A critique of the MIDP as a post-apartheid policy instrument

R. VILJOEN

12888389

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Study Leader: Prof Ronnie Lotriet

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Abstract

The motor industry is one of the leading industries in the South African economy. The MIDP, an import/export complementary arrangement, was introduced to help reintegrate the motor industry into the global economy. The aim was to improve the international competitiveness of companies in the industry; enhance the industry's growth through exporting; improve vehicle affordability; improve the industry's highly skewed trade balance; and stabilise employment levels, but succeeded in having the unintended consequence of growing vehicle imports.

In this study a literature review is done on studies that were done on governments' policy and the South African motor industry and an empirical study done on a critique of the MIDP as a post-apartheid policy instrument. Of the approximate 500 component manufacturers; only 32 manufacturers participated in this study. South Africa may not have a motor industry in seven to ten years if urgent attention is not paid to increasing local content, gaining certainty on government's support programme for the industry and improving South Africa's cost competitiveness.

Imports have grown rapidly and the industry has still not achieved a sufficient volume of production to realise full economies of scale. Another constraint is South Africa's location, remote from major automotive markets. After a long period of heavy protection followed by liberalisation and export support, it is now time for the industry to move towards a balanced growth path on the basis of policies which impose a more neutral incentive structure. This would involve some ongoing protection and assistance for production at low to moderate levels. Under such a scenario, both the domestic market and exports could provide the basis for sustained future growth.

Key words: Motor; Industry; Development; Programme; Automotive; Production; Original; Equipment; Manufacturers

Opsomming

Die motorvervaardigingbedryf is een van Suid-Afrika se vernaamste ekonomiese bedrywe. Die MIDP, 'n invoer/uitvoer-ondersteunende program, is geïmplementeer om die motorbedryf aan te spoor om die wêreldekonomie te betree. Die doel was om internationale meedinging van maatskappye in die bedryf te verbeter; om die bedryf se uitvoere te verbeter; asook voertuie bekostigbaar te maak d.m.v. ondersteuning; 'n bydra te maak tot 'n gunstige betalingsbalans; en om by te dra tot stabiele indiensnemingsvlakke. Nieteenstaande alle pogings het dit bygedra tot hoër invoere van voertuie.

Hierdie literatuur studie ondersoek vorige studies rakend die regering se beleid en die Suid-Afrikaanse motorbedryf. 'n Empiriese studie is gedoen oor die kritiek op die MIDP as 'n post-apartheid beleidinstrument. Net 32 van die ongeveer 500 onderdele vervaardigers het aan die steekproef deelgeneem. Die moontlikheid bestaan dat Suid-Afrika oor 7 tot 10 jaar nie meer motorvervaardigers sal besit as daar nie drasties iets gedoen word om plaaslike inhoud te bevorder nie (Beeld, 2009). Sekerheid oor die regering se ondersteuningsprogram en verbetering in Suid-Afrika se vervaardigingskostes, om meer kompeterend te wees, is ook nodig.

Invoere het drasties gegroei en die bedryf het nog nie volume of produksie-vlakke bereik om ekonomie van skaal te bereik nie. Nog 'n beperking is Suid-Afrika se geografiese ligging, verwyder van vername markte. Na 'n lang periode van beskerming, gevolg deur liberalisering en uitvoerondersteuning, het dit tyd geword vir die bedryf om na 'n gebalanseerde groei, in samewerking met 'n neutrale beleidsvoordeelstruktuur te beweeg. Dit benodig voortgesette ondersteuning ter beskerming en produksie teen lae koste. Onder die voorwaardes kan die plaaslike mark en uitvoere 'n basis van toekomstige groei verseker.

Sleutel woorde: Motor; Industry; Development; Programme; Automotive; Production; Original; Equipment; Manufacturers

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Abbreviations

APDP	Automotive Production Development Program
DFA	Duty-free Allowance
FDI	Foreign Direct Investment
IRCC	Import Rebate Credit Certificates
MIDP	Motor Industry Development Program
NAACAM	National Association of Automotive Component and Allied Manufacturing
NAAMSA	National Association of Automobile Manufactures of South Africa
OEM	Original Equipment Manufacturers
SA	South Africa
UNIDO	United Nations Industrial Development Organisation
PAA	Productive Asset Allowance

Chapter 1 : Nature and Scope of the Study

1.1 Background

The Motor Industry Development Programme (MIDP) was introduced in 1995 to assist companies in South Africa (SA) to be competitive in the international motor industry. One of the biggest criticisms levelled against the industry's government support programme has always been its encouragement of exports, but having the unintended consequence of growing vehicle imports. In 2005 and 2006, the industry's trade deficit was just under R30-billion, for example. This was as a result of a combination of higher import prices and higher import volumes. (SARB, 2006:24) In simple terms, the MIDP is an import/export complementary arrangement, whereby the local content value of components or built-up vehicles exported, earn credits which can be used to rebate import duties on components and vehicles. This means several vehicle manufacturers use their credits to import models, not manufactured locally, from their parent companies. South Africans' growing enthusiasm for new cars – persisting until 2007 when the consumer boom started to decline – has also seen a growing number of vehicles being imported over the last few years, with vehicle manufacturers from China and India seeking new markets again contributing to the trade deficit. In contrast to booming imports, vehicle exports from South Africa have been more sluggish in gaining ground – until 2008. The MIDP was the subject of a review in August 2008, and is set to be replaced by a more production-based support mechanism after 2012. (Venter, 2008)

1.2 Problem Statement

Development must be seen as taking the industry out of its current situation and setting it on a path of self-sustaining growth. Exports are viewed as generating greater growth of productivity as a result of:

- Greater capacity utilisation;

- Greater horizontal specialisation as firms concentrate on a narrower range of products;
- Increasing familiarity with new technologies;
- Greater learning-by-doing; and
- The stimulating effect of the need to achieve greater internationally acceptable quality standards.

The rapid growth in aggregate exports has resulted in rapid growth in manufacturing's share of value. It is therefore reasonable to assume that effective organisations would pursue economic policies, which would help them to create value for all stakeholders.

Economic growth, in turn, leads to higher profitability. Exports contribute to economic growth as the export sector is not only more productive than the non-export sector, but it also generates some external effects that enhance the productivity of the non-export sector. Export expansion results in better resource allocation, which, in turn, leads to increased productivity

The beneficial effect of foreign direct investment is stronger in countries that pursue an outwardly-orientated trade policy than those that adopt an inwardly-orientated policy. A country pursuing an export promotion strategy is likely to attract a higher volume of Foreign Direct Investment (FDI) and to promote more efficient utilisation thereof than an import substitution strategy.
The research proposal is therefore aimed at looking at the MIDP as mechanism for:

- Contributing to an increase in levels of employment and skills development;
- Contributing to profitability of the motor industry;
- Contributing to an increase in foreign direct investment; and
- Contributing to productivity improvement of the motor industry

1.3 Objectives

1.3.1. The Primary Objective:

The primary objective of this study is to critically evaluate the MIDP as an instrument of trade to enhance the competitiveness of the SA motor industry.

1.3.2. Secondary-Objectives

The secondary-objective of this study is to:

- Investigate Government policy and the motor industry
- Investigate the domestic motor industry as an exporter.

1.4 Research Methodology

1.4.1. Literature Study

This study was based on a comprehensive study of literature relevant to the objectives posed above, with the aim to gather vital information regarding the MIDP, in order to determine the success as a post apartheid policy instrument. Relevant information was gathered from various publications such as textbooks, journals and computer-based searches on databases such as EBSCO-host, Emerald and the Ferdinand Postma library's various other databases.

1.4.2. Empirical study

Quantitative information was gathered by using a questionnaire, which was e-mailed to managers, owners or the person responsible for MIDP. Due to geographical location it is impossible to visit the majority of manufacturers that are mostly located in the Eastern Cape.

1.5 Scope of the Study

The scope of the literature research in Chapters 2 and 3 covers the broad spectrum of the motor industry value chain in order to provide an understanding of how the decisions of government impact on the global motor industry environment and specifically the SA motor industry. A value chain describes the links in the chain of production of a product or service. Usually the value chain involves backward linkages in the supply of inputs from the lower tier suppliers to the first tier suppliers to the Original Equipment Manufacturers (OEM). These chain linkages are not only important upstream but also downstream. The SA motor industry will be analysed in more detail in Chapter 2.

The scope of the empirical research involves an empirical survey of the companies affected by the MIDP. The survey sample includes OEMs and component manufacturers. The research design and methodology will be discussed in more detail in Chapter 4.

1.6 Limitations of the study

The statistical analysis in this study is limited to SA manufacturers. The information was gathered mainly by electronic distribution of a questionnaire and is solely dependant on participants' willingness, time and resources to complete the questionnaire. The geographical location of participants made it impossible to arrange personal interviews. Phone calls were made to participants to encourage participation in questionnaire. Due to costs and time restrictions an in-depth study of the industry could not be done.

1.7 Layout of the study

Chapter 1: Nature and scope of the study

The introductory chapter 1 encapsulates the research problem, objectives, research methodology, scope, limitation, layout and terminology of the study.

Chapter 2: Government Policy and the Motor Industry

The second chapter of this study takes a look at the rationale for the MIDP, an overview of government policy, the functioning of the MIDP and the APDP.

Chapter 3: The South African Motor Industry

The third chapter takes a look at the industry's vision and mission, performance in the apartheid era, performance in the post apartheid, view to 2012 and industry expectations after 2012.

Chapter 4: Empirical Study
Chapter 5: Conclusion and recommendation
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1.8 Terminology

Passenger cars are motor vehicles, with at least four wheels and no more than eight seats, driver included, used for transporting persons.

Light commercial vehicles are motor vehicles, with at least four wheels, used for transporting of goods. Gross vehicle weight (GVW - in metric tons) is used as a limit between light commercial vehicles and heavy trucks. This limit depends on national and professional definitions, and varies between 3.5 and 7 tons. Minibuses, derived from light commercial vehicles, enter this category. They are used for transporting persons, have more than eight seats, driver excluded, and their GVW is below this limit.

Light vehicles include passenger cars and light commercial vehicles.

Heavy trucks are vehicles intended for transporting goods. Their GVW is over 7 tons. They include tractors designed for towing semi-trailers.
Buses and coaches are used for transporting persons, have more than eight seats, driver excluded, and a GVW in excess of above limit.

Commercial vehicles include light commercial vehicles, heavy trucks, coaches and buses.

Chapter 2 : Government Policy and the Motor Industry

2.1 Introduction

According to Flatters (2005) the Motor Industry Development Programme (MIDP) is widely regarded as a major success of South Africa's post-apartheid trade and industrial policies. Government identified the motor industry as one of the leading industries in the economy, and wanted to deepen local manufacturing in it. The programme has been modified and/or extended several times, since its introduction in 1995, and is scheduled to continue until 2012. A Department of Trade and Industry (DTI) funded review is in progress and is considering further adjustments to and possible extensions of the programme after 2012. At the same time high-level discussions are under way in several ministries and agencies about future industrial policy strategies for South Africa. While most popular discussions focus on MIDP successes, concerns have been raised about some of its unintended impacts.

Following complaints about the failure of prices to respond, as expected, to the appreciation of the Rand, the Competition Commission has conducted an investigation of domestic motor vehicle pricing. The Commission has pointed to the possible role of the MIDP in restricting consumer choice and maintaining prices at higher levels than in other markets. The motor industry, supported by a recent study by industry specialists, has disputed these claims. Despite its importance there has been surprisingly little analysis of MIDP economic benefits and costs. Black (2001) and Black and Mitchell (2003) did a historical analysis of the programme and discussed some of its economic impacts. Based on a more thorough economic analysis, a few recent papers have taken a more critical view of the programme.

The failure of policy makers to appreciate the costs of such an important programme raises serious questions about the government's capacity to design and manage industry specific policies, and about the transparency and accountability of processes for monitoring and reviewing them. The design of industrial policy requires knowledge of what is happening "on the ground" and this requires informed communication with stakeholders in the private sector. But to make and manage policies in the broader national interest, policy makers need the capacity and the independence to filter, expand and analyse the information so obtained. Otherwise policy-making processes are prone to being captured by vested interests.

2.2 The Rationale for MIDP

In order to help the motor industry adjust to South Africa's reintegration into the global economy the MIDP was introduced in 1995. Prior to 1995 the industry was protected by tariffs in excess of 100 percent and unworkable local content requirements. Unsurprisingly it produced a very wide range of products at low scales of output and at high cost. It was a very inefficient import substitution sector that could not have competed either domestically or internationally in the face of immediate trade liberalisation. The MIDP was designed to help the industry adjust and increase its competitiveness in the new post-apartheid trade policy environment. The programme comprised four principal elements (Black & Mitchell, 2002):

- Reduced import tariffs on light vehicles and components.
- Removal of local content requirements;
- Duty-free import of components up to 27 percent of the wholesale value of the vehicle;
- Duty rebate credits to be earned on exports of vehicles and components and used for duty-free import of vehicles and components.

The incentives in respect of components apply only to those sold directly to OEM manufacturers. This excludes from the programme after-market components, an industry in which South Africa might have some regional and maybe even global comparative advantage. The aim of the programme was to provide incentives to rationalise production into a smaller range of products and achieve economies of scale through exporting them. All other products would be imported.

The MIDP has been reviewed and extended twice. It is scheduled to continue until 2012. It has been expanded to include a direct investment subsidy in the form of a Productive Asset Allowance (PAA) that provides import duty credits equal to 20 percent of the value of qualifying investments, spread equally over five years and may only be used to rebate duties on imported light motor vehicles. The main purpose of this allowance is to encourage model rationalisation: the assemblers are encouraged to produce less models at increased volumes and import low volume models instead using the duty credit certificates that they may get based on productive assets they invest in. Some assets may not be considered as qualifying for this purpose, e.g. delivery vehicles; however the final decision rests with an evaluation committee of the DTI. The industry benefits from a wide variety of other initiatives by national, provincial and domestic governments as well. These ranges from restrictions on imports of used vehicles to provision of infrastructure, factory facilities and special financial arrangements (Flatters, 2005).

2.2.1. The MIDP objectives

The MIDP involves a gradual reduction in assistance up to the year 2012. Government's role is to set a clear policy agenda , maintain good communication with the motor industry, provide efficient administration of the MIDP, monitor developments closely and provide support for initiatives in respect of technology, productivity upgrading and new investments, which could increase employment and/or the competitiveness of the industry.

The MIDP was aimed at the development of an internationally more competitive and growing motor industry, which would be able to (DTI, 2003):

- Provide high quality and affordable vehicles and components to the domestic and international markets;
- Provide sustainable employment through increased production;
- Make a greater contribution to the economic growth of the country by increasing production and achieving an improved industrial trade balance.

These national objectives were to be achieved by:

- Encouraging a phased integration into the global motor industry;
- Increasing the volumes and the scale of production by expanding exports and gradually rationalising models produced domestically;
- Encouraging the modernisation and upgrading of the motor industry in order to promote higher productivity and facilitate the global integration process.

The major policy instruments to achieve these objectives have been the following:

- A gradual and continuous reduction in tariff protection in so far as to expose the industry to greater international competition;
- The encouragement of higher volumes and a greater degree of specialisation by allowing exporting firms to earn rebates on vehicle import duties;

The introduction of a range of incentives designed to upgrade the capacity of the industry in all spheres.

2.3 Overview of Government policy

The MIDP succeeded the local content programs in 1995 and heralded a marked shift in vision and aims. Its new objectives were to improve the international competitiveness of firms in the industry; enhance the industry's growth through exporting; improve vehicle affordability; improve the industry's highly skewed trade balance; and stabilise employment levels. In order to achieve these aims a series of mutually reinforcing export-orientated incentives were introduced, coupled with a reduction in import tariffs between 1995 and 2002. These export incentives had a number of key elements (Barnes et al., 2004):

- A PAA was introduced after the 1999 review of MIDP, providing duty credits equivalent to 20 percent of the investments, spread out over a period of five years. However, this only applied to investments which were designed for exports and which enhanced scales of a particular product line.
- Introducing an import/export complementation (IEC) scheme and abolishing a minimum content provision allowed both vehicle and component manufacturers to earn duty credits from exporting. These duty credits were tradable and could be used to offset import duties on cars, components or materials. It, thus, allowed assemblers to buy credits from component exporters to finance the import of completely assembled vehicles, which aren't produced locally, or components which they preferred to source from overseas.
- There was a small vehicle incentive (SVI), which provided a subsidy for the manufacturing of more affordable vehicles. The incentive operated via a duty drawback mechanism, with the value of the drawback linked to the value of the vehicle; it was withdrawn in 2001 as it was perceived to have a limited impact on making vehicles more affordable to the poor.
- A tariff phase down schedule was designed to reduce nominal rates of protection to 38 percent for completely built-up units (CBU) and 29 percent for completely knocked down (CKD) components by 2003 (Table 2.1).

- There was a duty-free allowance (DFA) for assemblers of 27 percent of the wholesale value of the vehicle (Table 2.1).

Table 2.1: Main parameters of MIDP incentives, 1995 - 2012

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
MIDP Tarrif Rates (%)																		
Cars	65	61	57.5	54	50.5	47	43.5	40	38	36	34	32	30	29	28	27	26	25
Parts	49	46	43	40	37.5	35	32.5	30	29	28	27	26	25	24	23	22	21	20
Ratios of exports to imports																		
Car Exports / Car Imports	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
Car Exports / Part Imports	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
Parts Exports / Car imports	0.95	0.9	0.85	0.8	0.75	0.7	0.7	0.65	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Parts Exports / Part imports	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
Deemed Value of Exports	1	1	1	1	1	1	1	1	0.94	0.9	0.86	0.82	0.78	0.74	0.7	0.7	0.7	0.7
Converters:																		
Qualifying PGM Content	1	1	1	1	0.9	0.8	0.6	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
IRCC Values (%)																		
Car Exports / Car Imports	65	61	57.5	54	50.5	47	43.5	40	35.7	32.4	29.2	26.2	23.4	21.5	19.6	18.9	18.2	17.5
Car Exports / Part Imports	49	46	43	40	37.5	35	32.5	30	27.3	25.2	23.2	21.3	19.5	17.8	16.1	15.4	14.7	14
Parts Exports / Car imports	61.8	54.9	48.9	43.2	37.9	32.9	30.5	26	21.4	19.4	17.5	15.7	14	12.9	11.8	11.3	10.9	10.5
Parts Exports / Part imports	49	46	43	40	37.5	35	32.5	30	27.3	25.2	23.2	21.3	19.5	17.8	16.1	15.4	14.7	14
Catalytic Converters																		
Parts Exports / Car imports	61.8	54.9	48.9	43.2	34.1	26.3	18.3	13	9.1	8.6	8.2	7.7	7.2	7	6.7	6.5	6.2	6
Parts Exports / Part imports	49	46	43	40	33.8	28	19.5	15	11.6	11.2	10.8	10.4	10	9.6	9.2	8.8	8.4	8
DFA (%)	27	27	27	27	27	27	27	27	27	27	27	27	27	27	27	27	27	27

(Source: Flatters, 2005)

The MIDP is effectively an extension of the previous industry policy in terms of export facilitation; namely, the import/export complementation scheme where export credits could be used to offset import duties, thus effectively attempting to reduce the industry's import duty liability. The MIDP is based on Australia's Button Car Plan, with particular reference to tariff transformation and export facilitation. Local content requirements were abolished under the MIDP from September 1995 (Damoense & Simon, 2004).

Other features that are lacking from Phase VI but incorporated under the MIDP include: a tariff phase-down programme for CBUs and components, and government support schemes, DFA and the SVI. The economic research regarding motor industry specific programmes adopted by many low volume vehicle producing economies, such as Argentina, Australia, Malaysia, the Philippines and others indicate that the above-mentioned measures, or similar ones, are common features of automotive programmes.

The collective government policy measures of the MIDP have increased the effective protection of the South African motor industry in the face of increased tariff emancipation imposing damaging costs on the development and growth of the industry. Incentives provided under the MIDP are estimated to cost the domestic industry in the region of R11 billion per annum.

2.4 The functioning of the MIDP

The MIDP creates substantial incentives that help the motor industry to invest in the latest technology and to help production for export and for the domestic market. The domestic market manufacturers benefit from tariff protection against imports and from the DFA, which offsets the cost-raising effect of import duties on components. Consumers pay for this through price levels that are higher than they would be in the absence of the import duty on vehicles. As a consequence, the National Treasury pays by foregoing customs duties on components. Manufactures producing vehicles or components for export qualify for duty drawbacks on all imported components and also receive Import Rebate Credit Certificates (IRCC) in proportion to their exports. These allow them to import vehicles and/or components duty-free and sell them domestically at the duty-inclusive price. The value of the IRCC depends on the price mark-up permitted by the tariff. Without this price mark-up the principal MIDP incentive would be of no value to vehicle and components exporters. It might be argued that the MIDP creates a duty-free environment for SA consumers, that is, importers pass all the duty savings from their use of IRCC to domestic buyers and that consumers, in effect, face world prices for vehicles in the SA market. A corollary of this view would be that the MIDP does not provide subsidies to vehicle and components producers in South Africa. This would contradict basic principles of economics as well as the facts in South Africa. As long as some vehicle importers are paying import duty (and many are), market dynamics will ensure that the domestic price reflects the duty-inclusive cost of importing. Sellers would be foolish to sell at a duty-free price as long as some have to pay duty, and if they did, no one would buy from the sellers who were subject to duty.

Evidence from the South African motor vehicle market confirms that consumers are paying at least a duty-inclusive price.

- Vehicle sellers often pay 80 to 90 percent of the face value of import rebate credit certificates and have been complaining recently about shortages of IRCC in the market. Sellers wouldn't pay such a high price for these certificates if they had to compete with vehicles being sold at a duty-free price.
- Vehicle producers have been unanimous in their chorus of announcements and press releases, in the Engineering News for example, about the necessity for a continuation of MIDP to induce them to continue to produce in South Africa after 2012. This would appear to

contradict the claim that the MIDP incentives are of no value to them, as would be the case if duty savings were being passed on to consumers.

- Discussions of market pricing with South African vehicle sellers suggest that 2008/2009 prices are higher, not lower, than the duty-inclusive price. According to the sellers domestic prices can be thought of roughly as the sum of the cost of importing, all import duties and taxes, all domestic distribution and sales costs, including a normal return to all capital invested, plus another 10 percent, making South Africa one of the most profitable vehicle markets in the world at the moment.

2.5 The Automotive Production Development Programme (APDP)

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. A process of extensive research and consultation resulted in a report being submitted to the DTI at the end of 2006. After intense evaluation of the report and recommendations therein, it was felt necessary to extend the analysis of industry dynamics and alternative support options going forward. It should be noted that part of the recommendations was for the introduction of a production allowance to replace the current export incentive in line with the country's multilateral obligations, however the design and development of such an allowance was not done.

A task team involving the DTI and National Treasury with the assistance of independent experts has, from the end of 2007, worked on designing a new architecture for industry support in line with the new targets being set for the industry. Substantial research, followed by intensive and comprehensive industry consultations took place. The United Nations Industrial Development Organisation (UNIDO) and Automotive Industrial Development Corporation (IDC) provided valuable information and assistance in respect of global industrial policy trends and economic modelling respectively. The final proposals were arrived at after several interactions with industry stakeholders at various levels, culminating in a consideration by Cabinet.

The motor industry is the largest and leading manufacturing industry in the domestic economy. Since the introduction of the MIDP the industry has rationalised and restructured into a more efficient basis achieving significant growth in production volumes, exports and investments whilst maintaining significant employment levels.

The industry generates strong linkages with other

- Input industries such as aluminium, chemicals, electronics, leather & textiles, plastics, steel, machinery and equipment,
- Service industries such as engineering, logistics, tooling,
- Industries such as financial, wholesale & retail, advertising.

The Motor Industry continues to be a highly competitive global industry where almost all countries hosting a motor industry provide substantial support. The industry is also facing one of the worst times globally as vehicle growth slows down and the consumer demand shifts to more fuel efficient vehicles in response to the oil price and environmental concerns. There is now increased competition from low cost and market booming regions such as eastern Europe and Asia with a continuing overcapacity problem that puts added pressure to the SA industry that barely produces and sells 1 percent of the vehicles in the global vehicle market.

The revised MIDP would therefore seek to provide industry with a reasonable level of support in a market neutral manner (that is, it cannot be an export incentive anymore as this might be inconsistent with WTO, therefore there will be no discrimination for products either sold domestically or exported).

Government is thus now looking at further development of the motor industry in line with the National Industrial Policy Framework (NIPF) and 2007/8 Industrial Policy Action Plan (IPAP). Long-term development of the industry will be achieved by doubling production to 1.2 million vehicles by 2020 with associated deepening of the domestic components industry.

The revised programme will have the following four key elements;

- Tariffs: Stable, moderate tariffs will remain at 25 percent for light motor vehicles and 20 percent for components from 2012. These tariffs are meant to provide just enough protection to justify continued domestic vehicle assembly.
- Domestic Assembly Allowance: This support will be in the form of duty credits issued to vehicle assemblers based on 20 – 18 percent of the value of light motor vehicles produced domestically from 2013. This support effectively provides a lower duty rate for domestic assemblers and should provide enough encouragement for high volume vehicle production in line with the target of doubling production.
- Production Incentive: From 2013 this support of 55-50 percent of value added, computed in simple terms as sales less raw materials, in the form of a duty rebate credit, will replace the current export-based scheme. The value-added support will encourage increasing levels of local value addition along the motor industry value chain with positive spin-offs for employment creation.
- Automotive Investment Allowance: From 2009, this assistance will replace the current PAA and will be 20 percent of qualifying investment paid over to participants over a three-year-period. This support will be available to

encourage investments by vehicle assemblers and component manufacturers in a manner that supports equipment upgrading.

Further work is to continue in the following areas:

- Sub-industry investigation aimed at evaluating growth opportunities and appropriate support mechanisms in the Catalytic Converter and other material-intensive industry as well as Medium and Heavy Commercial Vehicles. Further announcements can be expected in due course after more detailed consultations, however, within the current financial year.
- Programmes aimed at addressing broad-based empowerment imperatives as well as challenges pertaining to firm level competitiveness, will be enhanced in partnership with relevant stakeholders.
- In partnership with key stakeholders such as DEAT, DME and industry, work aimed at responding to climate change imperatives including tighter emission standards will be given more attention.
- A strong monitoring and review system will be set to allow better information flows for decision-making as well as more frequent reviews.

Whilst Government will provide support aimed at further stimulating growth in the industry, the private sector is also expected to show progress in the areas of transformation, increasing local content and contributing to skills acquisition and or training. Industry will also be expected to achieve high volumes of production so as to benefit from such improved economies of scale.

In this current process of designing a new support mechanism it becomes important to build in measures of success, to the extent that it then becomes easier to determine the success of the support programme in the future. As the DTI set up the necessary regulatory amendments and administration system for the programme, they will ensure that it is in line with the need for a strong monitoring and evaluation system but still not unduly burdensome to stakeholders.

2.6 Summary

In summary, the MIDP works by subsidising production of vehicles and OEM components for both the domestic and export markets. The subsidies are paid for by domestic consumers of vehicles in the form of restricted choice and higher prices. The system of duty credits on exports means that consumers subsidise not only vehicles produced for the domestic market, but also those produced for export. The import duties that the Treasury foregoes in honouring export IRCC do not lower the prices paid by domestic consumers. Rather, they subsidise vehicle and components exporters while domestic buyers still pay (at least) a duty-inclusive price.

One can observe a selective industrial policy targeted at the vehicle and components industry. It has a long history, in two phases. The first phase (1961–1995) was focused almost entirely on increasing local content either by weight or by value. The second phase (post-1995) was targeted at rationalisation and the reaping of scale economies as well as net import saving, achieved through a series of export incentives built around access to duty-free imports for the domestic market. Although not directly linked to the recent vintage of functional and horizontal policies introduced after transition in 1994, this selective industrial policy was synergistically embedded in a coordinated framework in which it gained from the macroeconomic incentive regime, and drew on new horizontal policies introduced in the latter half of the 1990s (Barnes et al, 2004).

Industry will be expected to achieve high volumes of production so as to benefit from such improved economies of scale. Whereas Government will provide support aimed at further stimulating growth in the industry, the private sector is also expected to show progress in the areas of transformation, increasing local content and contributing to skills acquisition and or training.

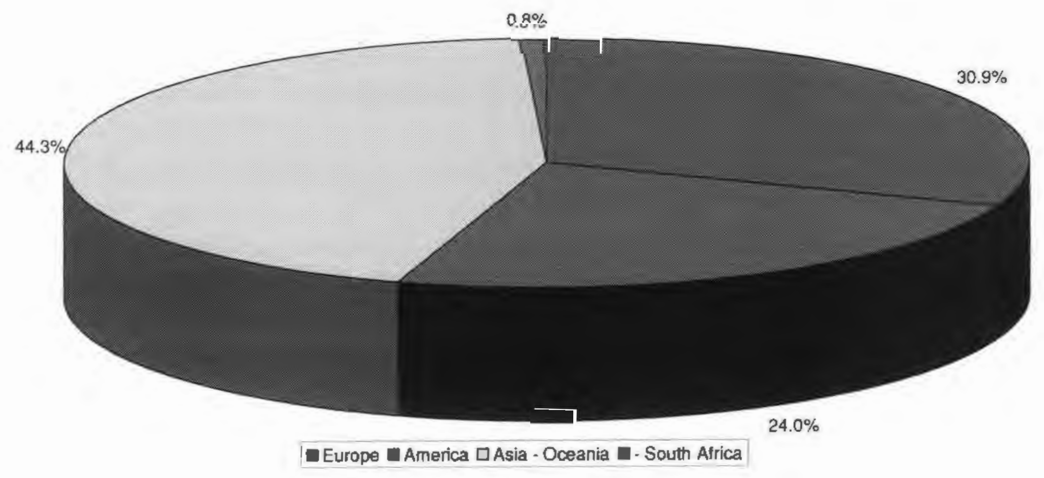
Chapter 3 : The South African Motor Industry

3.1 Introduction

The motor industry is the leading manufacturing industry in the South African economy. It is the third largest contributor to national GDP after the mining and financial sectors (Kwaggwa. 2008). In 2005, the industry accounted for 7 percent of the country's GDP and 87 percent of Africa's vehicle output.

SA represents most of the major vehicle brand manufacturers. These include Volkswagen, Toyota, BMW, DaimlerChrysler, Nissan, General Motors, Ford (incorporating Mazda, Land Rover and Volvo) and Fiat. Despite its significant role on the continent, the SA motor industry accounts for only 0.8 percent of the world's vehicle production (Figure 3.1). The industry still has a long way to go before it becomes a significant player in the global motor industry.

Figure 3.1: World Vehicle Production for 2008



(Source: NAAMSA 2008)

According to Mr. R. Pitot (2009) there are about 250 1st tier component manufacturers, who supply directly to the OEMs and about 250 makers of sub-components. The only companies that need to be registered for the MIDP, which are about 200 companies, are those who claim IRCC for their exports. The component manufacturers exported R30.5 billion in 2006 (Table 3.1).

Table 3.1: Component exports 2001 to 2006

Component category	2001	2002	2003	2004	2005	2006	% of Total 2006
Catalytic converters	8 989	9 204	8 104	8 289	9 935	15 810	51,8%
Leather components	2 391	3 184	2 899	3 113	2 693	2 549	8,4%
Tyres	781	1 379	1 278	1 285	1 183	1 220	4,0%
Engines	88	623	564	701	781	1 216	4,0%
Engine parts	520	771	843	894	1 000	984	3,2%
Silencers/exhaust pipes	282	340	327	407	492	880	2,9%
Road wheels and parts	725	955	809	753	738	681	2,2%
Car radios	115	171	332	257	268	377	1,2%
Axles	81	129	119	140	201	375	1,2%
Radiators	70	199	191	162	220	365	1,2%
Transmission shafts/cranks	149	236	263	332	553	351	1,1%
Automotive glass	241	328	307	311	359	321	1,1%
Automotive tooling	441	363	529	383	332	272	0,9%
Filters	114	184	142	164	174	218	0,7%
Wiring harnesses	391	457	427	359	258	208	0,7%
Gauges/instruments/parts	77	119	128	142	161	184	0,6%
Ignition/starting equipment	195	231	270	230	185	174	0,6%
Brake parts	118	215	198	146	120	120	0,4%
Body parts/panels	107	140	168	116	78	115	0,4%
Gear boxes	21	38	29	34	82	113	0,4%
Other components	2 690	3 617	3 342	3 515	3 464	3 970	13,0%
Total (R Millions) (FOB)	**18 586**	**22 883**	**21 269**	**21 733**	**23 277**	**30 503**	**100%**

(Source: NAAMSA 2007)

SA's track record as a manufacturer and supplier of built-up vehicles, components and after market parts has been firmly established and, in addition to vehicles, major exports comprise catalytic converters, stitched leather components and seat covers, engines and engine parts, silencers and exhausts, road wheels and parts and car radios.

3.2 Industry vision and mission

In 1995, all motor industry stakeholders formulated a common vision for the motor industry and this is used as a platform by government, business and labour to determine the future direction of the MIDP. The vision is to establish a viable, competitive industry, domestically and internationally, capable of achieving both continuous growth and sustainable employment creation (DTI, 2003:10)

The DTI export strategy for the motor industry explains the motor industry vision under the MIDP as follows (Lamprecht, 2006):

- Viable in order to be profitable, innovative, productive, efficient, rationalised and consumer-focused.
- Internationally competitive, working towards the highest global standards of quality, price, service delivery times and inventory levels.
- Continuous growth by the means of new investments from global and domestic players, skills development, increased exports and increased volumes.
- Sustainable employment.

The mission for SA motor and associated industries is to offer enhanced customer satisfaction through:

- Internationally competitive products
- Fuel efficient, environmentally friendly vehicles
- Improved quality and choice
- High quality after sales service

Secondly, to encourage a more focused and rationalised assembly and supplier industry, progressively more globally competitive with major export focus based on economies of scale production; thirdly, to promote well-developed linkages with multi-national vehicle corporations and growing participation in OEM global sourcing. Fourthly, to develop more efficient distribution networks. Fifthly, to promote employment equity and the development of Black Economic Empowerment in the broader motor industry; and lastly, to focus on Union-Employer partnership results and the achievement of substantial further improvements in productivity and the development of improved and more flexible skills.

3.3 Industry performance in the apartheid era.

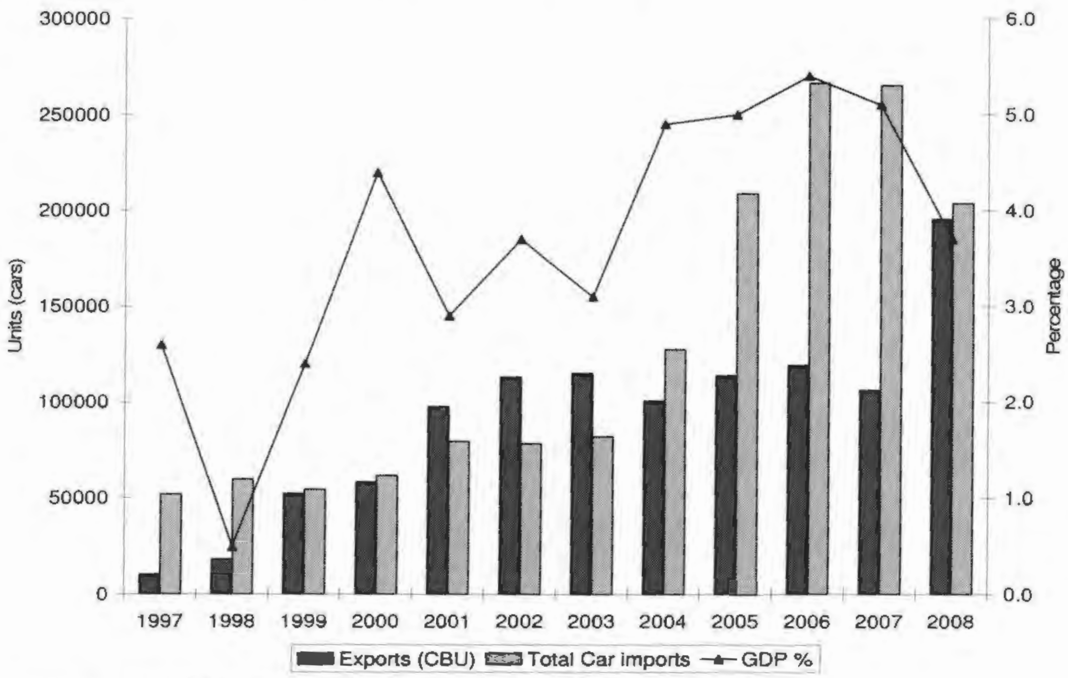
In the 1920s the first SA vehicle assembly plants were established and protected by high tariffs. The domestic motor industry thus developed mainly as an assembly industry to service the needs of the domestic market. Demand grew rapidly over the course of several decades, and the industry developed many small scale plants with high unit costs. In addition, each plant was producing a number of different models and in some cases different makes as well, contributing further to the high costs of production. The market could best be described as monopolistically competitive, as evidenced by the large number of models produced and the small scale plants with excess capacity. While profits might have been earned over operating costs, these would have been dissipated by the costs of capital and developing new models. As demand grew, new models were introduced. Thus, while the import tariff effectively prevented competition by imported vehicles, there was nonetheless a high degree of competition among domestic assemblers in the form of the introduction of new models. The relatively small scale of the domestic market led to high prices (Black & Mitchell, 2002).

The first local content programme was introduced as a result of local content being only 20 percent of domestically produced vehicles, in 1960. Net local content rose to approximately 52 percent by 1971. In 1977 the local content rose to 66 percent under Phase III of Government support system. The Phase VI local content programme, introduced in 1989, was aimed at promoting investment, improving productivity, minimising price increases and maintaining competition. This Phase marked a significant change in direction. Local content was to be measured by value rather than mass. Most importantly, local content was to be measured not just by the value of domestically produced components fitted to locally assembled vehicles but on a net foreign exchange usage basis. In other words, exports by an assembler counted as local content and enabled it to reduce actual local content in domestically produced vehicles (Black & Bhanisi, 2007).

3.4 Motor Industry performance post-apartheid

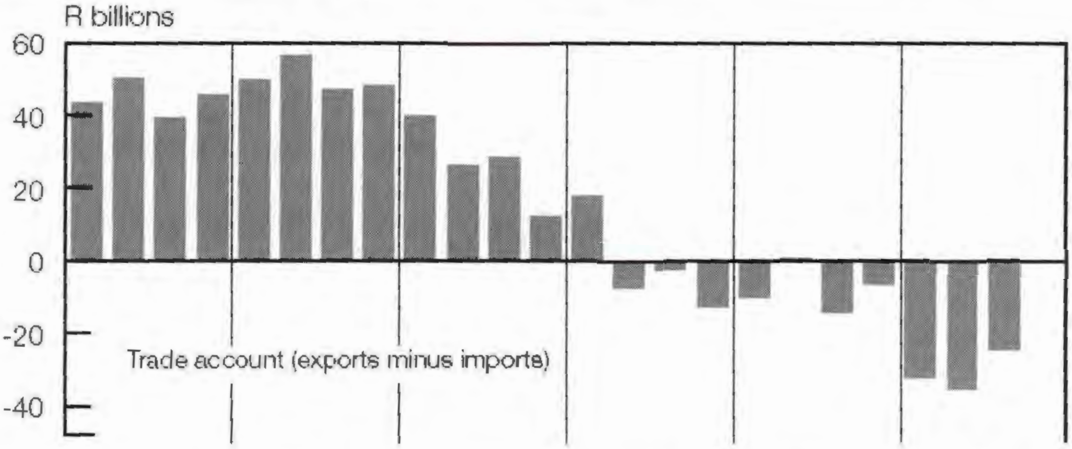
The motor industry performances since 1995 are highlighted and summarised in Figure 3.2. Vehicle exports grew from negligible amounts in 1997/98 to well over 150,000 units per year in 2008. Imports grew from about 50,000 units per year in 1997 to 250,000 in 2006. Investment in the motor industry has been substantial and has grown steadily, from less than R1 billion in 1995 to over R3.5 billion in 2004, and has exceeded R2.5 billion in every year since 2001. Components exports have grown in a similar fashion and are now in excess of R30 billion (Figure 3.3) per year. While a wide variety of products are exported, over 60 percent of the total is accounted for by just two, catalytic converters (51.8 percent of the total) and stitched leather seat covers (8.4 percent).

Figure 3.2: Vehicle Assembly in South Africa



(Source: NAACAM, 2009)

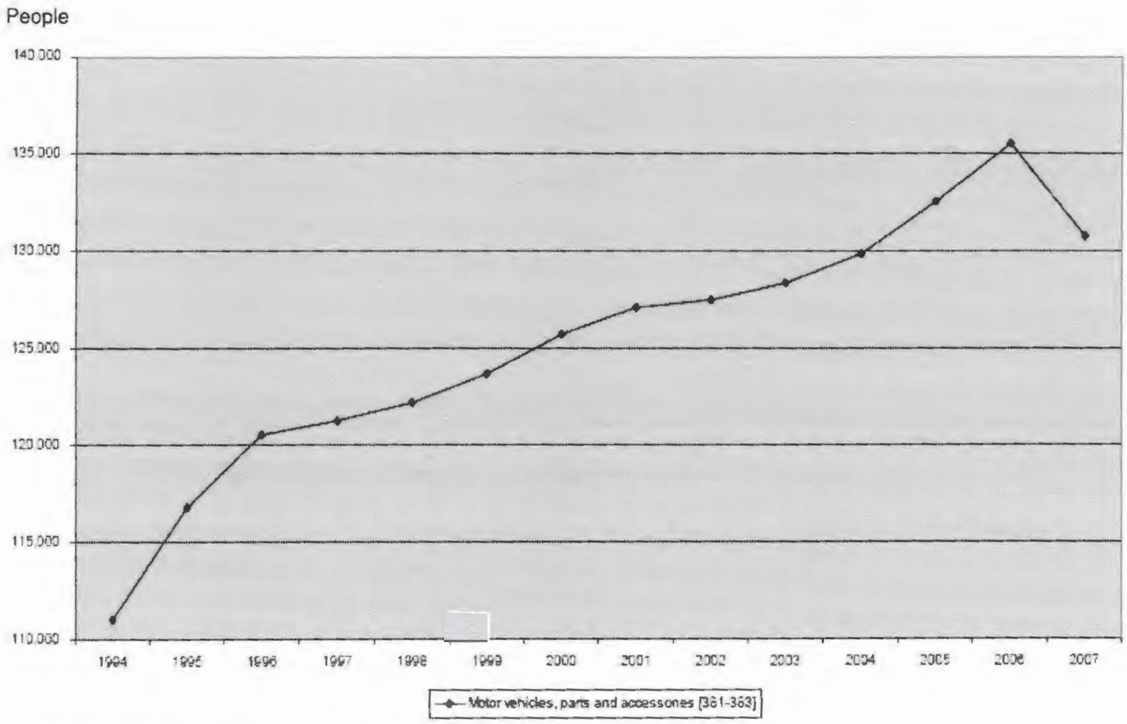
Figure 3.3: Balance of payments: Current account



(Source: Quarterly Bulletin December 2006)

Vehicle production increased from 388 442 units in 1995, to 534 490 units in 2007. Vehicle exports increased from 4 percent of production in 1995, to 32 percent in 2007. By 2007, the motor industry contributed between 1.5 percent (manufacturing) and 6.9 percent (including retail and other services) to the country's GDP. It was also responsible for 8.3 percent of the country's manufacturing value add, creating between 135 000 (manufacturing, Figure 3.4) and 450 000 (including retail and other services) jobs. By 2007 the motor industry represented 10 percent of the country's manufacturing investment, and 16 percent of total South African exports (Zalk, 2008).

Figure 3.4: Total Employment 1994 to 2007



(Source: RSA Standardised Industry Database, 2008)

International competition in the SA motor industry has increased as a result of the MIDP. Vehicle manufacturers faced the prospects of the domestic market being eroded by imports, as tariffs were reduced. The component industry, which had only begun the transition from low volume and flexible production, faced further restructuring and consolidation.

3.5 Industry view to 2012

The recession has resulted in far fewer vehicles being sold worldwide which could make multinational vehicle manufacturers rethink the volumes produced in SA. Total SA vehicle sales declined by 21 percent from 2008 to 2007, with January 2009 sales down by 35 percent, compared with January 2008. In total, last year's new vehicle sales reached 533 387 units (Table 3.2), compared to the 676 097 units recorded in 2007, and the record 714 000 vehicles achieved in 2006.

Table 3.2: Industry vehicle sales, production, export and import data: 2007 - 2011

	ACTUALS				
	2007	2008	2009	2010	2011
CARS				Projections	
Domestically Produced					
Local Sales	169 558	125 454	95 000	98 000	105 000
Exports (CBU)	106 460	195 670	130 000	145 000	160 000
Total Domestic Production	**276 018**	**321 124**	**225 000**	**243 000**	**265 000**
CBU Imports					
NAAMSA	214 873	169 610	125 000	135 000	150 000
Non-NAAMSA	50 222	34 198	27 000	30 000	32 000
Total Car Imports	**265 095**	**203 808**	**152 000**	**165 000**	**182 000**
TOTAL LOCAL CAR MARKET	**434 653**	**329 262**	**247 000**	**263 000**	**287 000**
LIGHT COMMERCIALS					
Domestically Produced					
Local Sales	156 626	118 641	80 000	90 000	100 000
Exports	64 127	87 314	55 000	65 000	75 000
Total Domestic Production	**220 753**	**205 955**	**135 000**	**155 000**	**175 000**
CBU Imports					
NAAMSA	34 592	40 647	28 000	32 000	35 000
Non-NAAMSA	13 168	10 178	9 000	12 000	15 000
Total LCV Imports	**47 760**	**50 825**	**37 000**	**44 000**	**50 000**
TOTAL LOCAL LCV MARKET	**204 386**	**169 466**	**117 000**	**134 000**	**150 000**
MEDIUM & HEAVY COMMERCIALS					
NAAMSA sales (incl. Imports)	37 069	34 659	24 000	26 000	28 000
Exports	650	1 227	1 000	1 100	1 200
TOTAL MCV/HCV MARKET	**37 069**	**34 659**	**24 000**	**26 000**	**28 000**
TOTAL AGGREGATE MARKET	**676 108**	**533 387**	**388 000**	**423 000**	**465 000**
TOTAL AGGREGATE EXPORTS	**171 237**	**284 211**	**186 000**	**211 100**	**236 200**
TOTAL DOMESTIC PRODUCTION	**534 490**	**562 965**	**385 000**	**424 500**	**469 200**
GDP GROWTH RATE	**5,1%**	**3,1%**	**- 1.5%**	**2,5%**	**3,0%**

(Source: NAAMSA, 2008)

The total employment in the automobile manufacturing industry currently amounts to about 38 700 persons whilst employment in the component manufacturing industry amounts to 81 000 employees. Total employment in the trade area, namely in the vehicle sales and vehicle maintenance and servicing field, currently amounts to about 200 000 persons. The Business Monitor International's Autos Report (Q2, 2009) states that while the run up to the 2010 FIFA World Cup should alleviate the situation; the outlook still remains meagre with a 0.3 percent contraction of the economy in 2009 with real private consumption falling by 0.7 percent and contracting actual export growth. Consumer spending will fall as unemployment rises and wage growth stagnates. On the upside, aggressive monetary easing by the SARB and the government's fiscal incentive should mitigate the effects of the recession. BMI forecast the central bank to reduce interest rates by another 350bps to 7 percent during the remainder of 2009. This will overturn much of the increase, which had been the main contributor to the collapse in the domestic vehicle market, seen in 2008.

An increase in income tax relief and social grants for individuals will ease the burden for consumers somewhat over the coming year. NAAMSA forecasts a 16 percent year on year fall in domestic sales to below 450,000 units in 2009, compared with the 533,387 new vehicles sold in 2008. However, it expects a recovery in the domestic market from late 2009 as lower interest rates and declining inflationary pressures are likely to improve the financial position of many SA consumers. BMI does not believe there will be a recovery in market conditions before 2011, despite their earlier optimism about World Cup-related sales to vehicle hire fleets. Predictions are that there will be a drop of 19.4 percent in sales to just over 430,000 units. Growth will return at a modest 5.9 percent in 2010 and at 11/13 percent annually in 2011-13 as the economy recovers and lending resumes.

A major risk factor is the value of the rand, which is pushing up the price of imported vehicles. By March 2009, the currency had fallen by 41 percent and 31 percent against the Yen and Euro, respectively, over the period of a year. Market leader Toyota SA said that it would have to raise prices by 40 percent in response just to break even, but in order to maintain its market presence it may only be able to raise prices by 10/20 percent, therefore running at a loss. Toyota had already pushed up prices by 9 percent in 2008. Other players often wait for Toyota to set out its pricing policy before making a move. In February a Honda SA executive said that vehicle prices were likely to rise by 40 percent over the next two years as a result of the rand's depreciation. Nissan SA stated that the automaker plans to maintain positive free cash flow in 2009. The vehicle producer is aiming to save cash and resources to face the global economic slowdown.

There are concerns about the Japanese currency, which has strengthened significantly against the SA rand, increasing pressure on the vehicle producers' costs. Nissan SA might also raise vehicle prices by up to 15 percent based on the market situation. The potential for price hikes could explain why low cost brands, such as China's Chery Automobile, are keen to stay in the country despite the contracting market. The company revealed that it is considering a SA production plant based on steady growth in sales. However, if low cost vehicle producers are to attempt to undercut the competition, they first need to survive. Chery's statement of intent followed the sudden withdrawal of fellow Chinese brand Geely Automobile as its domestic importer went into liquidation in January, while McCarthy Motor Holdings, Chery's SA partner, cancelled imports of the Meiya brand in December. Combined Motor Holdings has also reduced the availability of models from Nanjing Automobile. NAAMSA also forecasts a 26 percent fall in output to 415,500 units in 2009, down from the 562,965 units produced in the previous year.

BMI believes the pressure on domestic vehicle producers will continue well into 2010, with the negative impact of the economic downturn increasing throughout the year. In 2009, BMI forecast output down 30.4 percent to just over 392,000 units. Output will remain flat in H110 with capacity utilisation rates likely to remain unchanged. It will not be until H210 that growth will return to the SA motor industry and by 2013, production could easily exceed 600,000 units and reaching new highs. The main threat to this outlook is the possibility of plant closures as majors seek to cut costs and consolidate operations. The poor domestic market situation, the logistics involved in exporting vehicles from SA to key markets in Europe and Asia and exchange rate volatility are all factors that could count against the long-term viability of operations in the country. South Africa's market-led, export-oriented and, in African terms, relatively industrialised economy means that it will remain the prime focus of regional investment among motor industry majors.

3.6 The Industry after 2012 (expected)

According to Matona (2008) the economies of scale now need to be developed so as to reduce production costs and to deepen the component industry. These are the two main pillars of the new support instrument and this also implies greater levels of investment by the industry, skills development, and a stronger emphasis on industrial upgrading in the components industry. The DTI will have to benchmark to provide comparable levels of support against competitor countries.

The new framework (APDP) will replace the current MIDP that expires in 2012, and will emphasise volume-production support over the current export-focused model. The new programme will seek to double local production to around 1.2million units in 2020. The new incentives will focus on the creation of a strong and sustainable components manufacturing industry, the development of which was seen as insufficient under the MIDP. The APDP will drive an increase in the local content of vehicle makes from 35 percent to 70 percent. One incentive under the APDP is an automotive investment allowance in the form of a direct grant to support investment in new plant and machinery (Venter, 2009). This replaces the MIDP production asset allowance and will be 20 percent of the project value over a three-year-period. There will also be a company specific support allowance which will provide a maximum of an additional 10 percent for costs such as training, technology transfer, localisation and research and development.

3.7 Summary

A competitive advantage ultimately results from an effective combination of national circumstances and company strategy. Company strategies are often concerned with taking action that will lower the cost of value creation and explore new growth opportunities in other markets. Successful execution of strategies requires a degree of flexibility, an ability to adapt to world standards and a long-term perspective that puts building a sustainable business before short-term profits (Franse, 2006).

SA may not have a motor industry in seven to ten years if urgent attention is not paid to increasing local content, gaining certainty on government's support programme for the industry and improving SA cost competitiveness (Venter, 2009). On average SA is 20 percent more expensive as a vehicle-manufacturing country than Western Europe, with China 12 percent less expensive than Western Europe. The average local content of vehicles manufactured in SA has been 35 percent and this needs to grow to 70 percent in order to negate the cost of importing components using long supply chains and weathering a fluctuating currency.

The new incentives (APDP) will focus on the creation of a strong and sustainable components manufacturing industry, the development of which was seen as insufficient under the MIDP. The APDP will drive an increase in the local content of vehicles to reduce production costs and to deepen the component industry. This also implies greater levels of investment by the industry, skills development, and a stronger emphasis on industrial upgrading in the components industry.

Chapter 4 : Empirical Study

4.1 Introduction

This study will use a qualitative research method to investigate the findings of the literature review on the MIDP as a post-apartheid policy instrument.

4.2 Literature review

A literature review was conducted to gain insight into the subject, to incorporate what is already known in this particular field and to review accumulated knowledge of other researchers. Relevant information was gathered from various publications such as textbooks, journals and computer-based searches on databases such as EBSCO-host, Emerald and the Ferdinand Postma library's various other databases on the MIDP as a post-apartheid policy instrument.

4.3 Empirical study

The empirical research describes a process whereby data or facts on the specific subject were gathered and analysed. Participants provided information so that the researcher could develop a better understanding of aspects relating to the specific research objectives and characteristics. A qualitative research method was employed to gather information from the target population for this study. The research methodology and the limitations of the study will be defined in the following paragraphs.

4.3.1. Research Methodology

Qualitative research generates data that is normally difficult to quantify. This research approach is often expressed as personal value judgements from which it is difficult to draw any collective general conclusions. Qualitative research seeks insight through less structured, more flexible approach. The questionnaire was distributed to Top Management, Finance and Specialist employed to handle all aspects of the MIDP.

4.3.2. Limitations of study

The information was gathered solely by electronic distribution of a questionnaire and was dependant on participants' willingness, time and resources to complete the questionnaire. Of the approximate 500 component manufacturers; only 32 manufacturers participated in this study. The geographical location of participants made it impossible to arrange personal interviews. Phone calls were made to participants to encourage participation in questionnaire. Due to time, cost and geographical location of participants there were a limited number of responses. Most of the motor industry manufacturers are located in the Eastern Cape. The major exports comprise of catalytic converters (52.8 percent). These manufacturers were targeted and 15 percent of the participants were from the catalytic converters.

4.4 Research Findings

General questions regarding participants' industry and position in company were asked as general information. There were 13 options in the industry to choose from, catalytic converters, leather, etc. Some participants are in more than one industry, for example, in the catalytic converters, shock absorbers and stamping industry. The positions in the company that were targeted were Top Management, Finance and Specialist employed to handle all aspects of the MIDP. The industries with the most participation are catalytic converters, brake parts and assembly (Figure 4.1) and the majority were in the Top Management position (Figure 4.2).

Figure 4.1: Industry participation

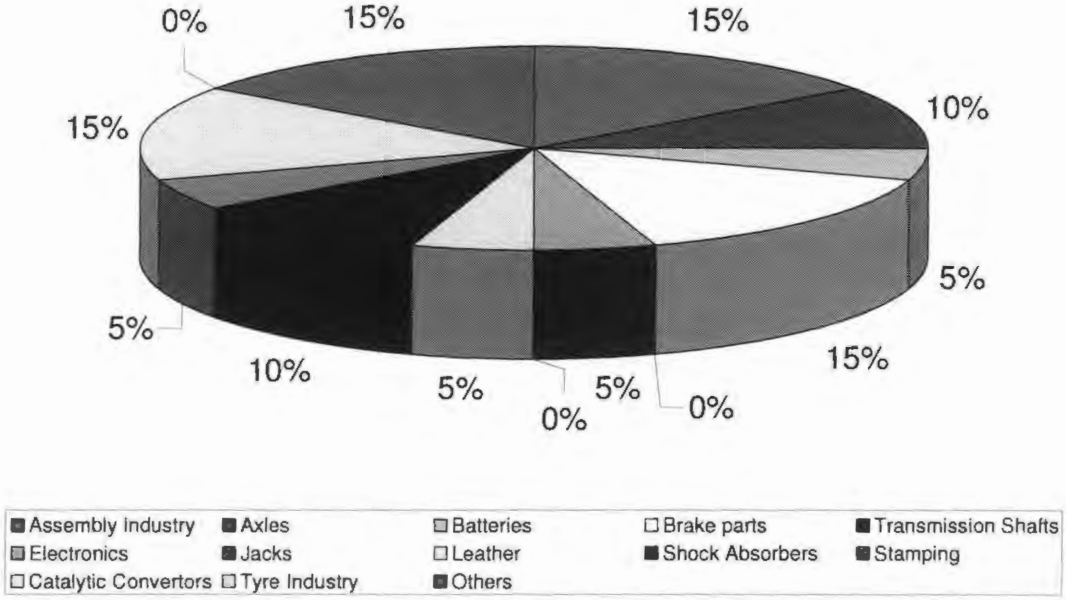
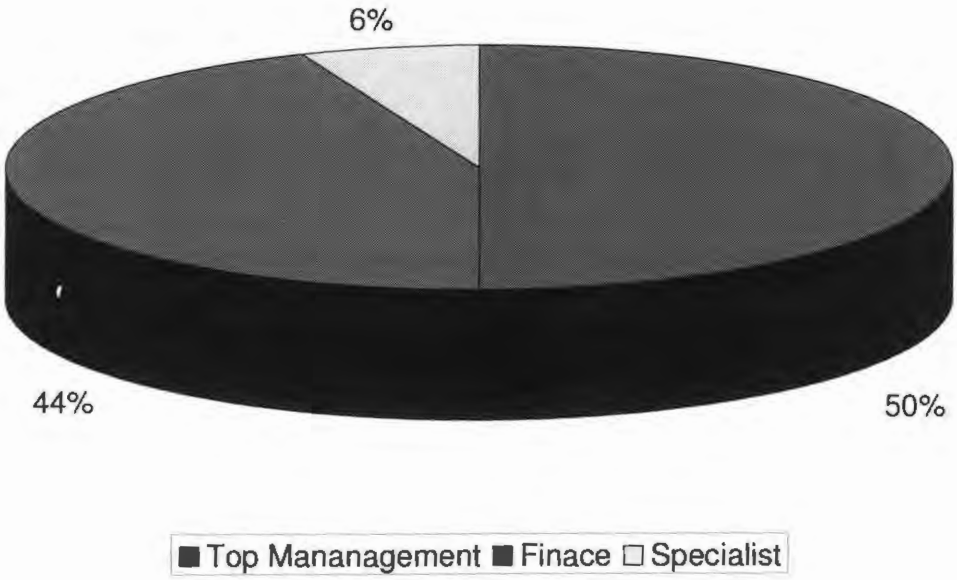
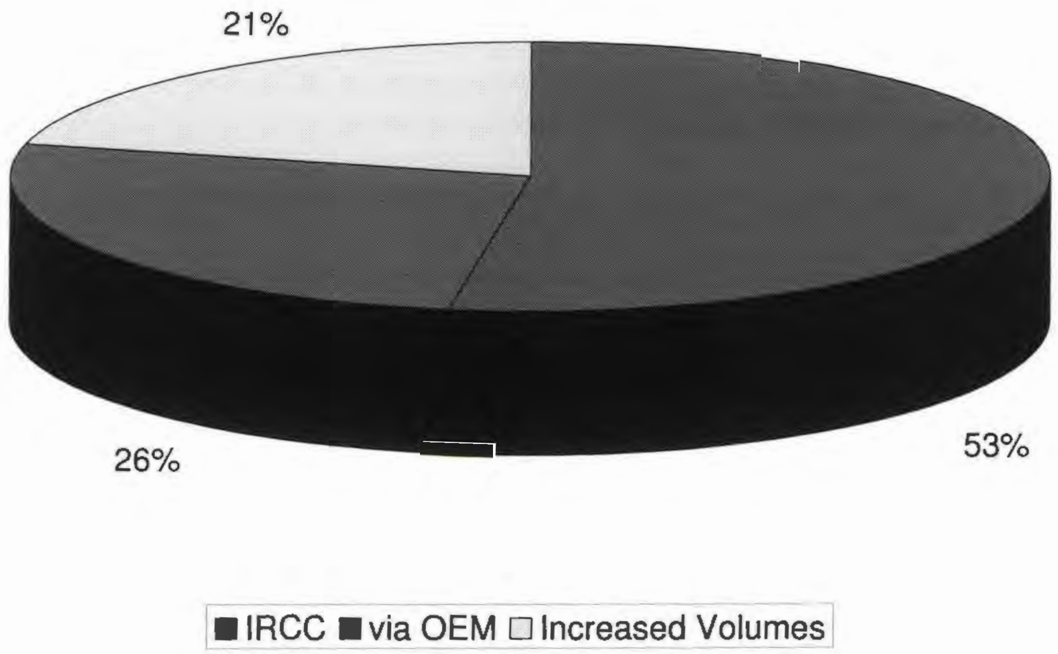


Figure 4.2: Participants' position in company



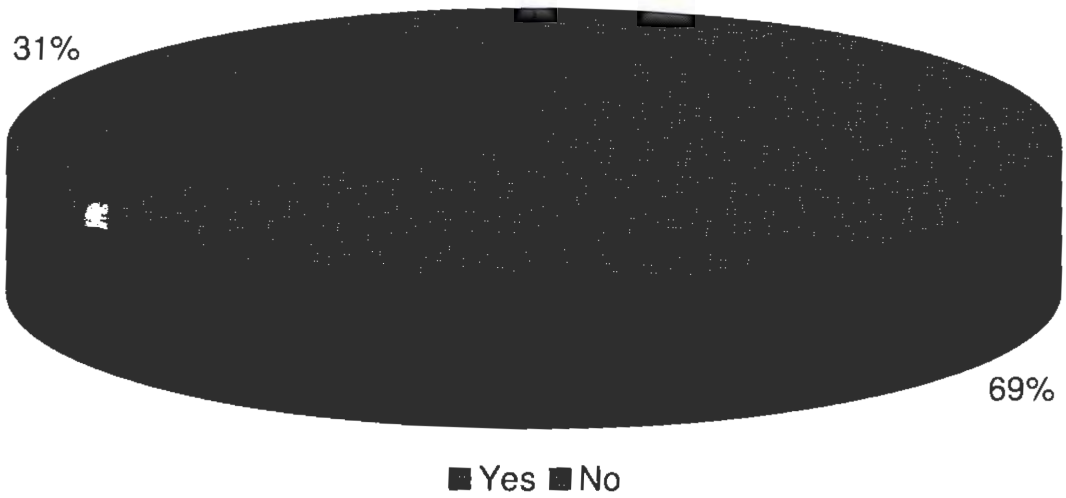
The participants that are registered under the MIDP can benefit via one or more methods. Companies can benefit directly via IRCC claims and/or indirectly via increased orders by OEM and/or indirectly via increased volumes. Participants claim mostly via IRCC claims (Figure 4.3).

Figure 4.3: Industry's methods of benefits from MIDP



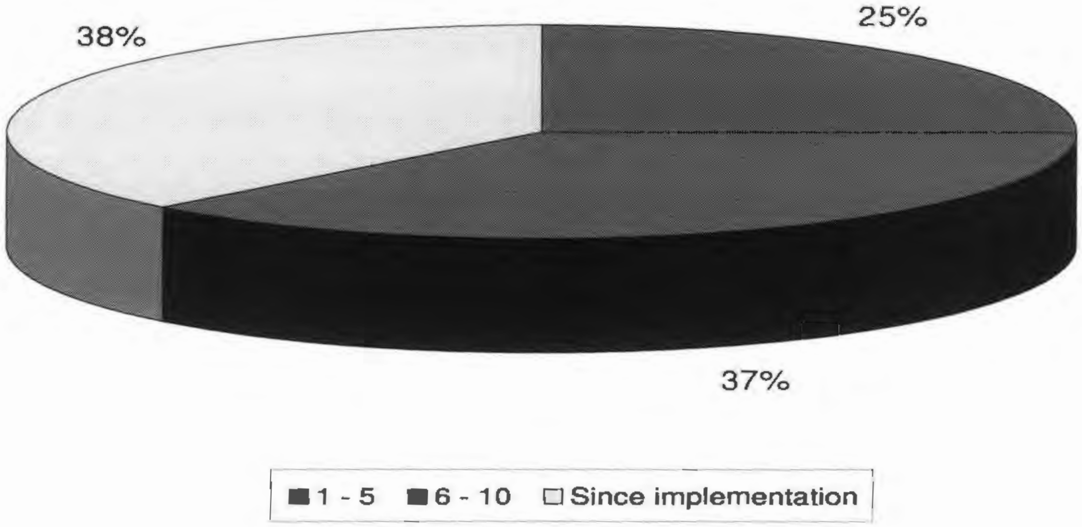
Only 25 percent of the participants companies are not registered under the MIDP the main reason being that they do not export directly. All of the participants know how the MIDP works and understand the rules of the MIDP. The participants were asked whether or not they thought their company could exist without the MIDP and a surprising 69 percent responded that they did (Figure 4.4).

Figure 4.4: Participants' response to the question about whether or not their company would be able to exist without the MIDP



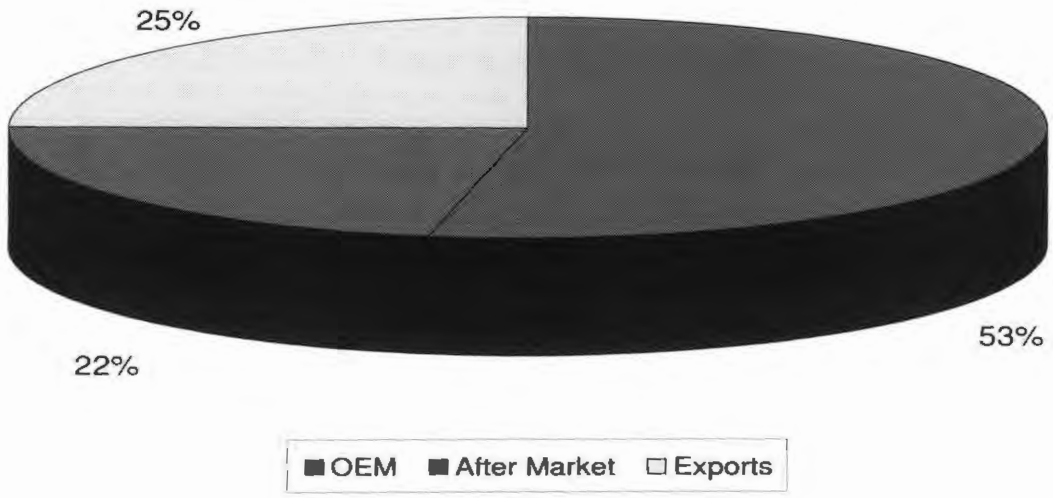
Since the implementation of the MIDP only 38 percent of participants have been registered and 25 percent have only registered as recently as the past 5 years (Figure 4.5). Participants stated that they had seen, on average, a 216 percent growth since implementation and forecast, on average, a 47 percent increase in growth up to 2012. Some participants expected negative growth.

Figure 4.5: Participants' participation in MIDP



Participants sell, on average, 53 percent of their components to OEMs and export only 25 percent directly (Figure 4.6).

Figure 4.6: Sales area of manufacturers



Participants were asked to indicate their views on the value and relevance of the MIDP as a promotional tool for the *SA automotive industry* in general in the global automotive environment. The responses were as follows:

- Restrictive – limited to OEMs only, as they benefit from importing vehicles by discounting the duty payable by offsetting with the exporting of vehicles and components.
- The MIDP is perceived more as a financial consideration, but not a determining factor when evaluating project viabilities, as customers tend not to factor it into their cost/benefit calculation. It's perceived as a legacy issue by European companies who consider it to be a government incentive.
- The motor industry needs incentive to compete with other countries.
- Not good - incentives for volumes have not materialised to the extent expected and OEMs will forgo local supply for cost reduction.
- OEMs developed the component export industry around the framework and benefits received under the MIDP. The incentive was clear, for example, job creation, increasing local content and competitive pricing of CBU imports
- Not enough benefit to compete with the East.
- Without the MIDP the SA motor industry will not be in a position to export and become a first tier supplier.
- MIDP in the catalytic converter industry definitely attracts overseas OE business.
- Key offset for being "stuck" at the foot of Africa. Without the ability to export there is simply not the critical mass within SADEC.

Participants were further asked to indicate their views on the value and relevance of the MIDP as a promotional tool for *their company* in the global automotive environment. Responses were as follows:

- It can be beneficial in securing export products via the parent company.
- Invaluable in order to remain competitive due to high input costs.
- Has no value and relevance to their company
- In its current format it has surpassed its life i.e. offering export credits to offset imports. Certificate value has diminished in value.
- Tier 1 or 2 suppliers always compete internationally excluding the direct MIDP benefit; the monetary benefit never accrued directly to the Tier 1 or 2 suppliers, with OEM as exporter. Some OEMs used some of the MIDP benefit to off-set some of the logistical costs for getting the products to market due to the disadvantage from a geographical point of view
- Not much of a benefit when competing with the East.
- Relevance is low relating to global automotive environment, but relevant relating to the after-market in selling wheels as separate components.
- MIDP in the shock absorber industry. Sales volumes have increased as a result of their wholesale distributors being able to claim MIDP based on their approval.
- Should companies choose to export directly, their throughput will be boosted.
- Fundamental in allowing their company to work closely with local suppliers to develop truly competitive products.
- Companies benefit as there was a transfer of skills/training from overseas, employment opportunities increased, capital investment in the company and greater awareness from overseas in the capabilities of SA companies.

Participants were asked to indicate their views on the role of the MIDP with its extension until 2012 in terms of attracting foreign investments. Responses were as follows:

- Critical – very important for industry.
- Not applicable to small privately owned companies – relevant to their customers.

- Clearly it's an incentive to retain OEMs in SA and is a factor in considering new investment (BMW, VW), but as an incentive to attracting new foreign investments, it has not succeeded- new players need economies of scale and a proximity to their market, neither of which SA offers.
- Not much incentive with excess manufacturing capacity worldwide in the current economic climate and the assumed lack of cost competitiveness.
- When the initial extension was announced, pending decisions were made and as a result more work was placed in SA. However, with the uncertainty about the details of the APDP, some OEMs are getting stage fright. Even declining MIDP benefits as from 2010 result in some OEM projects not being viable.
- Foreign investments will become less due to the fact that MIDP assistance reduces every year, making it more difficult to export.
- Shock absorber prices are more competitive in relation to overseas prices and thus local manufactures normally get the business.
- The MIDP could do a lot more to expose South African motor industry globally for vehicle components. This would then encourage the companies that have closed due to the recession, to reopen for business.
- The AIS is already more significant for Foreign Investment, but the industry will only invest for specific models, as opposed to general capacity investments.
- As a result in the delayed announcement of the APDP benefits, there have been a number of new projects which have been placed with companies in other countries, for example Turkey, India, China and eastern block countries.

Participants were asked to indicate their views on whether the automotive industry in SA was capable of coping with global competition without the MIDP. Responses were as follows:

- Not possible

- It's doubtful the that local industry would be competitive in comparing unit costs because of the relative proportions of fixed to variable costs lacking due to economies of scale, so from that perspective, it will be uncompetitive. However, in the case of OEM suppliers, the proximity to the OEM allows flexible planning because of the shorter logistics supply chain, so OEMs can supply bespoke customer requirements, i.e. .lower volume, but higher margin products, in which case, if they specialise their product ranges, that may offer a more viable sustainable industry.
- Not much incentive with excess manufacturing capacity worldwide in the current economic climate and the assumed lack of cost competitiveness.
- SA automotive suppliers have on many occasions proven competitiveness on an ex-works basis, however, growing logistical costs and the distance to market requires a policy mechanism to somehow even the playing fields. Without any support mechanism such as the MIDP the export component industry is at risk. Alternative incentive mechanisms for foreign investors, such as the OEMs will have to be devised.
- The SA motor industry relies on MIDP to export. We cannot compete in world markets on mass production units. Only in niche markets.
- South Africa is a long way from the main stream. The freight costs to get goods to the overseas markets are already a major disadvantage.
- The motor industry could cope without the MIDP as each motor company negotiates with its own parent company to export components, i.e. SA would be the only country manufacturing certain components for the rest of the world per motor manufacturer. But making seats, shocks, springs, batteries, for instance, could be manufactured for all car companies.
- Critical mass and the geographic distances to market are major factors.
- It will be very difficult to compete if no incentive is forthcoming due to distance from overseas markets, high interest rates and the shortage and lack of skilled labour.

Participants were asked what the main drivers of competitiveness in the automotive industry were. (What gives SA a competitive edge- do we have a competitive edge – a comparative cost advantage – vs. our competitors). Responses were as follows:

- Participants do not believe that SA has a competitive edge without an incentive due to high cost of labour compared to India and China and the high interest rates compared to European countries. A weak rand does compensate.
- Only competitive on volume based production as tooling cost prohibitive for only the local market.
- SA has few advantages, other than as a gateway into the African market, which is not being exploited. All forms of labour are relatively cheap compared to other markets- this needs to be exploited.
- Comparative cost advantage at global quality levels required, volumes don't allow for cost competitiveness although quality standards are comparable. No clear competitive advantage.
- In the Leather industry, the availability and access to the key raw material is an advantage. On quality and labour costs we are competitive, however economies of scale is important in justifying big capital investments, for example Leather Tanneries.
- Capable machines/manning - technical know-how
- Can compete with competitors on low volume items where competitor is not really interested in manufacturing the items.
- Local raw materials as long as they manifest within competitive prices as opposed to import price parity. Aluminium, Steel, Platinum, etc.

Participants were asked about their take on the value of the MIDP to promote their company, in particular, in the global environment since it was implemented in 1995.

- We have been able to secure contracts to manufacture and sell converters directly to overseas customers without the involvement of OEMs and therefore take advantage of the MIDP by selling IRCCs for our own benefit
- Can be of benefit in securing export products from overseas parent company.
- Helped tremendously, they would not be able to compete on price.
- Allowed the industry to weather the recent economic storms, but encouraged complacency. It encouraged development in low tech areas where weight was a determining factor instead of focusing on technological improvement or innovation.
- No direct value at all for chemical industry - supplying into engineering environment. Compared to component suppliers - small value (however very strategic).
- Without the motivation and support from OEMs who derive a benefit from the MIDP in SA it will be extremely difficult to obtain orders from international customers (OEMs & Tier 1s). There is huge competition from low cost Eastern European, North Africa, Asia and South America just waiting to pick up work lost out of SA.
- Since implementation in 1995 MIDP has been a massive benefit to a few companies

In the last part of the questionnaire participants were asked about government's new APDP programme that replaces the MIDP in 2012. Only 31 percent didn't know about the new programme and 50 percent don't know how the new ADPD will work. Participants were asked to indicate their views on the dependence on support for the automotive industry post 2012 when the new APDP will be implemented. Responses were as follows:

- Any incentive can be manipulated and will have to be managed correctly. We do not believe that many companies, including OEMs, can survive without any incentive.

- Critical for motor industry as most countries have some form of incentive for their industry.
- Business as usual- different name but same outcome.
- Unless there is some incentive for local content, cost will drive sourcing off shore with direct imports. We can't compete with long supply chains and low volumes of OEM production compared to elsewhere in the world.
- It is vital to sustain an industry which has been established and which is already competitive on an ex-work basis. The next step would be to become competitive to your customer's door to Europe! This will require support and more time. In excess of 10,000 jobs have been created and cannot be lost at any cost.
- The industry will still be highly dependent on any kind of assistance to survive/compete as world class manufactures.
- It depends to what extent the OEMs will "Claim" the APDP as price reductions.

To conclude, the participants were asked for any suggestions regarding this type of programme? (Short-term and long-term views)

- Consider incentives for developing R&D facilities contracted to OEMs-shared R&D benefiting from cheaper labour costs.
- Link to SDL- employees need to benefit from skills transfer.
- Support for learner ships for Engineers, mechanics, etc. is required - these skills are on the decline.
- Reduce /simplify duties on imported goods.
- These programs hold no direct, or very little, benefit to the auto suppliers (and none to chemical suppliers). No real focus on chemical and paint suppliers, mainly geared to engineering dimensional component suppliers.
- The initial studies conducted on the APDP indicate that the benefit derived from Component exports will be substantially lower than those derived under the current MIDP. The full benefits which will be accrued to the

OEMs under the APDP are still not clarified and therefore un-quantified and remain an open question.

- In our view the MIDP has been very beneficial to this and many other companies In order to create stability in the industry, Government must announce their plans for the long term.

4.5 Summary

It is clear from the study that although the component manufacturers are of the opinion that their companies could survive without the MIDP assistance (69 percent said they could) the motor industry cannot survive without the assistance. Strong views were expressed on the MIDP role in generating business, attracting foreign investment and triggering interest in respect of its relevance and value as a promotional tool in SA motor industry in general. The manufacturers are of the opinion that the MIDP is limited to OEMs only as that they benefit from importing vehicles by discounting the duty payable by offsetting with the exporting of vehicles and components. The advantages lie in the fact that companies benefit from a transfer of skills/training from overseas, employment opportunities increased, capital investment in the demure and greater awareness from overseas in the capabilities of SA companies.

There is a lot of uncertainty regarding the new APDP. When the initial extension was announced, pending decisions were made and in more work was placed in SA. However, with the uncertainty about the details regarding the APDP, some OEMs are getting weary, declining MIDP benefits as from 2010 will result in OEM projects not being viable. It is vital to sustain an industry which has been established and which is already competitive on an ex-work basis. The next step would be to become competitive to your customer's door to Europe. This will require support and more time. In excess of 10,000 jobs have been created and cannot be lost at any cost.

Chapter 5 : Conclusion and Recommendations

5.1 Introduction

Directing the focus on the contribution of the component manufacturers in the motor industry, it is easy to highlight that these companies have been neglected to a large extent. While the MIDP has undoubtedly been a great benefit to the OEMs there has been some concern that motor industry suppliers further down the value chain have not realised the same benefits. Additional to this concern within the motor industry is the general level of competitiveness of these lower level suppliers. In most cases, these organisations are excluded from direct initiatives launched by most OEMs and further do not benefit from international expertise in the form of international joint ventures and multinational participation (UNIDO, 2009).

5.2 Conclusion

The increase of local content will contribute to the creation of additional employment and will ensure stability within the motor industry in South Africa. Manufacturing is caught up in a global whirlwind. Having bailed out the financial system, governments are now being called on to save industry, too. Manufacturing is still a big employer and it tends to be a very visible one. The failure of a famous manufacturer like General Motors (GM) would be a severe blow to people's faith in their own prospects when a lack of confidence is already dragging down the economy.

There are no painless choices, but industrial aid suffers from two big drawbacks. One is that government programmes, which are slow to design and amend, are too cumbersome to deal with the varied; constantly changing difficulties of the world's manufacturing industries. Part of the problem has been a drying-up of trade finance. Another part has come as firms have run down their inventories (in China some of these were stockpiles amassed before the Beijing Olympics). The inventory effect should be temporary.

The other drawback is that industry aid does not address the underlying cause of the crisis: a fall in demand, not just for manufactured goods, but for everything. Because there is too much capacity (far too much in the motor industry), some companies must close, however much aid the government pumps in. Governments don't know which firms to save or the "right" size of any industry. That is for consumers to decide. Giving money to the industries with the loudest voices and cleverest lobbyists would be unjust and wasteful. Shifting demand to the fortunate industry that has won aid from the unfortunate one that has not will only exacerbate the upheaval. One country's preference for a given industry risks provoking a protectionist backlash abroad and will slow the long-run growth rate at home by locking up resources in inefficient firms. The economy is like a network in which everything is connected to everything else, and in which every producer is also a consumer. The important distinction is not between manufacturing and services, but between productive and unproductive jobs (Economist, 2009).

The government is committed to ensuring that the motor industry remains one of the key industries in SA (Doneva, 2009). However, the survival of the industry is not government's responsibility alone. If SA doesn't have higher local content there's no reason for the SA motor industry to exist. At present only a third of the parts in SA cars are local content.

5.3 Recommendations

Although government is committed to ensuring the survival of the motor industry they should make decisions about the how the new APDP will work and communicate their plans to the industry. The momentum of the MIDP should not be lost because of indecisions on government's side. It will take the industry years if, ever, to recover if momentum is lost.

NAACAM, NAAMSA and the DTI should set up a task team and investigate the possibility of increasing market share and not only local content. Unemployment was at 25.6 percent in 2006 (SARB, 2006) and by increasing local content more jobs will be created and this will help alleviate poverty.

On a broader level, the government should reflect on the lessons from the MIDP for the future of industry-specific industrial policies in South Africa.

5.4 Study Evaluation

The primary objective of this study was to critically evaluate the MIDP as an instrument of trade to enhance the competitiveness of the SA motor industry; to investigate Government policy and to investigate the domestic motor industry as an exporter. As seen in this study it is clear that SA is primarily an importer of vehicles. High production costs and geographical location is the greatest contributors.

A suggestion is that the players in the motor industry, in cooperation with government, fund a research into leaner production units and transport corridors into Europe, Asia and the rest of the global market.

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Appendix

Appendix 1: MIDP Questionnaire

Please answer this questionnaire by indicating the applicable columns with an X, or answer in short sentences.

1. Indicate the industry you are in:

Assembly industry (1)	
Axles (2)	
Batteries (3)	
Brake parts (4)	
Catalytic converters (5)	
Electronics (6)	
Jacks (7)	
Leather (8)	
Shock absorbers (9)	
Stamping (10)	
Transmission shafts (11)	
Tyre Industry (12)	
Other (please indicate) (13)	

2. Indicate your position in your company

Top Management (1)		Finance (2)		Specialist (3)	

3. Indicate if your company is registered under the Motor Industry Development Program (MIDP)

Yes (1)		No (2)	

4. Do you know how the MIDP works?

Yes (1)		No (2)	

5. Motivate your answer briefly

---

6. Do you understand the rules of the MIDP?

Yes (1)		No (2)	

7. Motivate your answer briefly

Please answer the following questions irrespective of your answer to Question 6.

8. Indicate the number of years your company has participated in the MIDP

9. Indicate whether your company benefits from the MIDP.

Directly via Import Rebate Credit Certificates (IRCC) claims (1)	
Indirectly via increased orders by Original Equipment Manufacturers (OEM)(2)	
Indirectly via increased volumes (3)	
Other (please indicate) (4)	

10. Indicate whether or not your company would be able to exist without the assistance of the MIDP.

Yes (1)		No (2)	

11. Indicate the relevant sales area in percentage

Sales to OEM	
Sales to after market	
Exports	

12. Indicate the percentage of growth your company has had since the implementation in 1995 until currently and your expected growth forecasted up to 2012

1995- 2008		Forecast to 2012	

13. Indicate your views on the value and relevance of the MIDP as a promotional tool for the *SA automotive industry* in general in the global automotive environment.

14. Indicate your views on the value and relevance of the MIDP as a promotional tool for *your company* in the global automotive environment, in particular.

15. Indicate your views on the role of the MIDP with its extension until 2012 in terms of attracting foreign investments.

16. Indicate your views on whether the automotive industry in SA is capable of coping with global competition without the MIDP.

17. What are the main drivers of competitiveness in the automotive industry? (What gives SA a competitive edge- do we have a competitive edge – a comparative cost advantage – vs. our competitors)

18. What is your take on the value of the MIDP to promote your company, in particular, in the global environment since it was implemented in 1995.

19. Do you know about the new Automotive Production Development Program (APDP)?

Yes (1)		No (2)	

20. If no, motivate shortly

21. Do you know how the new ADPD will work?

Yes (1)		No (2)	

22. Indicate your views on the dependence on support for the automotive industry post 2012 when the new APDP will be implemented.

23. To conclude: any suggestions regarding this type of programs? (Short term and long term views)

Thank you for participating in this questionnaire.

The author

Riana Viljoen

Appendix 2: World motor vehicle production by country and type

UNITS	YTD 2007	YTD 2008		
ALL VEHICLES	Q4	Q4	VARIATION	DIFFERENCE
EUROPE	**22 852 578**	**21 770 785**	**-4,7%**	**-1 081 793**
- EUROPEAN UNION 27 countries	**19 724 773**	**18 432 070**	**-6,6%**	**-1 292 703**
- EUROPEAN UNION 15 countries	**16 691 210**	**15 170 358**	**-9,1%**	**-1 520 852**
Double Counts Austria / Germany	*0*	*0*		
Double Counts Austria / Japan	*0*	*0*		
Double Counts Belgium / Germany	*-196 323*	*-132 402*	*-32,6%*	63 921
Double Counts Italy / EU	*-15 088*	*-12 472*	*-17,3%*	2 616
Double Counts Portugal / Japan	*-18 569*	*-19 695*	*+6,1%*	-1 126
Double Counts Portugal / Spain	*0*	*0*		
AUSTRIA	228 066	150 877	-33,8%	-77 189
BELGIUM	834 403	724 498	-13,2%	-109 905
FINLAND	24 309	18 376	-24,4%	-5 933
FRANCE	3 015 854	2 568 978	-14,8%	-446 876
GERMANY(1)	6 213 400	6 040 582	-2,8%	-172 878
ITALY	1 284 312	1 023 774	-20,3%	-260 538
NETHERLANDS	138 568	132 494	-4,4%	-6 074
PORTUGAL	176 242	175 155	-0,6%	-1 087
SPAIN	2 889 703	2 541 644	-12,0%	-348 059
SWEDEN (2)	366 020	309 034	-15,6%	-56 986
UNITED KINGDOM	1 750 253	1 649 515	-5,8%	-100 738
- EUROPEAN UNION New Members	**3 033 563**	**3 261 712**	**+7,5%**	**228 149**
Double Counts Slovakia / Czech republic				
Double Counts Slovakia / Germany	0	0		
CZECH REPUBLIC	937 648	945 822	+0,9%	8 174
HUNGARY	292 027	346 055	+18,5%	54 028
POLAND	792 703	950 908	+20,0%	158 205
ROMANIA	241 712	245 308	+1,5%	3 596
SLOVAKIA	571 071	575 776	+0,8%	4 705
SLOVENIA	198 402	197 843	-0,3%	-559
- OTHER EUROPE	**2 028 392**	**2 191 605**	+8,0%	163 213
SERBIA	9 903	11 628	+17,4%	1 725
CIS	**2 018 489**	**2 179 977**	**+8,0%**	**161 488**
Double Counts Ukraine / World	-257 754	*-270 000*	+4,8%	*-12 246*
RUSSIA	1 660 120	1 790 301	+7,8%	130 181
BELARUS	27 706	28 511	+2,9%	803
UKRAINE	402 591	423 127	+5,1%	20 536
UZBEKISTAN	184 900	208 038	+12,5%	23 138
TURKEY	**1 099 413**	**1 147 110**	+4,3%	
AMERICA	**19 154 059**	**16 916 515**	-11,7%	-2 237 544
- NAFTA	**15 454 764**	**12 974 058**	-16,1%	-2 480 706
CANADA	2 578 790	2 077 589	-19,4%	-501 201
MEXICO	2 095 245	2 191 230	+4,6%	95 985
USA	10 780 729	8 705 239	-19,3%	-2 075 490
- SOUTH AMERICA	**3 699 295**	**3 942 457**	**+6,6%**	**243 162**
Double counts Venezuela / World	-105 729	-82 200	-22,3%	23 529
ARGENTINA	544 647	597 086	+9,6%	52 439
BRAZIL	2 977 150	3 220 475	+8,2%	243 325
CHILE	10 804	4 405	-59,2%	-6 399
COLOMBIA	73 667	38 327	-48,0%	-35 340
ECUADOR	26 338	29 322	+11,3%	2 984
PERU	0	0		
URUGUAY	0	0		
VENEZUELA	172 418	135 042	-21,7%	-37 376
ASIA-OCEANIA	**30 714 858**	**31 256 384**	**+1,8%**	**541 526**
Double Counts Asia / world	*0*	*0*		
Double Counts China / world	*-102 754*	*-81 750*	*-20,4%*	21 004
Double Counts Thailand / world	*0*	*0*		
AUSTRALIA	334 617	329 556	-1,5%	-5 061
CHINA	8 882 456	9 345 101	+5,2%	462 645
INDIA	2 253 729	2 314 662	+2,7%	60 933
INDONESIA	411 638	600 844	+46,0%	189 206
IRAN	997 240	1 051 430	+5,4%	54 190
JAPAN	11 596 327	11 563 629	-0,3%	-32 698
MALAYSIA	441 661	530 810	+20,2%	89 149
PAKISTAN	169 861	130 857	-23,0%	-39 004
PHILIPPINES	49 492	54 434	+10,0%	4 942
SOUTH KOREA	4 086 308	3 806 682	-6,8%	-279 626
TAIWAN	283 039	182 969	-35,4%	-100 070
THAILAND	1 287 346	1 393 742	+8,3%	106 396
VIETNAM	23 898	33 418	+39,8%	9 520
AFRICA	**544 566**	**582 847**	**+7,0%**	**38 281**
Double Counts Egypt / world	-33 608	*-40 186*	*+19,6%*	*-6 578*
Double Counts South Africa / world	*-104 919*	*-103 100*	*-1,7%*	*1 819*
BOTSWANA	0	0		
EGYPT	104 473	114 782	+9,9%	10 309
KENYA	705	1 080	+53,2%	375
LIBYA	0	0		
MOROCCO	36 671	41 731	+13,8%	5 060
NIGERIA	3 072	2 040	-33,6%	-1 032
SUDAN	0	0		
SOUTH AFRICA	534 490	562 965	+5,3%	28 475
TUNISIA	2 071	2 190	+5,7%	119
ZIMBABWE	1 611	1 345	-16,5%	-266
OTHERS				
TOTAL	**73 266 061**	**70 526 531**	**-3,7%**	**-2 739 530**

(Source: NAAMSA 2009)

Appendix 3: Sub-Programme: Customized sector Programmes

Measurable Objectives	Expected Outcomes	Performance indicator/ measure	2009/10 Target	2010/11 Target	2011/12 Target
Niche Tourism Sector Development	Niche Tourism Development Framework Establish, register (with dti) and support niche tourism associations	Niche Tourism Development Framework in place Number of association registered with **the dti** under the Sector Specific Assistance Scheme (SSAS)	Niche Tourism Development Framework complete South African Youth Tourism Confederation (SAYTC) registered under SSAS Birding Tourism research complete	Birdlife South Africa registered under SSAS Initiate second niche tourism research project	M & E
Sustaining and Growth of local automotive and components manufacturing capacity	Retention of jobs	Value of investment per annum	R3bn	R3bn	R4bn
Cosmetics SMME Development Programme	Improved collaboration amongst various stakeholders in the cosmetics value chain	MoU signed between **the dti** and various stakeholders in the cosmetics industry	Black cosmetics SMMEs operating from backyards and other remote areas made 'bigger and better'	Black cosmetics SMMEs operating from backyards and other remote areas made 'bigger and better'	Black cosmetics SMMEs operating from backyards and other remote areas made 'bigger and better'
Agro-processing sector strategy development	Development and commencement of implementation of strategy	Strategy approved by Exbo	Strategy approved by Exbo	Implementation of strategy	Implementation of strategy
Business Process Outsourcing (BPO) Sector Development	Create an enabling environment for a thriving BPO&O sector that contributes to job creation, economic growth and fighting poverty	BPO Sector Strategy approved	Review of current strategy and development of a new one	Implementation of strategy	Implementation of strategy

(Source: DTI 2009)