville. A tolled second causeway connecting South Padre to Hwy. 77 is in the planning stages.

"This will open up about 4,000 new acres for development that will create \$8 billion in new real estate in the region," says Alex.

The Port of Brownsville recently spent nearly \$10 million deepening its ship channel.

"Fifteen miles of the man-made channel are now 42 feet deep while the last two miles are 36 feet deep," says German Rico, director of business development for the port.

Rico notes that a study is being conducted to determine whether to further widen and deepen the ship channel to handle larger Panamax and Post Panamax vessels. Increased ship traffic is expected in the Gulf of Mexico when the widening of the Panama Canal is completed around 2014.

"2010 is going to be a better year than last year for the port," says Rico. "In 2011 and 2012, the port will be able to add wind-mill components to its list of cargo with the introduction of a new \$60 million wind turbine facility."

The plant, owned by South Korean firm CS Wind, is being constructed in Matamoros. The company will manufacture metal towers and generator components for large commercial windmills. The new plant will primarily serve the Midwestern United States.

Job Diversification Through Education

The U.S. Department of Labor reports that industrial output nearly doubled during the past 30 years. However, manufacturing employment has declined by about 40 percent during the same period.

The loss of manufacturing jobs in both McAllen and Brownsville has exceeded the national average. The two Metropolitan Statistical Areas (MSAs) have retained only about half the manufacturing jobs they reported in 2000 (see table). As a result, the MSAs are striving to develop a more diverse job base.

So far, the largest job gains have occurred in the service sector. Within that category, health service jobs have increased the most. About half the total nonfarm employment increases in the McAllen MSA and two-thirds of the increases in the Brownsville MSA since 2000 have been related to generally higher-paying health service jobs.

"A number of health-related entities have recently chosen to locate in the Rio Grande Valley," says Bill Martin, CEO of the Harlingen Economic Development Council and chair of the Rio South Texas Economic Council. "In Harlingen alone, we have captured a UnitedHealth Group service center, a new Veterans Administration Ambulatory Surgery Center and a third- and fourth-year medical student training facility for University of Texas (UT) Health Science Center's Regional Academic Health Center," he says.

Martin points out that many of the new jobs in the health services category are outside traditional hospital-related employment.

Education and Workforce Training

As governor of Texas, George W. Bush helped create a ten-year economic development plan for the Rio Grande Valley that strongly emphasized vocational and technical training.

"We didn't have any technical training in the Valley before the ten-year plan," says Alex. "We just had a large pool of labor. Now we have both."



Source: Brownsville Economic Development Council

Vocational training schools in the Valley include Career Centers of Texas (Brownsville), South Texas Vo-Tech Institute (Weslaco), Southern Careers Institute (Pharr), South Texas

Employment Growth by NAICS Designation (July 2000 to July 2010)

NAICS Industry	State of Texas		McAllen/Edinburg/Mission MSA		Brownsville/Harlingen MSA	
	10-yr. Total Percent Change	Total Jobs Lost or Gained	10-yr. Total Percent Change	Total Jobs Lost or Gained	10-yr. Total Percent Change	Total Jobs Lost or Gained
Total Nonfarm	10.07	945,600	40.92	62,600	13.77	15,000
Total Private	8.29	656,000	42.42	49,000	11.68	10,000
Goods Producing	-8.89	-159,200	-31.02	-6,700	-42.35	-7,200
Mining, Logging, and Construction	10.27	74,000	-13.13	-1,300	-20.00	-900
Manufacturing	-21.80	-233,200	-46.15	-5,400	-50.40	-6,300
Service Providing	14.54	1,104,800	52.74	69,300	24.16	22,200
Private Service Providing	13.31	815,200	59.32	55,700	25.07	17,200
Trade, Transportation, and Utilities	4.18	82,200	31.10	10,700	6.51	1,400
Wholesale Trade	4.84	22,800	10.91	600	-17.14	-600
Retail Trade	3.94	43,100	32.64	7,900	12.95	1,800
General Merchandise Stores	22.30	47,600	46.00	2,300	38.71	1,200
Transportation, Warehousing, and Utilities	4.04	16,300	46.81	2,200	4.88	200
Information	-31.50	-87,100	42.86	600	33.33	500
Financial Activities	10.38	59,300	24.59	1,500	16.28	700
Professional and Business Services	14.50	162,500	47.83	4,400	31.75	2,000
Educational and Health Services	38.25	381,000	130.04	31,600	61.03	11,900
Leisure and Hospitality	23.71	199,000	37.06	5,300	-0.83	-100
Other Services	5.21	18,300	38.10	1,600	23.53	800
Government	19.63	289,600	36.27	13,600	21.46	5,000
Federal Government	10.02	19,300	10.34	300	16.67	400
State Government	12.09	38,000	37.50	1,800	0.00	0
Local Government	23.99	232,300	38.59	11,500	26.90	4,600

Source: Texas Workforce Commission

Vocational Technical Institute (McAllen) and San Antonio College of Medicine & Dental Assistants (McAllen).

Other workforce-related entities facilitating technical training and employment include Workforce Solutions, Workforce Solutions Cameron, the South Texas Manufacturing Alliance and the University of Texas-Pan American Rapid Response Manufacturing Center.

The University Articulation & Career Center, a 38,000-square-foot instructional facility, is under development in Harlingen. Through the center, any four-year university may offer bachelor's, master's and doctoral degrees at Texas State Technical College (TSTC).

"Twenty-eight public and private universities from around the country are looking into the program," says Martin. "The institutions will have the option to instruct students face-to-face in the classroom, through distance learning or via online courses."

Alternative energy is another educational focus. TSTC offers an alternative energy wind and solar program. UT Brownsville's International Technology Education and Commerce Center provides incubator space and research and development facilities to Photon8 Inc., an algae-to-biodiesel start-up company based in New Jersey.

Photon8 scientists are working together with UT Brownsville chemistry, environmental science and molecular biology students and professors. The project represents the university's latest promotion of regional economic development through research collaborations with private companies, particularly in the renewable energy area.

Challenges Remain

The Rio Grande Valley still faces challenges. The region has not escaped the recent economic downturn.

"Industrial rents on both sides of the border have probably declined an average of 15 to 20 percent through this down cycle," says Alex.

Numbers reported by Josh Aguilar of Grubb & Ellis for the McAllen market are a bit worse. "Our mid-year 2010 numbers show a decline in industrial rents from a peak of \$0.36 per square foot per month in 2007 to about \$0.27 today," says Aguilar. "No industrial space was delivered in any of our submarkets during the first months of 2010."

Still, Alex is upbeat about the future.

"This region will do well. But I would like to see more entrepreneurial spirit in the future. I want to see young people take a leadership role in this community, to take the risks to make the area really prosper." ➔

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THE TAKEAWAY

In the wake of China's world dominance in manufacturing, the Rio Grande Valley is rebranding itself as Rio South Texas. The bi-national region boasts a population of 3.5 million with a strong manufacturing infrastructure. The hope is that the area will emerge as a powerhouse transportation-workforce corridor for the 21st century.



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