

MIDP and future support for the Automotive Sector

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Performance overview since 1995

The South African automotive industry has been through a major process of adjustment since the introduction of the Motor Industry Development Programme in 1995. After decades of extremely high protection levels, tariffs have been significantly reduced, and as a result the industry has become more competitive and export oriented. These achievements are due to the predictable policy environment created by the MIDP and the response of manufacturers as evidenced by their investment decisions and productivity improvements.

The industry is structured on a more efficient basis and has achieved:

1. Greater economies of scale with four vehicle models presently being manufactured in volumes greater than 40,000 units per annum. Nevertheless, the industry still operates significantly below world scale.
1. Significant improvements in productivity and manufacturing benchmarks. Investment has increased but remains at levels below that being achieved in the more dynamic emerging producer countries. However, local content remains low - often below 50% - resulting in high logistics costs for the industry.

Sustained growth in both domestic and international markets represents a major growth opportunity for the sector and for the national economy as a whole. This is recognised in the Government's National Industrial Policy Framework, where the automotive industry is identified as a key growth sector. Government has consequently set the objective of increasing production to 1.2 million units by 2020, whilst at the same time significantly increasing local content.

Further growth and development of the automotive industry will depend on a much stronger interaction between Government policy and industry commitment. Consistent with its approach since 1995, Government appreciates the importance of a clear and consistent policy framework within which firms can make investment decisions. The industry will be expected to show significant additional efforts regarding:

1. Further investments in modern technologies and skills development,
1. Attainment of higher economies of scale in production,
1. Consumer care, and
1. Transformation in line with relevant empowerment legislation.

In 2005 **the dti** initiated a review of the MIDP in order to assess its impact and recommend options to deal with identified gaps, whilst also ensuring that support to industry is consistent with South Africa's multilateral obligations, as well as domestic priorities. Whilst the proposals forwarded by the consultants made a useful contribution to the review, it was felt necessary to extend the analysis of alternative options going forward.

The objective of this statement is to provide policy clarity over the short to medium

term and also to signal the longer term direction of automotive strategy. More detail will be provided by August 2008 on completion of the current review process.

Strategic direction

The architecture of Government strategy for the future development of the automotive industry will be underpinned by the following principles:

The level of support

Mindful of the achievements of the MIDP and the cost of support to the automotive industry, and in light of additional performance targets the industry must achieve, including lower vehicle prices, government will maintain reasonable support for the industry in a future programme.

The specific level of support will be determined on the basis of a cost-benefit analysis and will be announced upon the finalisation of the details of a new programme in August 2008.

Over the longer term, it is also important to recognise that the growth of the regional and domestic market, coupled with enhanced firm-level productivity and broader infrastructural improvements in the South African economy, should ensure that the industry becomes competitive and gradually less dependent on government support.

A more neutral incentive structure

Prior to the introduction of the MIDP, industry growth was directly linked to the expansion of the domestic market. With the introduction of the MIDP, exports became the major growth area. It is appropriate that policy now adopt a more neutral approach supporting the balanced expansion of production for both export and domestic markets.

Achieving high volumes and economies of scale

Economies of scale are very important in the automotive industry. Higher model production volumes make it possible to achieve higher local content on an economic basis. Gains have already been made in this regard over the last decade and government would like to see further substantial progress in this direction. Model production volumes of at least 50 000 units per platform should be the target for firms by 2012 to 2015, in line with the vision of attaining volumes of about 1.2 million by 2020. A return to low volume plants and the proliferation of low volume models is not encouraged.

Promote an integrated value chain

Priority should be given to strengthening the value chain leading into South African based vehicle producers. This means increasing local content in South African assembled vehicles. It also means that the relatively high levels of export assistance to certain categories of component exports should be carefully assessed. The vehicle producers themselves see this as an essential prerequisite to establishing a more sustainable productive base. Progress to date has been mixed, although high volume vehicle projects have brought clear advantages.

MIDP support during the transition to a future programme

Given this context, the MIDP's existing architecture, as determined in the 2002-2003 review will continue with gradual phasing down of support until the introduction of the new replacement programme as per the following parameters set out in the 2003 MIDP review:

1. The continued phase down of tariffs to 25% for CBU imports and 20% for CKD components to 2012, with annual reductions of 1%.
1. The continued reduction of the eligible export value of exports for import credit purposes by 4% per annum to 2009 and then the stabilisation of this benefit at 70%.
1. The maintenance of the Duty Free Allowance for vehicle assemblers at 27% to 2012
1. The maintenance of the Productive Asset Allowance (PAA) in its existing format - until further notice.

The new programme

The MIDP is legislated until the end of 2009. A new support programme for the motor industry aimed at improving the domestic value chain will be introduced to last until 2020. The new programme will focus on value addition whilst being consistent with South Africa's multilateral obligations. It is likely to take the form of a subsidy to production. The programme will also include a robust monitoring and evaluation structure.

The design of the new support programme will result in further job creation and the long-term sustainability of the industry, emphasizing the attainment of internationally competitive economies of scale in production. Government intends to support production platforms/investment plans that intend to reach a minimum volume of output per platform of 50,000 units per year within a reasonable period of time.

The medium and heavy vehicle sector has been extensively liberalised. It is not envisaged that large scale support to this sector will be reintroduced although further investigation may be warranted.

The specific parameters of the future MIDP are presently being developed by an Inter-Departmental Task Team, comprising senior officials in the Department of Trade and Industry as well as National Treasury officials, with support from independent experts. Recommendations from this work will be decided upon at the political level within Government.

Extensive consultations have already taken place with the industry. From early 2008, this will take place on a more formal basis through the creation of an appropriate forum in which all stakeholders will be represented with a view to finalisation of the technical parameters of the new programme. This forum will work within tight guidelines established by **the dti**.