



DEVELOPING AN EASTERN CAPE AUTO SECTOR STRATEGY

A REPORT FOR THE EASTERN CAPE SOCIO-ECONOMIC CONSULTATIVE COUNCIL

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This Report has been prepared at the request of the ECSECC, and is intended only for this purpose.

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INTRODUCTION

The purpose of this report is:

- To describe and analyse the historical performance of the Automotive sector of the Eastern Cape economy and to identify current trends
- To identify its growth and labour absorption potential
- To identify key constraints or blockages
- To identify key infrastructural blockages and constraints and to make recommendations on how Government and stakeholders can address the constraints / blockages in a more systematic and pragmatic way

A significant amount of space is devoted to the global industry, its relationships and the inter-relationships between vehicle manufacturers (OEMs) and component suppliers. This has been done because the investment decisions internationally, and this is equally applicable to South Africa, are increasingly being driven by global considerations. These decisions are often, in turn, motivated by OEMs, with the appropriate supplier investments following. Further, the significant rationalisation taking place globally is resulting in a reduction in the number of OEMs, suppliers and model platforms, each of which will have repercussions in all automotive-producing countries. A proper understanding of these complex global trends is essential background to any approach to OEMs or component suppliers for investment.

It is important, therefore, to realise that in attracting new investment to a country or a region, it is unlikely that a component supplier will set up a manufacturing base without prior assurance of OEM business, at least in the local market or for export volumes. In many cases, OEMs are desirous of suppliers investing in the market, but suppliers refuse because the returns are insufficient. In these cases, regional investment and other financial incentives, together with pressure from one or more OEMs, often can assist in attracting that investment.

We have also put South Africa in the international context, namely a very small player with less than one percent of the world's automotive production. As a supplier of automotive products in the global context, we face challenges not only from the traditional first-world markets but also from other emerging markets, many of who have advantages over us. Two of the major disadvantages we have to overcome are (i) geographic, where regions such as Latin America, Eastern Europe and Asia are situated relatively closer to the world's major markets, and (ii) domestic market volume, where countries such as Brazil, China and India have far larger domestic volume bases to attract new investors.

However, South Africa has some advantages, including an efficient government support mechanism in the Motor Industry Development Programme, an abundant supply of raw materials, and a combination of third-world costs and first-world infrastructure. Other specific advantages and opportunities are identified in the report.

It is clear that the South African Government wants the country to increasingly become a global player. This is being achieved through more international trade agreements and continuing reductions in protection. The challenge is to be able to take advantage of the opportunities that flow from these changes, opportunities which the ECSECC can, and must facilitate to ensure its success.

A. THE GLOBAL AUTO INDUSTRY

THE PRESENT STRUCTURE – OEMs

The auto manufacturing industry consists of vehicle manufacturers, component suppliers, raw material suppliers and a complicated network of service and support providers. There are only 23 major vehicle manufacturers or original equipment manufacturers (OEMs) that produce one or more of the major types of vehicles. Only six of them produce heavy vehicles exclusively namely, Navistar, Paccar, Volvo, MAN, Scania and Hino. Another four produce only passenger and light commercial vehicles namely, Honda, PSA (Peugeot-Citroen), Suzuki and BMW. All the others produce all three major categories of vehicles. In addition, a host of smaller specialty vehicle manufacturers have emerged mainly in developing countries such as Malaysia, Russia, India and China, some of which are associated with the larger OEMs in one way or another.

In the passenger vehicle sector, six automakers, namely GM, Ford, DaimlerChrysler, Toyota, Renault-Nissan and VW, have developed critical mass sufficient to be distinguished above the others from a volume point of view with a clear global footprint. Most of them developed dominant positions in their home markets and have developed a clear globalisation strategy, with each producing more than 4,5 million vehicles per annum. As cutting edge R&D demands huge budgets, the smaller OEM's will increasingly be exposed to mergers, takeovers and strategic alliances. Over the last decade a number of prominent OEM's have been taken over and whilst their brand is still available to the consumer, they lost independent status namely, Volvo, SAAB, Kia, SsangYong, Rover, Mazda, Land Rover to name a few. Further, DaimlerChrysler has increasingly begun to exercise control over Mitsubishi. However, this relationship did not last as DC sold their 12,5% stake to Goldman Sachs who sold it on to their investors in November 2005.

The battle for market share globally is intense and with Honda over exposed in North America and making losses in the UK it may lose its independence soon. PSA and Fiat are making inroads in emerging markets – notably South America and Eastern Europe – but have been absent from North America. Fiat has dissolved its alliance with GM and will launch a model jointly developed with Ford Ka model in order to contain costs. This JV trend has been started by PSA/Citroen/Toyota in Poland when these companies announced the development of a joint platform for the manufacturing of 3 models badged as Peugeot, Citroen and Toyota. Hyundai and Kia have not developed much presence outside of Korea and Daewoo has been bought by GM. BMW has just recovered from their disastrous purchase and sale of Rover and as a premium brand owner is largely considered as a low volume player of less than one million vehicles annually. This has now changed as the high volume Mini brand pushed BMW over the million a year threshold. Entry level cars like Renault's low cost Logan will increasingly become the market leaders in the new entrant buyers of the world start to play a bigger role. This vehicle will compete head on with the cheap cars from China and India. Tata recently announced that it is possible to introduce a R 15 000 car in the SA market aimed at the first time buyer of new but affordable transportation.

The volumes and market shares of the car producers is shown on the exhibit following. What is particularly interesting is that recent mergers, takeovers and alliances have concentrated volume in six broad groups: -

A different picture emerges when we look at total vehicle production, including trucks. The top companies and their production changes over the past five years also reflect the effects of takeovers and mergers.

Table of Global Production Trends by Vehicle Manufacturing Group

<u>ALL VEHICLES</u>		<u>2000</u> <u>position</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>% Chng</u>
1	GM	1	8,133,375	7,582,561	8,325,835	8,185,997	8,066,536	-1%
2	Toyota-Daihatsu-Hino	3	5,954,723	6,054,968	6,626,387	6,246,798	6,814,554	14%
3	Ford	2	7,322,951	6,676,491	6,729,499	6,566,089	6,644,024	-9%
4	VW	4	5,106,749	5,108,982	5,017,438	5,017,760	5,095,480	0%
5	DaimlerChrysler	5	4,666,640	4,364,492	4,456,325	4,225,016	4,620,115	-1%
6	Peugeot Citroen	6	2,879,422	3,102,449	3,262,146	3,310,368	3,405,245	18%
7	Honda	10	2,505,256	2,673,671	2,988,427	2,922,526	3,237,434	29%
8	Nissan - Nissan Diesel	8	2,628,783	2,558,979	2,745,596	2,981,154	3,230,326	23%
9	Hyundai-Kia	11	2,488,321	2,518,443	2,641,825	2,697,435	2,766,321	11%
10	Renault- Dacia – Samsung	9	2,514,897	2,375,084	2,328,508	2,386,098	2,471,654	-2%
11	Fiat-Iveco	7	2,641,444	2,409,016	2,190,595	2,077,828	2,119,717	-20%
12	Suzuki-Maruti		1,457,056	1,541,103	1,703,959	1,811,214	1,976,824	36%
13	Mitsubishi		1,827,186	1,647,817	1,821,466	1,582,205	1,428,563	-22%
14	Mazda		925,876	957,012	1,044,536	1,152,578	1,275,080	38%
15	BMW		834,628	946,730	1,090,258	1,118,940	1,250,345	50%
16	Daihatsu		0	0	0	897,116	965,295	
17	Daewoo		716,250	503,689	406,907	520,556	898,940	26%
18	AvtoVaz		755,997	786,008	703,040	699,888	717,985	-5%
19	Fuji-Subaru		581,035	569,191	541,783	544,868	601,205	3%
20	FAW		0	128,976	370,092	556,391	587,427	
21	BeijingJC		124,824	200,524	146,426	261,868	538,699	332%
22	Isuzu		539,085	453,554	436,734	492,464	500,337	-7%
23	Dongfeng		157,038	366,112	334,103	367,537	442,027	181%
24	Chana AG		0	225,399	261,064	0	418,587	
25	Tata-Telco		193,580	175,769	174,624	288,998	378,532	96%
26	SAIC		0	151,591	201,191	323,867	308,665	
27	Gaz – Paz		227,673	201,759	198,135	201,399	214,251	-6%
28	Harbin		122,007	0	0	200,007	205,991	69%
29	Volvo Truck-Renault Trucks-Mack		93,262	154,673	160,820	153,573	191,354	105%
30	Mahindra&Mahindra		0	62,020	72,320	94,782	185,468	
31	Ssangyong		117,485	128,313	162,792	159,314	144,358	23%
32	Anhui Jianguai Auto		0	0	0	93,646	131,300	
33	Navistar		95,242	69,640	68,516	66,495	125,507	32%
34	Paccar-Daf		101,572	75,685	88,416	94,099	125,479	24%
35	Jinbei Auto holdings		0	0	0	124,438	110,505	
36	MG Rover		174,885	163,144	147,037	133,557	106,213	-39%
37	Changhe Aircraft Industry		0	0	0	118,121	104,289	
38	Ijmach-Avto-Roslada		0	87,202	78,236	94,214	96,497	
39	Hino		0	0	0	83,122	94,845	
40	Nanjing Auto		0	0	0	99,469	94,551	
41	Zhejiang Geely		0	0	0	0	91,744	
42	Porsche		51,574	56,746	55,903	81,324	84,095	63%
43	Chery Auto		0	0	0	0	79,565	
44	MAN		70,562	68,144	59,341	60,775	70,482	0%
45	Kamaz		57,043	59,946	58,791	64,082	70,450	24%
46	UAZ		84,872	71,096	69,480	76,897	66,701	-21%

47	Scania	55,581	48,129	45,145	51,276	58,672	6%
48	Southeast Auto Industrial	0	0	0	86,655	57,798	
49	Great Wall Motor	0	0	0	0	54,904	
50	Evobus	6,906	0	0	6,587	7,768	12%
51	Irisbus	7,894	0	0	10,330	5,997	-24%
52	Changan/Harbin	203,127	260,246	454,669	0	0	-100%
53	Hindustan	0	24,063	23,649	15,801	0	
54	Jiangling Motor Group	0	0	0	63,169	0	
55	Perodua	85,000	0	0	0	0	-100%
56	Roslada	31,941	0	41,424	27,649	0	-100%
57	Samsung	13,416	0	0	0	0	-100%
58	SVC	15,943	0	0	0	0	-100%
	Total	56,571,101	55,609,417	58,333,438	59,496,340	63,338,701	12%
	Others	1,821,275	715,850	530,510	1,113,277	836,297	-54%
	Grand Total	58,392,376	56,325,267	58,863,948	60,609,617	64,174,998	10%

Source : OICA

The share of the top six groups has changed dramatically with GM's dominant volume position maintained following the acquisition of Daewoo, but DaimlerChrysler challenged by the merger of Nissan and Renault which pushed it into number 5 position. Similarly, but not due to mergers, Honda's organic growth challenges PSA group. More mergers and consolidations are possible. For a discussion of the vehicle manufacturers' individual strategies see the section titled "STRATEGIES OF MAJOR PLAYERS" later

Whilst critical mass seems to be the most obvious challenge for passenger vehicle OEM's such as GM, Ford and DC most smaller players like Honda, Audi, BMW, Renault, PSA, Fiat, Nissan and Hyundai seems to be on a constant shopping list of the big three. Only Toyota and Honda has declared no intention to merge with others. Later we will have a closer look at possible future strategies of these OEM's.

Apart from major shakeouts still to be expected in the major players, a radical change in the component-manufacturing sector is taking place. Whilst an unprecedented amount of vehicle re-calls due to inferior quality parts have taken place recently, only one of the top OEM's were seriously hampered by a component manufacturer when Firestone caused major re-calls for Ford on it's popular Explorer pick-up truck.

COMPONENT MANUFACTURERS

OEM consolidation has important knock-on effects on the global supply industry. The number of key decision-makers for purchasing is falling as the number of independent OEM's shrinks. Few decision-makers mean fewer core suppliers.

Purchasing is one of the key areas for optimising synergies and delivering cost savings. The newly merged OEM businesses look to develop a common supply base to take the best of what each party has to contribute and to reduce cost through larger volumes and shared design, development, research and testing expenses. DaimlerChrysler is looking to its German and North American suppliers to work together more closely and for some of the stronger partners to takeover the weaker ones. The GM-Fiat alliance began as a joint purchasing group aimed at achieving sourcing efficiencies. Carlos Ghosn, the Renault-seconded President of Nissan, closed three assembly plants in Japan when Renault bought 35% equity in Nissan. Chrysler closed a number of engine manufacturing plants when Daimler merged with them.

The drive to cut costs and the shift of most new model development to a platform basis means that this process is also under way within the supplier base. PSA Peugeot-Citroen is looking to raise the share of platform parts in models to over 60% on just three platforms, instead of less than 30% commonality across five platforms. PSA is typical of the global trend when there are fewer, larger contracts for component companies working on common platform parts.

OEM's no longer have the resources to handle the complete development and testing needs for their growing vehicle ranges. Audi now outsources over half of its engineering work on new models, compared to less than a third five years ago. OEM's are looking for competent system partners to develop and test larger and more complex systems. Increasingly they require suppliers to take responsibility for managing interfaces with other component suppliers.

The benefits of close and deep relationships with competent and innovative companies are recognised by OEM's. To encourage suppliers to deliver these ideas the OEM's are developing closer long-term relationships with their system and modules suppliers. Japan has perfected this system over decades and has been the pioneers in "lean manufacturing principles" to reduce costs in the value chain before it hits the assembly line. In Japan, the supply structure traditionally consisted of a series of tiers with 1st, 2nd, and 3rd tier suppliers. With increased globalisation the structure is rapidly changing with fewer but larger systems suppliers in tier 1, who in turn took over a number of tier 2 suppliers from OEM's.

In return, system suppliers are offered the opportunity of incremental volume and the promise of long-term security in key contracts, but requirements for product development and testing, international reach and system and module competence are being ratcheted up very quickly. Demands for complete safety systems for example, or assembly modules such as front-ends, doors, overheads systems or cockpits require system suppliers to broaden their range of skills.

The know-how required to find synergies, eliminate duplication and provide additional benefits requires a broad portfolio of product and process technologies and expertise in logistics and project management. In part this is being addressed by joint ventures and in part by acquisitions.

In this process, suppliers are required to undertake ambitious investments to acquire and develop these expanded system capabilities, raising the cost and risks of participation as well as opportunities for global specialisation. As a result some component manufacturers increased their commitment to built long-term relationships to secure its financial strength. Smaller players were absorbed and some big players decided to exit as shareholder returns were lowered as the OEM demands increased.

The big changes underway in the first tier co-design mega suppliers require restructuring in second and third tier suppliers in all automotive markets. Second tier suppliers are increasingly re-aligning their marketing efforts in support of these mega first tier suppliers who has now assumed the sourcing role previously done by OEM's. This often involves increased second and third tier quality, deliverability and lower cost competencies and synergistic opportunities which were previously hidden in the OEM procurement cycle. Herein lies the opportunity for lower cost sourcing as more and more high cost first tier suppliers are forced to offer second and third tiers an opportunity to break into new OEM's and territories.

The dynamics of the developments in tiers 1, 2 and 3 create differing strategic alternatives for suppliers, with many facing up to the challenge of rapid growth or exit which will continue to fuel mergers and takeover activity for the decade to come.

Exhibit 3: Top Twenty Automotive Component Suppliers by Turnover

Top twenty component suppliers by revenue, 2003

Rank & Company	Total global sales US\$ million	North America sales %	EU sales %	Asia sales %
1. Delphi Corp.	26,2	74	21	3
2. Robert Bosch GmbH	23,2	23	61	-
3. Denso Corp.	16,9	23	12	65
4. Visteon Corp.	16,5	67	18	8
5. Lear Corp.	15,7	60	36	-
6. Magna International Inc.	15,3	68	30	1
7. Johnson Controls Inc.	15,2	53	39	7
8. Aisin Seiki Co. Ltd.	13,5	12	7	80
9. Faurecia	12,7	10	86	3
10. TRW Automotive Inc.	11,3	41	50	-
11. Siemens VDO Automotive	9,5	18	73	7
12. Valeo SA	8,9	19	71	7
13. ZF Friedrichshafen AG	8,2	20	70	7
14. Dana Corp.	7,9	70	19	6
15. Continental AG	7,6	30	60	5
16. ThyssenKrupp Automotive AG	7,3	50	46	1
17. Yazaki Corp.	5,9	38	11	43
18. DuPont	5,5	50	35	11
19. CalsonicKansei Corp.	5,4	26	8	66
20. Autoliv Inc.	5,3	35	50	10

Source: Automotive World 2003

Component suppliers globally perhaps exceed 10,000, with the top 150 recording revenues over US \$ 500 million per annum. Many of the above major players are already larger than some of the smaller assemblers as listed in [Exhibit 2](#).

KEY ISSUES FACING THE INDUSTRY

KPMG assigned Applied Research and Consulting to conduct research to gain an insight into forces driving change within the automotive industry. The research included 35 top-level executives of OEM's and suppliers in Europe, US and Asia. The following key strategic issues emerged from this study.

Consolidation

Most executives agreed the industry would see more OEM and Supplier merger and acquisition activity. Many predicted a shakeout in the next 5 years, leaving only 5-8 large OEM's and intense consolidation of tier 1 and 2 suppliers. Consolidation will be driven by over-capacity, competition for global market share, need for scale economies and increasingly complex new technology with high entry costs. Ideal acquisitions will be companies with financial strength, new or complementary technologies, compatible platforms, global reach, or access to new product categories or market segments. On the supplier level, as more and more of the manufacturing and technology burden shifts to them, active consolidation will create larger, more powerful 1st tier suppliers. OEM's will encourage this as long as it creates efficiencies and cost reductions.

Excess Capacity

Global production of vehicles is now 65 million annually with excess capacity of 20 million vehicles, in Europe (7 million), US (3 million) and Asia (10 million) driving margins down to 3,9% at OEM's and 5,2% at Suppliers, and even lower in future years. Increasingly OEM's are prepared to close high cost plants and focus on low cost plants. Fiat planned to produce 1 million of their world-car Palio range outside of Italy in 13 low cost countries, including SA. Nissan closed three high cost plants in Japan after Renault bought 35% of Nissan. Renault's Logan will be their cheap world car platform and Toyota is focussing on the Corolla to achieve world car status. DaimlerChrysler shifted global production of RHD C-Class to SA as a low cost option and invested heavily in the SMART compact 2-seater in poverty stricken Hambach in France with huge EU support.

Shift to strategic alliances

Future deals will not merely focus on buying up excess capacity but on consolidating quality and expertise through strategic alliances, partnerships and JV's (mainly driven by government policies like China and economic realities). Post-merger business integration problems such as power sharing, personnel restructuring and cultural differences can be far more complex to handle in M&A's than strategic alliances (Daimler's problematic merger with Chrysler and GM's 6% share swap for 20% shares in Fiat which were abandoned). As OEMs expand into new market segments and increase revenue streams, deals for information, technology, service and consumer product firms will be more common.

Globalisation and Emerging Markets

Globalisation was often cited as the most important factor driving change and cross-border transactions are bound to increase. As technology and access to customers become homogenous in the major world markets, global reach is viewed as the chief means of remaining competitive. Reasons for global activity included dealing with excess capacity, expanding manufacturing and sales presence, cost reduction and procurement synergies.

Globalisation – Risks and Drawbacks

Whilst globalisation is inevitable, concerns around low growth and lack of profitability as well as intense price competition in major markets like Asia and South America will hamper a truly global industry. Cultural differences are viewed as a major drawback as investors are reluctant to support transnational deals. Other risks include foreign infrastructural problems, government regulation and labour force differences. Strategic alliances across borders were often mentioned as smarter alternatives to minimise risk in uncharted territories.

Emerging markets

Attitudes about emerging markets typically balanced concerns about over-estimated demand and excess capacity with the competitive importance of global reach. Southeast Asia, China, South America and Eastern Europe were the markets often cited as facing the most growth in the future, particularly with the prospect of developing economies and liberalised tariffs and regulations. Yet, the rate of growth in these markets is worrying but the long-term view is still favourable.

Suppliers and the supply chain

The supply chain will undergo considerable change in the near future, as fewer, larger tier 1 suppliers assume a greater responsibility for manufacturing, technology and cost control in an increasingly competitive environment. Eventually tier 1 suppliers would manage the bulk of the manufacturing process, becoming tier 0.5 suppliers (Magna, which conducts assembly of some vehicles for OEMs, already describe themselves as such). Modularity will require close cooperation with OEM's but will lead to a more competitive supplier environment and tighter margins.

Shifting the burden of innovation

Although OEM's continue to drive overall design and engineering, technology innovations will increasingly be made by tier 1 suppliers and their tier 2 and 3 suppliers. Component innovation and its inherent capital costs will be shifted onto suppliers but new opportunities for cost reduction and value enhancement will develop stronger ties than before with OEM's.

A reconfigured supply chain

The enormous complexity of the modules and systems integration will require suppliers to consolidate and result in the emergence of a few super suppliers. As these suppliers are looking to increased economies of scale, consolidation will occur at every tier of the supply chain. Robert Bosch AG and Delphi are already larger in revenue than Mitsubishi, Mazda, Hyundai, Audi and MAN to name but a few OEM's.

Innovation and new technology

New technology is one of the major forces dramatically changing the nature of the auto industry. Companies will have to become more responsive and more flexible as products and processes change in the face of stricter government regulation, modularity and consumer demand. Where technological innovation is a source of cost reduction and customer satisfaction, it is seen by many as the most important competitive edge in the near future. Cost of entry will be huge which will ensure that only a few OEM's and large suppliers will be resourced to compete effectively.

Specific new technologies will change the face of the industry in the next ten years. Development is happening fast as new products today become the standard tomorrow. Telematics, new materials, new frame and power-train technologies are already having an important impact.

E-commerce

The future emphasis on the internet between B2B and C2B will enhance cost reductions and customer satisfaction, whilst it represents enormous complex delivery systems best controlled through information highways. Product differentiation and shorter build to order cycles will create opportunities for sophisticated computerised companies. The ultimate vision is to switch from a push to a pull model by which a customer orders customised vehicles on-line and have it delivered within days. Japan already has an 11-day delivery from order model and the UK is studying a 3-day car model.

Brand relationships

As OEM's pass responsibilities down to suppliers, strong focus will be on brand ownership and development. As price, quality and technology becomes more uniform and standard, brand image is going to become more important to the customer. OEM's will be switching marketing strategies from "selling a car" to "buying a driver – for life". Values that are symbolised in a brand will become more important in the purchase decision. Brands currently owned by the major players are listed below: -

BMW: BMW, Rolls-Royce (since 2003), Mini, Riley, Triumph

DaimlerChrysler: Mercedes-Benz, Chrysler, Jeep, Dodge, Plymouth, Smart, Maybach, Benz, DeSoto, Nash, Hudson, Imperial

Fiat: Fiat, Lancia, Alfa Romeo, Ferrari, Maserati, Abarth, Autobianchi, Innocenti

Ford: Ford, Land Rover, Volvo, Lincoln, Mercury, Aston Martin, Jaguar, Daimler, Mazda, Cosworth

General Motors: Opel, Cadillac, Chevrolet, Buick, Pontiac, Oldsmobile, Vauxhall, GMC, Saab, Saturn, Holden, (Subaru, Suzuki,)

Honda: Honda, Acura

MG Rover: MG, Rover, Austin, Morris, Wolseley, Austin Healey

Nissan: Nissan, Infiniti, Datsun

PSA: Peugeot, Citroen, Talbot, Hillman, Hunter, Sunbeam, Singer, Simca, Panhard

Renault: Renault, Dacia, Sport, Alpine, Samsung

Toyota: Toyota, Lexus

VW: Volkswagen, Audi, Skoda, Seat, Lamborghini, Bentley, Bugatti, NSU, DKW, Horch, Auto-Union, Wanderer, Laurin & Klement.

Because of the topicality of the recent takeover of Nissan by Renault, and the impact it may have on their SA strategy, it is interesting to look at how this new group is projected to fare. The views of PWC are shown below.

Chart: Renault-Nissan Strategic Summary

Renault-Nissan Strategic Summary

Renault-Nissan is transforming itself from a successful partnership into an integrated strategic entity.

- The result of two mediocre, regional companies striving to become a global, multi-brand conglomerate.
- An alliance whose total is greater than the sum of its parts through:
 - Leveraging its new-found scale
 - Attaining global reach
 - Developing clear brand identities/visions
 - Cooperating in operational areas

Renault-Nissan
Destined to become a case study in how to (or how not to) manage a corporate alliance

Integration issues to resolve

Sustaining profitability in the wake of Nissan's revival

Brand differentiation and development

Platform consolidation initiatives

Upside Potential:

If goodwill and cooperation continue, the alliance could become the success story of the consolidation era.

Sufficient brand differentiation and product innovation will see both Renault and Nissan gaining market share.

Increased synergies within the alliance could lead to greater cost savings and a more stable financial situation for the group.

Downside Potential:

With Nissan the larger volume partner in an alliance where Renault continues to call the shots, risks of internecine struggles remain.

Badge engineering, platform sharing initiatives and insufficient brand development may lead to sales cannibalisation between brands.

Unaddressed excess capacity issues prove to be a drain on financial stability and negate the benefits of cost savings initiatives.



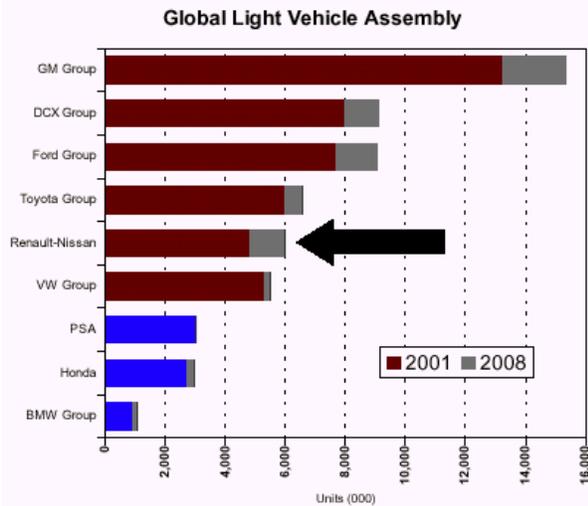
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Chart: Renault-Nissan: Global Competitive Context

Renault-Nissan: Global Competitive Context



Hot on Toyota's Heels: Renault-Nissan's almost 6 million units of global volumes may allow it to surpass VW by 2008

Renault-Nissan's growth over the period is greater than its closest global rivals

- Expansion within the group through organic growth at the expense of its competitors
 - Nissan Revival Plan implemented to re-build Nissan brand and increase sales volume
 - Dacia growing as a world-wide, East Europe-born emerging market brand
 - Exploitation of opportunities in South Korea with Samsung brand
- Sustained financial stability necessary to sustain volume growth

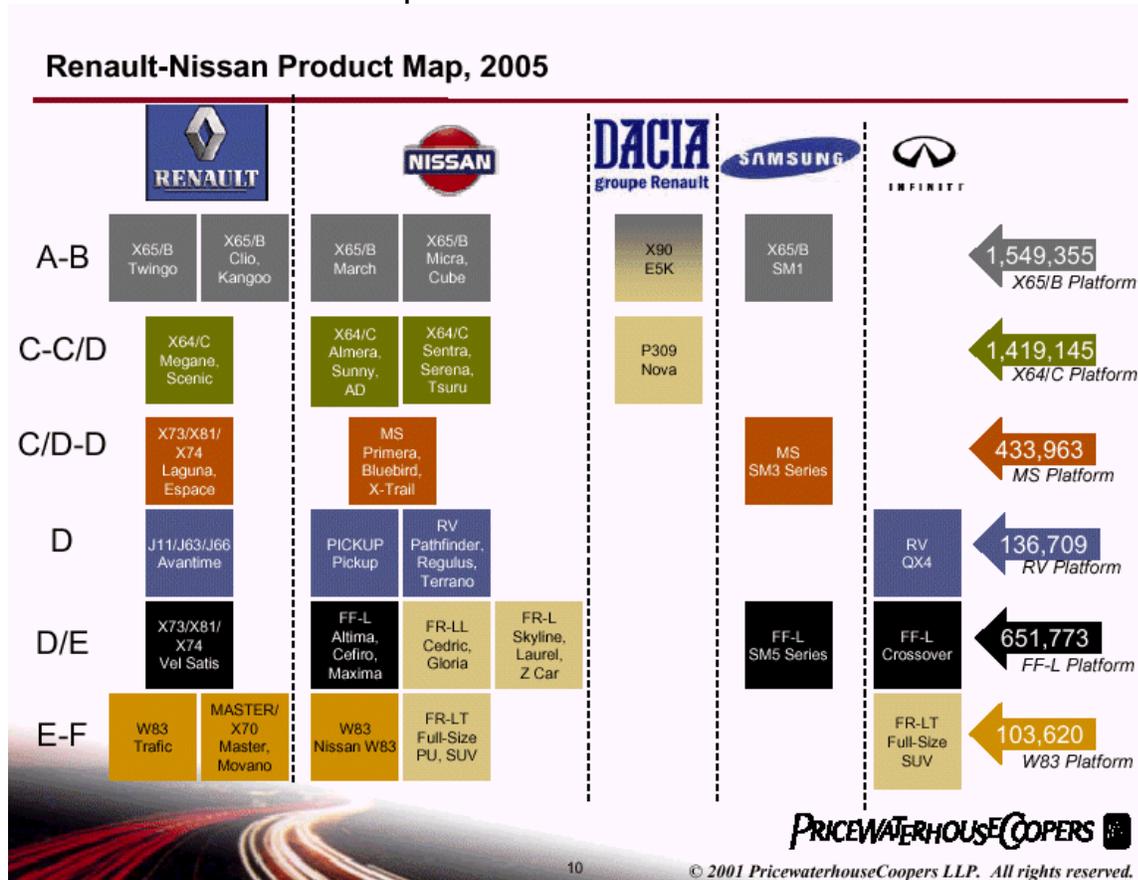
But will this be profitable growth?

- Emerging market growth tends to be risky
 - Low profit per vehicle
 - High volumes not always attainable
- Growth comes with greater cost
 - New outlets and brands to support
 - Broader product portfolio to maintain



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Chart: Renault-Nissan: Product Map 2005



Global Platform Commonisation and South African Opportunities

The chart above provides a good indication of the extent of the product commonisation and platform rationalisation that the major global OEMs are planning. The Renault-Nissan group will end up with one-third the number of platforms they had in 1999, and yet will produce 28 different models from these platforms. This will greatly simplify manufacturing while still providing a varied marketing choice. Other OEMs have announced similar programmes.

By 2008, there are expected to be 18 platforms with production in excess of 1 million vehicles each. The two highest volume platforms, 1.8 million each, will both be built in the Volkswagen Group. General Motors will have five and Fiat one, Renault the two shown above, Toyota three, Ford two, with Honda, PSA and Suzuki planning one each.

One interesting aspect of these high-volume platforms is the opportunity to assemble them in a number of different countries, with components being sourced in high volumes in fewer countries, and interchanged across borders. Projections of production volumes by major region show that there could be a concentration on global platform production in the major emerging markets. South America is expected to be producing 95% of its car volumes on global platforms by 2005, whereas for Europe the figure will be 65%, 50% in North America and only 35% in Japan/Korea. To some extent this reflects the lead that European and North American OEMs have taken in focussing on global platforms.

It is expected, in fact, that almost 25% of the total high-volume platform production will be in emerging countries. This will, in many cases, include South Africa, and there are likely to be opportunities for producing some components in very high volumes.

STRATEGIES OF MAJOR PLAYERS

Exhibit 4 Light vehicle OEM strategies

<p>GM incl SAAB USA</p>	<p>Core Strategy: Growth through globalisation, incl acquisitions & alliances, maintain top global selling position</p>	<p>Plan: GM is plagued by shrinking market share, with too many brands taking market share from each other rather than from rivals. Efforts to boost US market share to 30% failed in 1999, thereby forcing GM to rather focus on brand management and product differentiation of 10 global brands. Tough US union negotiation to reduce risk of bankruptcy like Delphi.</p> <p>Tactic: Consolidating platforms globally to cut costs. Got rid of Fiat put option and held onto JV with Fiat on Powertrain. Has cut 100-year-old Oldsmobile. Bought remaining 50% SAAB shares in January 2000. Seeks a 10% share of Asia-Pacific region, which is expected to grow to 30% of global sales by 2010. Bought bankrupt Daewoo to pursue this dream.</p>
<p>Ford incl Volvo USA</p>	<p>Core Strategy: Recovering market share domestically while becoming more global.</p>	<p>Plan: To assimilate Volvo, Aston Martin, Mazda, Jaguar and Land Rover acquisitions with it's three major US brands to avoid GM's pitfalls. Also cost cutting focus to improve results. Needs to reverse declining market share in EU after lost no 2 position to settle at no 4 with large overcapacity. Lost global no 2 position to Toyota in 2004.</p> <p>Tactic: Focus on e-business initiatives as a way to improve results by US\$ 5 billion on revenue and reduce costs by US\$ 1 billion. Focus EU restructuring plan to reduce overcapacity and cut costs by US\$ 1 billion.</p>
<p>Toyota incl Daihatsu JAPAN</p>	<p>Core Strategy: Recovering market share domestically while becoming more global.</p>	<p>Plan: Maintain momentum and stem market share loss in Japan as it grows organically towards achieving its goal of becoming dominant OEM overtaking GM soon. Joined e-commerce race through Covisint as a customer, not a partner of the Big Three.</p> <p>Tactic: Shift from being a low-cost, high quality OEM to becoming more customer service focussed with overseas operations yielding more revenues. Expand product offerings and increase production in non-Yen developing countries. Created Toyota Financial Services to offer customised services to customers globally. Replaced Ford as no2 seller in the world.</p>
<p>Volkswagen Audi Group (VAG) GERMANY</p>	<p>Core Strategy: Globalisation, expansion of product offerings. Protect itself from hostile take-over by selling shares to Porsche in 2005.</p>	<p>Plan: Leader in EU based on success in only 2 market segments and developing markets like Eastern Europe and China. Seeks to gain significant share in global markets by becoming a broad based product provider.</p> <p>Tactic: Entered light truck market in 2002 with AAC pickup/SUV, the result of a JV with Porsche. Has stated intent to seek partner in heavy truck market as well. Attacking Japanese market with new models and better distribution network and Europe with goal of keeping Golf no1. Created independent online supplier network similar to Big Three's Covisint. Increased sales in Brazil by 11% in 2000, but lost no.1 position to Fiat's Palio range. Face heavy competition in China from new entrants</p>
<p>DaimlerChrysler incl Mitsubishi GERMANY</p>	<p>Core Strategy: Continued integration after merger and closer focus on troubled SMART and Mercedes brand</p>	<p>Plan: Merger challenging two successful but limited firms into one full-line global player without damaging the uniqueness of both Mercedes Benz and Chrysler brands. Also looking to beef up presence in small car market through A-class and MCC Smart. Strong competition, dropping profits and problems in Mercedes and SMART business units force cost cutting strategies globally.</p>

		<p>Tactic: Formed a strategic alliance with Korean Hyundai and abandoned stake in Mitsubishi in Japan intended to create a small passenger car to be marketed worldwide. Bought 10% in Hyundai and 34% in Mitsubishi in June 2000. Disposed of Mitsubishi in November 2005.</p>
<p>Fiat Auto ITALY</p>	<p>Core Strategy: Looking to increase globalisation with US market a key target. Reconstruction plan showing new hope to profitability</p>	<p>Plan: The world's eleventh largest OEM largely controlled by ageing private owners who wants to sell. Protected by Italian government also hindered by limited but exciting product line-up and Korean attacks for market share.</p> <p>Tactic: Hopes for improved domestic market share with Punto, Stilo and Alfa Romeo 147. Dominates the growing South American market and globally experiencing mixed fortunes with a unique developing-market platform, the 178. In 2004, GM put option cancelled of its stock for 20% in Fiat. Two JV born focussing on Powertrain and Purchasing with a clear aim to cut costs. JV Purchasing dismantled in 2004. Fiat sees MAN as potential partner in Iveco its truck division.</p>
<p>Nissan JAPAN</p>	<p>Core Strategy: Turnaround from heavy losses to profitability</p>	<p>Plan: Three-year restructuring plan announced in October 1999, closed 3 of 7 assembly plants, cutting global workforce by 14%, Japanese production by 25% and product costs by 20%. Reduced US\$ 23 billion debt and losses over last 6 years of US\$ 2.8 billion, Nissan sold 1400 supplier companies to generate cash for new model line-up.</p> <p>Tactic: Renault bought a 36.8% stake in Nissan in March 2000 expecting to save US\$ 3.3 billion over 3 years. Adopted Renault's procurement system aiming to slice costs by 30% in 3 years. Will revamp new product line-up and platform sharing Almera with new Megane.</p>
<p>Honda JAPAN</p>	<p>Core Strategy: Expansion, continued globalisation, retain independence</p>	<p>Plan: Expanding limited product line-up. Will provide engines to GM staying independent.</p> <p>Tactic: Introduced low-emission engines and a gasoline-electric hybrid system to market in 2001 in US ahead of its competition. Regional autonomy in large markets in Japan, US and Europe has over exposed it in US and has new Europe focus.</p>
<p>PSA FRANCE</p>	<p>Core Strategy: Expanding to retain and increase newfound markets, mainly from Renault</p>	<p>Plan: Challenge is to hold onto Mercosur market share wrested from Renault on the strength of several new product offerings.</p> <p>Tactic: Posted record sales in 1999 and 2000 on the back of partnerships with rivals Renault, Fiat, Ford and Toyota to design common platforms for several new vehicles and expand in key global markets. Collaborating with previously owned Ford supplier, Visteon to create architectures for a next generation climate control system.</p>
<p>Renault incl Dacia and Samsung FRANCE</p>	<p>Core Strategy: Assimilating Nissan stake, globalisation and cost cutting</p>	<p>Plan: Focus on assimilating Nissan will further hinder launch of new models. Short-term strategy seems to be ready as a global player with Nissan for future years. Also buying a market presence in Asia through Samsung in Korea. Developed entry level world car, Logan on Dacia platform.</p> <p>Tactic: Instituted large-scale cost cutting plans aimed at US\$ 3 billion savings. Signed up to join Big Three's Covisint online parts exchange. In addition the alliance with Nissan expected to save another US\$ 3.3 billion.</p>
<p>Mitsubishi JAPAN</p>	<p>Core Strategy: Streamlining</p>	<p>Plan: Attempting to rejuvenate its image after 500 000 vehicle recall. Focus on advanced and unique powertrain technology and cost</p>

	operations	cutting to boost profits. Tactic: Streamline domestic operations, reducing employees by 10% and reducing production break even down from 1 million to 800 000 cars by 2004. Created a strategic alliance with DC and Hyundai to develop a small car for world markets. Sold 34% of shares to DaimlerChrysler who sold it to Goldman Sachs in November 2005.
Suzuki JAPAN	Core Strategy: Low-cost manufacturing	Plan: Global success comes from low-cost manufacturing via proliferation of models in limited volumes low-end segments. Tactic: Introducing new models of motorcycles and cars in an effort to boost sales outside of Japan. Is leader in mini car segment with 31% market share. Sold 10% shares to GM to have a strategic partnership for common platform possibility.
Hyundai incl Kia KOREA	Core Strategy: Assimilation of Kia and globalisation	Plan: Bought 51% of Kia and abandoned a strategic alliance with DaimlerChrysler. Started a major platform consolidation from 23 to 7 by 2005. Market growth in Europe and US planned. Tactic: Seeking closer ties with DaimlerChrysler and Mitsubishi and aims to build assembly plants in Europe and US to help achieve goal of 500 000 vehicles a year in both markets by 2005. Introduced a small car in 2002 in partnership with DaimlerChrysler and Mitsubishi but found success in Getz.
BMW GERMANY	Core Strategy: Increased profitability after Rover crisis averted.	Plan: In the midst of re-defining itself after near Rover crisis. Entered small car market with Mini and 1 Series and also contest the lucrative 4x4 market through experience gained from Land Rover. Tactic: Sold Rover group but retained Mini brand. Develop its highly successful "Ultimate Driving Machine" campaign further with the X5 introduction. Added X3 SUV and 1 Series to its model line-up. Also started production of Rolls Royce in 2003. Largely owned by Quant family, 46.6%, which could sell to others in future.
Daewoo KOREA	Core Strategy: Needs to settle deal with GM/Fiat soon	Plan: To become global player forced Daewoo into unaffordable investment programme leading them into a perilous financial crisis. Promotes itself as provider of reliable, high value transportation rather than an OEM. Cheap labour gives Korean companies advantages over US and Europe that GM wants to exploit. Tactic: GM take-over finalised and now focus on Europe and US for market share. Operate under Chevrolet in South Africa
Mazda JAPAN	Core Strategy: Stemming losses and reversing market share fall.	Plan: Offer unique products in market niches or key market segments. Tactic: Sold 33.3% of shares to Ford in 1999. Cost cutting pulled them back into profitability. Using Ford product development and marketing capabilities, Mazda is now studying more ways to leverage Ford affiliation. Shares platforms and engines with Ford and sell into young people segment in Japan.

Source: Standard & Poors industry surveys.

From the above surveys, it is clear that globalisation has certain advantages but can also destroy shareholder value if not managed properly. We know for sure that further consolidation is bound to take place and some strategic alliances will develop into stronger groups in future. These events will have major impacts on the supplier industry and the medium and heavy vehicle industries. It is therefore very problematic to predict who will be the leading suppliers of the future. Below, we will try to offer a similar analysis from the developments in the auto sectors of late.

Exhibit 5 Top 15 Global Automotive Supplier Strategies

<p>Delphi Automotive Systems USA</p>	<p>Core Strategy: Growth through globalisation, incl acquisitions & alliances, moving into the aftermarket - Hampered by USA operations and large social services employee costs</p>	<p>Plan: GM sold Delphi in 1999 to focus on assembly core competence which enabled Delphi to develop on market growth outside of GM. Promoting itself as a systems integrator, it must learn how to market and compete against other majors who have an independent supplier culture and much more experienced marketing and sales staff. Aims to grow worldwide aftermarket sales from US\$ 2 billion to US\$ 5 billion annually. Tactic: Recently acquired TRW's Lucas Diesel Systems and AP Distribution Services to help grow European aftermarket sales. Cut 900 jobs in France, UK and Poland to save the company more than US\$ 25 million a year. Formed JV with Plastech Engineering Products to make power and signal distribution system assemblies. Sales expansion strategy has already reaped some benefits but in USA, bankruptcy filed to reduce exposure to healthcare and pension costs.</p>
<p>Visteon Automotive Systems USA</p>	<p>Core Strategy: Life after Ford, clear globalisation vision</p>	<p>Plan: Facing challenges similar to Delphi, Visteon plans to become the world's leading supplier and to build business outside Ford and the US. Was spun off from Ford in 2000 as a tier 1 supplier of modules while also act as tier 2 and tier 3 supplier of sizeable critical mass. Tactic: Expanded its non-Ford business significantly, as they now serve several hundred customers and more than 50 OEM's and tier 1 suppliers. More than a third of new contracts are with non-Ford customers, 28% of them non-US based. Posted 42% drop in earnings as one time correction in selling prices after Ford disposal. In collaboration with PSA on next-generation climate control system tier 1 supplier.</p>
<p>Robert Bosch Germany</p>	<p>Core Strategy: Globalisation</p>	<p>Plan: Operating in 148 production facilities in 28 countries, it competes globally by developing licensees, buying local firms or direct greenfield investment. Bosch is world-renowned for electrical, electromechanical and electronic systems and is the number one European automotive parts supplier. Tactic: Bosch has recently focused its attention on ASIA and in Japan it is represented by 5 companies and 3 shareholdings. It lifted its share in Japanese Zexel Corp. to more than 50%. Teamed up with fellow German engineering group, Siemens to take over Mannesmann Ag's engineering and automotive arm, Atecs for US\$ 9.2 billion.</p>
<p>TRW INCL Lucas Varity USA</p>	<p>Core Strategy: Integrating parts of Lucas Varity, adapting to new environment and globalisation.</p>	<p>Plan: To enhance its competitiveness and profitability and accelerate the pace of change. Tactic: Transforming itself from a maker of engine components to a supplier of wheel control systems including suspension linkages, braking systems and other wheel-based active systems technologies. Transferring knowledge from its aerospace arm to automotive. May divest its sensors and auto components business to reduce debt by US\$2.3 billion. Chassis systems recently opened production facility in Malaysia.</p>
<p>Denso JAPAN</p>	<p>Core Strategy: Wants to be the world's top supplier</p>	<p>Plan: Separated from Toyota in 1946, Toyota still holds 24.6% in shares and sales to Toyota still close to 50%. Aims to gain top market share in more categories and products than it already has by increasing from 12 to 19 by 2005.</p>

		<p>Tactic: Developing new advanced products including a new image processing system that can help a vehicle follow the lane lines and other cars in an “advanced cruise control” mode. Denso recently bought the starter-alternator business from Fiat’s Magneti Marelli SpA and will acquire more European companies. Is working with Microsoft to develop next-generation devices for navigation and intelligent transportation systems applications. Intends to join as customer the Big Three’s Covisint online parts exchange.</p>
<p>Lear Corp USA</p>	<p>Core Strategy: Reducing debt, increasing cashflow</p>	<p>Plan: Holds down cost as JIT supplier. Acquisition phase is over. In response to OEM’s increasing tendency towards outsourcing the manufacture of entire modules of their cars, Lear is working towards offering complete auto interiors to OEM’s</p> <p>Tactic: Lear has been buying smaller auto component makers that can fill the gaps in its module offerings. Planning to buy back stock. Landed a contract to supply complete interiors for a GM line of luxury large vans.</p>
<p>Johnson Controls USA</p>	<p>Core Strategy: Continue expansion through partnerships rather than acquisitions</p>	<p>Plan: Over past 10 years accumulated over 250 subsidiaries and has become a full-service global company. The auto interior supplier will focus on partnerships with industry leaders in electronics to expand and grow in North America.</p> <p>Tactic: Announced alliances with Genrex Corp and Microchip Technology Inc. and plans to announce more. Developing new electronic products. Purchased Nissan’s seat maker Ikeda Bussan Co. as part of Nissans supplier disposal strategy. Built six new plants in USA to support future growth strategy.</p>
<p>Dana Corp USA</p>	<p>Core Strategy: Growth with focus on returns and fiscal discipline</p>	<p>Plan: To expand into aftermarket, and to increase current 40% of non-US revenue by 50% through exports. Seeks to save US\$1 billion over 4 years in cost and inventory expense via online supply chain management network. Divest from non-core businesses.</p> <p>Tactic: Purchased Echlin to support aftermarket strategy. Expanding operations in Brazil for export into developing countries and Europe. Has unloaded non-core businesses with annual revenue of US\$ 850 million annually. Closed its 75-year-old Reading plant.</p>
<p>Aisin Seiki Co JAPAN</p>	<p>Core Strategy: Creating value, continuing global growth</p>	<p>Plan: Challenge is to grow beyond Toyota keiretsu. Is seeking global OEM contracts on environmental and safety systems.</p> <p>Tactic: Launching new products, expanding sales of systems, application of electronic controls and actuating systems to traditionally mechanical components and systems.</p>
<p>Valeo SA FRANCE</p>	<p>Core Strategy: Keeping high profit margins.</p>	<p>Plan: A global supplier of electromechanical and thermal systems and no 2 independent parts manufacturer in Europe behind Robert Bosch. Valeo will continue to seek partners in Asia and wants to grow its e-business.</p> <p>Tactic: Enter into JV with Japanese Zexel Corp. Valeo bought its European and North American climate control businesses, owning 40% of Zexel. Valeo also announced JV with Unisia Jecs, a maker of clutches and transmission parts. Replaced its intranet EDI connections with suppliers with Internet connections. Cut 12 % of workforce and invest in Eastern Europe and South America.</p>
<p>Yazaki Corp JAPAN</p>	<p>Core Strategy: Globalisation</p>	<p>Plan: Wiring harness supplier to establish better alliances with OEM’s.</p> <p>Tactic: Already supplies Toyota, Nissan, Honda, Mitsubishi, Volvo & DC. Co-locating with OEM assembly plants globally, most operations</p>

		in Asia, US and Europe.
Magna International Canada	Core Strategy: Aim to grow to full-service, global company	Plan: Recently grew substantially in Europe, leveraging product diversity in the development of larger, more complex and integrated systems. A privately held firm, Magna is aggressively pursuing a strategy of becoming a major vehicle systems supplier, especially of interior systems and a full-vehicle assembler as well. Tactic: Culmination of this strategy came with the purchase of Steyr Daimler Puch in Austria. May dispose non-automotive sections to remain focussed. Higher revenue derived from increase in European and North American content per vehicle. Acquired 40% stake in Magna Automobiltechnik AG, enhancing position as top world metal forming company. No more acquisitions planned. Landed BMW X3 assembly contract and recently Chrysler Voyager.
Mannesmann AG Germany	Core Strategy: Plans to list automotive division on stock market.	Plan: Produces car information systems, commercial vehicle information systems, cockpit systems, rubber metal parts. Wants to increase VA in products. Tactic: Acquisitions of Philips Car Systems and Aralmex should increase market share. Disposed of Atecs to Robert Bosch and Siemens for US\$ 9.2 billion.
Faurecia France	Core Strategy: Expansion in new markets.	Plan: Europe's fifth largest supplier and No. 1 maker of complete exhaust systems, Seeks to expand global presence and achieve a critical mass in all its product groups. Significant number of new program launches and industrial start-ups. Tactic: Developing more business in North America. Signed a major seating contract with GM, and acquired AP Automotive Systems to advance its growth in exhaust systems. Bought cockpit and door module maker Sommer-Allibert (now SAI) forming Faurecia Interior Systems
Michelin Group France	Core Strategy: Expansion of product range, globalisation	Plan: The world's No 2 tyre maker with 18.3% market share behind Bridgestone. Plans to improve sales volume in aftermarket. Wants to increase productivity by 20% over 3 years by reducing workforce by 10%. Tactic: Major product development efforts focused on new tyre/wheel systems to meet OEM's specifications. R&D focus on using silica in tyres to reduce rolling resistance. Working with Goodyear and developed a PAX system of run-flat tyres mainly for BMW.
Bridgestone/Firestone Inc JAPAN	Core Strategy: Stemming losses and reversing market share fall in Firestone/Ford recalls, globalisation.	Plan: Bridgestone is world leader and wants to expand in newer and developing regions. Tactic: Acquisition activity in China and problems around 1 million Firestone tyres recall on Ford Explorer. Firestone faced legal action in US and Venezuela after 62 fatal accidents were recorded.
Thyssen Krupp Automotive GMBH Germany	Core Strategy: Globalisation and further connection with OEM's	Plan: Supplier of various components such as bodies and chassis, automotive systems and suspensions, but planning to become more of a systems partner to leading OEM's. Tactic: Future projects should emulate the cooperation on SMART, where the company's rear axle facility is closely integrated with the SMART production complex.
ArvinMeritor Inc USA	Core Strategy: Developing as a new company, assimilating	Plan: Essentially a new company after the merger of Arvin Industries and Meritor Automotive in 2000. Also bought 51% in Zeuner Starker of Germany. Will continue to cut costs and

	acquisitions.	restructure. Tactic: Has combined heavy and light vehicle system businesses and looking for growth by joining Covisint.
Freudenberg and NOK Group Germany	Core Strategy: Developing more products, becoming a systems provider.	Plan: World's largest producer of sealing components and the largest non-tyre rubber manufacturer who spent heavily on new product launches. Seeks to become more productive, trimming inventories and minimizing defects. Tactic: Developing lighter alloy for body parts in steel.
Autoliv Inc Sweden	Core Strategy: Expansion of product range, globalisation	Plan: World's No 1 producer of safety systems with products ranging from airbags, seat belts and sensors. Despite supplier to all major OEM's, it plans to expand global presence, expand product ranges, increase vertical integration, improve quality and cut costs. Tactic: Make an obvious move into Japan by acquiring two leading companies and has joined Covisint. Reduce take-over risk by buying back shares.

Source: Standard & Poors industry surveys.

GLOBALISATION AND NEW COMPETITION

Overview

Major trends in the industry are driven by the radically different nature of mature and emerging markets. The different competition bases in mature and emerging markets are changing very quickly. The major manufacturers compete on a global basis aimed at market requirements that differ from country to country in the level of differentiation and specification demanded. In so doing the global OEM's and tier 1 suppliers introduce fierce competition to the local players who responds through M&A activity or face exit strategies.

Global expansion

Over the last few years there has been an increasing trend towards globalisation as is witnessed by the above industry surveys. The main reasons are: -

- Low-cost production sites
- Emerging market sales potential
- Risk reduction through geographic diversification
- Expansion of vehicle product range
- Future competitiveness
- Desire to remain or become a major OEM or OES achieving adequate critical mass

Truly Global Suppliers

Automotive News International developed a supplier-ranking formula - which they call the Global Quotient - using a statistical formula developed by A.T. Kearney. They produced a ranking of the top 50 Global Suppliers, measured on presence in Asia, Europe and North America. The results are very different from the largest suppliers shown in Exhibit 3 above. In fact Delphi, the world's biggest, is only ranked 44th by Automotive News because the company's sales are primarily in North America.

The global strategies adopted by the successful and less-successful suppliers are revealing. While the top-ranked global suppliers tend to be specialists, they adopt a variety of strategies to enter new markets. Autoliv, for example,

forms joint ventures with local companies, then gradually assumes control. Freudenberg formed a close alliance with NOK, a Japanese competitor. And some, such as Takata and Bosch, acquire key suppliers.

Overseas expansion does not guarantee high profits. The ranks of suppliers are littered with companies that tried - and failed - to go global.

None of the top five suppliers in the ranking have made such a blunder. Some, such as Bosch, Autoliv and Takata, have made major overseas acquisitions when it fit their strategies. But none believes in growth for growth's sake.

Conclusions? It's possible to expand into new overseas markets without forming joint ventures or buying a local supplier. But this do-it-yourself approach takes time - lots of time. "If you have a decade to work with - and if you can follow your own customers - you can do it," says Jim Mateyka, a vice president at A.T. Kearney. "But it's very slow. If you don't make acquisitions, you have to follow your customers around the globe."

Top suppliers Global Quotient

1. Takata Corp.	89.7
2. Freudenberg and NOK Group	87.1
3. Autoliv Inc.	72.1
4. DuPont	71.4
5. Robert Bosch GmbH	71.0
6. Yazaki Corp.	68.2
7. TRW Inc.	66.4
8. Goodyear Tire and Rubber Co.	65.4
9. Valeo SA	64.9
10. TI Group Automotive Systems	64.7
11. Continental AG	64.4
12. Tenneco Automotive Inc.	63.5
13. GKN plc UK	62.6
14. Siemens AG, Automotive Group*	62.5
15. Venture Industries	62.2
16. Bridgestone-Firestone Inc.	61.4
17. Thyssen-Krupp Automotive Inc.	61.4
18. Michelin Group	60.9
19. Calsonic Corp.	60.7
20. ZF Friedrichshafen AG	59.9
21. ArvinMeritor Inc.	59.2
22. Federal-Mogul Corp.	58.5
23. Motorola Inc.	57.8
24. Koyo Seiko Co. Ltd.	56.1
25. Lear Corp.	56.0
26. Compagnie de Saint Gobain	55.1
27. Borg-Warner Inc.	54.8
28. Johnson Controls Inc.	54.8
29. Denso Corp.	54.7
30. Mitsubishi Electric Corp.	54.3
31. Sachs Automotive of America	53.2
32. Textron Automotive Corp.	52.1
33. Magna International Inc.	51.4
34. Dura Automotive Systems	50.9
35. NSK Ltd.	49.9
36. Eaton Corp.	49.8
37. Mahle GmbH	45.4
38. Dana Corp.	44.8
39. Faurecia	42.0

40. Mannesman VDO AG*	41.5
41. Sommer Allibert	40.7
42. Magneti Marelli SpA	39.4
43. Visteon Corp.	38.6
44. Delphi Automotive Systems Corp.	37.6
45. Toyoda Gosei Co. Ltd.	37.5
46. Aisin Seki Co. Ltd.	34.5
47. Tower Automotive Inc.	33.9
48. Cummins Engine Co.	33.2
49. NHK Spring Co. Ltd.	31.0
50. American Axle & Manufacturing	22.0

*Siemens AG, Automotive Group is planning to merge with Mannesman VDO AG, in October.

Source: Automotive News

Global sourcing

With competition so intense global OEM's seek "world prices" at the right quality and deliverability for everything they buy. Through networked information highways, they search the globe for the best price and are often willing to purchase components regardless of a supplier's location, hence the term "global sourcing". The price-leading supplier is likely to supply parts to every country where that OEM assembles vehicles. For example, any supplier linked to the Fiat small-car platform stands a chance of producing for well over a million cars on a single platform in ten or more countries versus a supplier who might supply to BMW's global operations at less than one million vehicles in total, covering a variety of different platforms in three or four countries.

Production responsiveness

In order to respond quickly to market demand, the advent of a three-day production car is around the corner. It used to take 11 days for Toyota to assemble a car with fewer variations than is currently being planned. This requires massive changes in production processes, supply and ordering of parts. This will give new meaning to e-B2B systems that needs to link the whole value chain to an OEM's assembly lines.

Supplier villages

As the number of tier 1 suppliers declines, fewer but larger firms supply an increasing percentage of the vehicle. The need to deliver these parts or systems in the proper order is leading supplier village formation around assembly plants. In a supplier village, tier 1 suppliers and state-of-the-art computerised warehouses are located close to the assembly plant, reducing shipping costs and allowing for just-in-time production. This in turn cuts inventory-carrying costs, facilitates shorter build-to-order times and introduces scope for cash on delivery systems. It also facilitates communication between the supplier and OEM and allows both to adjust their production levels as needed. A good example of such a "lean OEM" surrounded by tier 1 suppliers is the SMART factory in Hambach, France owned by DaimlerChrysler. In SA we see the emergence of this trend in East London around DaimlerChrysler's plant and in Rosslyn around BMW/Nissan/Fiat, the latter being supported by the CSIR's Automotive Industry Development Centre and Gauteng Government's Blue IQ package. VWSA will also benefit from the Nelson Mandela Bay Logistics Park. In future, it can be expected that new OEMs investing in a region will attract a number of suppliers at 1st, 2nd and 3rd tier levels in close proximity.

Long-term OEM/supplier relationships

To reward the tier 1 suppliers for their continuous cost cutting and investments in product and systems development, the OEM's are awarding "Life of Platform" or otherwise long-term contracts. As long as the supplier meets price, quality and delivery, the OEM's will guarantee the supplier business for a given part, component or system for a particular vehicle platform's life. With the promise of shared platforms after M&A activities, suppliers can either be marginalized or developed into global giants.

Supply chain management

OEM'S are working with their supply chains to reduce costs. In many cases, OEM's are working with their tier 1 suppliers on an open-book costing basis, thereby deciding up front what is reasonable margin for a certain activity adding direct and indirect costs to determine a fair price. OEM's then expect annual price reductions equal to inflation as obtained from continuous improvements in operating costs and de-contenting. Other means of controlling costs by OEM's is to use their greater buying power to force down quantity discounts in raw material or commodity prices which they contract to and free issue to suppliers who convert it into components or parts. OEM's currently only produce in-house about 30 to 40% of the vehicle, the remaining value is supplied by a few tier 1 and a multitude of 2nd, 3rd and lower tier suppliers.

Emerging markets

Vehicle production in 2005 is estimated to be 65 million in the following regions by ranking as follows: - North America , Western Europe, Japan, rest of Asia, Eastern Europe and South America . Whilst the mature markets are largely saturated, OEM's are focused on emerging markets in Eastern Europe, South America and Asia where markets are expected to grow at up to 10% annually. Africa is hardly noticed in the global picture and South Africa contributes 84% of the continent.

Responding to OEM globalisation and platform consolidation, parts suppliers are revamping and concentrating more on core competencies, becoming system integrators and assuming more R&D responsibilities. As strategic M&A activity brings consolidation to a head and suppliers struggle to gain a competitive edge of being a global supplier, parts suppliers are able to spread risk regionally and globally. Even the previously closed Asian markets are now exposed to foreign investments and competition, though several Asian OEM's tightened their grip on subsidiary parts suppliers to keep foreign investment out for the time being. Renault however has demonstrated how fatal such a strategy could be as it tended to drag a giant like Nissan to near bankruptcy. GM bought Korea's Daewoo for a song, which will fulfil their vision to have a strong Asian presence.

Changes in Component Products

Despite extended operational life for most major car components, investigations indicate that the overall demand is set to rise to 2005, according to a new 600-page study of the world automotive components market published by the Economist Intelligence Unit (EIU). The EIU forecasts strong demand in particular for adaptive cruise control (using radar and sensors), keyless entry systems, air conditioning, cabin filters, fuel filters, entertainment systems, seat comfort features, electronic braking systems, safety features and automatic transmissions.

They believe this will be driven by a number of factors, including:

- Higher replacement demand reflecting the 10% increase in global vehicles in use - from 525m cars in 1999 to 578m by 2005.
- Growth in world car output of 15% over the same period to 40m, which will support OE demand.
- More extensive roadworthiness tests including regular emissions testing.

- A progressive upgrading of standard vehicle specifications to include items such as satellite navigation systems, side airbags, electronic stability programmes, and high intensity discharge headlamps.

Table: Forecast Change in Global Demand by Type of Component (units mils)

	1994	1999	2005	2005/1999 (%change)
Airbags				
Driver b	11.2	27.3	28.7	5
Front passenger b	4.2	22.3	27.1	22
Front side b	0.0	14.7	39.5	169
Air conditioning systems	14.6	21.0	28.5	36
Alternators	95.0	103.0	115.2	12
Transmissions				
Automatic	15.1	17.2	20.3	18
CVT	0.0	0.7	2.4	243
Manual	16.7	17.2	19.3	12
Batteries	129.7	140.9	157.6	12
Brakes				
Disc	86.3	94.5	112.2	19
Drum	47.0	42.7	44.4	4
Clutches	50.6	49.0	50.0	2
Electric motors (OE only)	2,007.3	3,098.1	6,350.2	105
Exhaust systems	147.7	147.2	149.8	2
Filters				
Air	275.0	289.0	304.1	5
Oil	446.5	420.6	407.7	-3
HID headlamps	0.0	2.7	10.0	270
Vehicle navigation systems (OE)b	0.0	2.1	5.6	167
Radiators	47.4	41.1	42.5	3
Seatbelts	167.0	172.2	198.3	15
Shock absorbers	222.5	234.4	253.5	8
Sparking plugs	1,261.7	1,052.1	845.5	-20
Starter motors	101.6	110.4	123.1	12
Tyres	668.2	708.9	779.8	10
Wiper blades	348.8	378.3	415.9	10

(a) Combined OE and aftermarket. (b) Combined Western Europe, Japan and North American markets only. Sources: EIU; industry estimates and forecasts.

Source: Economist Intelligence Unit

B. THE S.A. AUTO INDUSTRY IN THE GLOBAL CONTEXT

OEMs REPRESENTED IN SOUTH AFRICA

During the 1960s and 1970s, a large number of makes were assembled in South Africa. This was a result of the prohibitively high import duties, and sometimes import quotas, during this period, which meant that for vehicles to be sold in South Africa, local production was necessary. With cars having to achieve local content of 66% by weight, prices were high and production generally very inefficient.

During the late 1970s and into the 1980s, political pressures resulted in several makes stopping production and withdrawing from the market completely. These included Alfa Romeo, Chrysler, Citroen, Fiat, Peugeot, Renault, and Volvo. This left only vehicles sourced from Germany and Japan, a situation which prevailed until 1994, when the new political dispensation allowed vehicles from any country to enter the market. Most have returned on a fully imported basis.

Of the 15 global OEM groups and companies that produce at least half a million cars annually, all are now represented in South Africa, either by local production or by importers.

Table of the local producers and importers of light vehicles

<u>OEM/Importer</u>	<u>Makes</u>
General Motors	Opel, Isuzu, Saab*, Suzuki*, Daewoo*
General Motors	Cadillac*, Chevrolet*
Ford	Ford, Mazda, Volvo, Jaguar*, Land Rover
VW	VW, Audi*
Toyota	Toyota, Lexus*, Daihatsu*
Renault-Nissan	Nissan, Renault*
Fiat (assembled by Nissan)	Fiat, Alfa Romeo*
PSA*	Peugeot*, Citroen*
Honda*	Honda*
DaimlerChrysler	Mercedes, Chrysler*, Smart*
Hyundai*	Hyundai*, Kia*
Mitsubishi (assembled by DC)	Mitsubishi
BMW	BMW, Mini*
Subaru*	Subaru*
Tata*	Tata*
Proton*	Proton*

Note: * indicates fully imported.

The ownership of the OEMs has also undergone a change in the post-1994 era. Now BMW, DaimlerChrysler, GM, Ford, Fiat, Nissan and VW are wholly-owned subsidiaries of their parents, while Toyota bought a controlling stake.

Although the South African market is considered important by most of the world's global OEMs, it should be recognized that local production accounts for less than 1% of the world automotive volume, and South Africa is only the 20th largest producer of vehicles in the world. This makes the country vulnerable to global policy changes, and it is therefore critical that the economic and government policy framework is sufficiently friendly to attract and retain the major automotive companies of the world. The MIDP, which will be discussed in a later section, is the major consideration here.

MAJOR COMPONENT COMPANIES IN SOUTH AFRICA

Many of the largest component companies in the world are represented in South Africa. During the sanctions era, many European and Japanese suppliers entered into technical or licensing agreements with South African companies. These were, in some cases, companies that were created after the foreign shareholder disinvested. In other cases, new local suppliers were compelled to obtain foreign assistance to manufacture components for local OEMs.

In recent years, certain foreign suppliers have reinvested in existing South African companies. A more important trend has emerged as a result of the vehicle export programs entered into by BMW, DaimlerChrysler, VW, Ford, GM and Toyota. In these cases, the OEMs need to purchase components from the same global companies situated in South Africa as they source from in Europe and elsewhere. In many cases this has necessitated the European suppliers either buying out or entering into a JV with an existing local company, or setting up a new company in South Africa. While this may benefit certain existing South African suppliers, in some cases it has resulted in business being lost by existing local companies, thereby threatening their viability.

Unfortunately, details of technical and licensing agreements between foreign and local companies is usually confidential, and we are therefore not able to provide a comprehensive list of global suppliers represented in South Africa. However, the following information on the largest global suppliers is relevant.

Table of Major Global Suppliers represented in South Africa

<u>Global Supplier</u>	<u>South African Representation</u>
Delphi	Subsidiary
Robert Bosch	Subsidiary
Visteon	Subsidiary
Denso	License/JV Smiths
Lear	Subsidiary
Johnson Controls	Subsidiary
Goodyear	Subsidiary
Michelin	Representative
Bridgestone	Subsidiary
Continental	License
Dana	Subsidiary
TRW	Subsidiary
Magna	-
Valeo	License
Aisin Seki	-(Controlled by Toyota Japan)
Arvin Meritor	Subsidiary
Federal Mogul	Subsidiary
Faurecia	Subsidiary
Yazaki	License
Autoliv	Subsidiary
Magnetti Marelli	Subsidiary
Siemens	License
ZF	Subsidiary
Zeuner Starker	JV ArvinMeritor

In addition to the above, there are a significant number of European-based suppliers present in South Africa either through direct shareholding or by technical agreements. In fact most of the local OEMs are insistent that they will not purchase components from a supplier that does not have a strong association with one of that OEMs global suppliers.

Whilst several of the local component manufacturers are foreign owned or have already made foreign contacts, there are still many local companies looking for some form of relationship. The local production ability is rapidly changing as more foreign contacts are made. For most local companies, their survival is dependent on forming these international links, so they will be made – it is a matter of who the partner will be.

It is notable that Delphi, the largest component company in the world, only manufacture catalytic converters in South Africa, but no presence from Magna, Canada's largest supplier company. The introduction of these companies into the country can only be a matter of time. Delphi will probably be encouraged to broaden its product range by the return of General Motors. Investments by companies in ELIDZ should be actively encouraged.

Denso is another large player who will probably focus on Durban around Toyota.

STRENGTHS AND WEAKNESSES OF THE SA INDUSTRY

The South African auto industry's major weakness continues to be volume-related, namely low domestic volumes, as well as the distance from high-volume markets. In addition, there is still a perception in several countries, notably the United States and Japan, that products from developing economies are inferior in terms of quality. This makes it difficult for South African companies to enter these large markets without the help of OEMs.

NAACAM, the local supplier association has developed the following list of strengths that the South African industry has:

- Emerging market cost advantages. South Africa has a mixed first/third world economy. This offers cost advantages in certain areas, e.g. labour and property costs.
- Flexible production ability. Through the sanctions era, it became necessary to be able to manufacture a wide range of products that could not be imported. This ability has been retained and single production facilities can usually make a range of quality products at competitive prices.
- Low volume production. Given the above flexibility, South Africa has a competitive advantage when it comes to low volumes. The local production costs will usually be lower than countries that are set up for long production runs. This could be used in lower volume vehicles in niche markets or at model runout.
- Low tooling costs. With its lower labour rates, local tooling under 30cm can be produced at about half the European cost. Note that this does not always apply to plastics injection moulding tooling or tooling of bigger dimensions where the volume is sometimes too low for local operations to be effective.
- Raw material availability. Historically, South Africa exported its raw materials. There is now a move to benefit before exporting. Locally produced materials include: stainless steel, precious metals, steel, aluminium, PVC, polythene and chrome.
- Electricity/land/services costs. With its cheap coal, South Africa has one of the lowest electricity costs in the world. Land is plentiful and, therefore, cheap, as are services.
- Southern hemisphere distribution. With significant markets developing in the southern hemisphere, it frequently makes sense to manufacture and distribute from that area. South Africa falls between South America in the west and Australasia in the east. It also provides easy access to India and China.
- First world production. There are a number of first world production facilities in the country, which are presently focussed on exports, demonstrating South Africa's ability to produce world-class vehicles and components.
- First world infrastructure. With having a mixed economy, some elements will be first world. Relevant ones that stand out are the financial services and logistics areas. A number of institutions offer world-leading financial facilities and comprehensive road, rail, sea and air systems are in place.

- Some unique technologies. There are some novel South African developed technologies. For example, a differential lock to give off-road vehicles performance similar to a 4x4 at a fraction of the cost; aluminium welding technology for radiators and; design of components such as air cleaners and air conditioners that must cope with the higher ambient temperatures and dust found in South Africa.
- As with most countries, the government offers some supply-side measures to encourage investment, development and growth. These schemes are updated on a regular basis to keep them relevant.

This means that there are opportunities for foreign companies to become involved in the development and success of South Africa's local and export markets. The development is happening rapidly and will continue to do so. It is just a matter of who the foreign partners will be and the nature of the relationships that are developed.

STRENGTHS OF THE SOUTH AFRICAN ECONOMY

Unlike several other emerging markets, South Africa continues to perform well as an economy. In a recently published article, Mike Schussler, Economist at T-sec highlighted a healthy economic review of SA as follows:

- Private debt is the lowest in the world @ 65% of GDP compared to 133% in USA; 110% in Germany; 140% in Sweden and 130% in Asian Tigers;
- SA Government deficit at 3% is lower than is required by the European Union on members. Further, government expenditure declined in real terms, and future growth will be modest by world standards;
- SARB and Bank of International Settlements show that labour productivity improved since 1996 at 4,9% pa., double that of the USA;
- Biggest threat is unemployment;
- Exports improved from 21,3% of GDP in 1992 to 29,1% in 2000. Manufactured goods exports increased from 10% of total exports in 1990 to 30% in 2000;
- Exports in dollar terms is growing third fastest in the world, while the trade balance continues to improve;
- Cars are more affordable as the monthly loan repayment on a VW City Golf has reduced 4% since 1995;
- IMF predicts that SA's GDP growth in 2001 will, for the first time since 1980, exceed world GDP growth. The SA forecast at 2,5% is better than the average for the world at 1.1% and this trend is expected to continue in the medium term;
- Airlines are increasing flights to SA whilst cutting back on other popular routes.

INTERNATIONAL PERCEPTIONS OF THE SOUTH AFRICAN INDUSTRY

While South Africans are justifiably proud of the export achievements of the automotive industry, we need to put these into perspective. Firstly, South African vehicle production this year is likely to equate to about three-quarters of one percent of the total global production. Secondly, many international analysts and companies ignore South Africa when talking about the automotive industry worldwide.

C. THE STRUCTURE OF THE SOUTH AFRICAN AUTO INDUSTRY

SIZE OF THE INDUSTRY

The industry's performance over the past five years together with projections for 2001 and 2002 are reflected and summarised in the following industry vehicle sales, export and import data.

INDUSTRY CAR/LCV SALES, EXPORT AND IMPORT DATA : 1995 – 2007

	1995	2000	2001	2002	2003	2004	2005*	2006*	2007*
CARS									
Domestically Produced									
Local Sales	233 512	172 373	172 052	163 474	176 340	200 264	215 000	230 000	250 000
Exports (CBU)	8 976	58 204	97 599	113 025	114 909	100 699	118 000	145 000	160 000
Total Domestic Production	242 488	230 577	269 651	276 499	291 249	300 963	333 000	375 000	410 000
CBU Imports									
NAAMSA	7 246	51 749	67 008	68 128	70 919	100 889	155 000	160 000	170 000
Non-NAAMSA	15 059	10 000	12 500	10 000	11 000	26 500	42 000	48 000	55 000
Total Car Imports	22 305	61 749	79 508	78 128	81 919	127 387	197 000	208 000	225 000
TOTAL LOCAL CAR MARKET	255 817	234 122	251 560	241 602	258 259	327 651	412 000	438 000	475 000
LIGHT COMMERCIALS									
Domestically Produced									
Local Sales	127 363	104 121	113 111	101 956	102 007	123 467	145 000	155 000	165 000
Exports	6 356	9 148	10 229	11 699	11 283	9 360	25 000	60 000	80 000
Total Domestic Production	133 719	113 269	123 340	113 655	113 290	132 827	170 000	215 000	245 000
CBU Imports									
NAAMSA	1 034	1 114	2 035	2 791	2 877	4 162	11 500	12 500	13 500
Non-NAAMSA	3 000	3 000	2 500	2 500	2 500	4 776	10 000	12 000	13 500
Total LCV Imports	4 034	4 114	4 535	5 291	5 377	8 938	21 500	24 500	27 000
TOTAL LOCAL LCV MARKET	131 397	108 235	117 646	107 247	107 384	132 405	166 500	179 500	192 000
Total Car/LCV imports	26 339	65 863	84 043	83 419	87 296	136 325	218 500	232 500	252 000
Total Car/LCV Sales	387 214	342 357	369 206	348 849	365 643	460 056	577 500	620 000	660 000
Imports as % of Car/LCV Sales	6,8%	19,2%	22,8%	23,9%	23,9%	29,6%	37,8%	37,5%	38,2%

Total Car/LCV Production	376 207	343 846	392 991	390 154	404 539	433 790	503 000	590 000	655 000
Imports as % of Car/LCV Production	7,0%	19,2%	21,4%	21,4%	21,6%	31,4%	43,4%	39,4%	38,5%
TOTAL AGGREGATE MARKET	399 967	354 632	382 529	363 184	382 600	481 520	606 200	646 200	696 800
TOTAL AGGREGATE EXPORTS	15 764	68 031	108 293	125 306	126 661	110 507	143 400	205 500	240 500
TOTAL DOMESTIC PRODUCTION	388 442	356 250	406 149	404 441	421 335	455 052	530 400	618 500	684 500
GDP GROWTH RATE	3,1%	4,2%	2,7%	3,6%	2,8%	3,7%	4,3%	4,6%	4,8%

Notes: Domestically produced cars and lcvs total represents a proxy for aggregate local production.
Data excludes imported vehicles which have been re-exported.
Information based on data collected by NAAMSA and estimates of non-NAAMSA sales.
GDP growth rate represents GDP annual changes at market prices in real terms.
CBU Export figures are based on projects announced to date. Announcements of new CBU export programmes could change projections.
*Projections 24th October, 2005

EXPORTS

Exports of South African produced automotive original equipment components, replacement parts and vehicles – as illustrated by the following export revenue figures – continue to grow rapidly. By 2007, the Model being used by the NAAMSA-NAACAM Task Group on the MIDP extension to 2012 indicates significant growth in exports. In real terms, exports of components are projected to rise by 63% between 2000 and 2007, and of vehicles by 112% during the same period.

The vehicles manufactured in South Africa comprise mainly cars and light pickups. Other vehicles, such as SUVs, vans and trucks are mostly imported, as the volumes do not justify local production.

When the MIDP began in 1995, there were 39 different models of cars and light commercials manufactured. By October 2005, that had reduced to 18 with a projection from Naacam that we may see only 15 platforms remaining by 2014. This is in line with the objectives of the MIDP, which is to focus local production on higher-volume models, while permitting the importation of low-volume models through export complementation. South Africa currently imports 47 brands and sells 1000 models locally.

The exports of locally produced vehicles, which prior to the MIDP comprised mainly small cars and pickups to Africa, have grown significantly as shown above. The first major car programme to be announced was the Volkswagen Golf 4 right-hand drive to Britain. The main reason was the lack of capacity in Europe due to high demand for the new model, although the fact that export credits could be used to import vehicles was also an important factor. BMW soon followed with a major expansion and modernisation of their Rosslyn plant in order to permit the export of world-class quality 3-Series to all the right-hand drive markets. During 2000, production was further expanded to include left-hand drive cars destined mainly for the United States. Late in 2000, DaimlerChrysler began production of the new C-Class in right-hand drive form for export, mainly to Britain, Australia and Japan.

All these vehicle export programs have resulted in the respective OEMs rationalizing their local production ranges – BMW from three models to one, DaimlerChrysler from four to two, and Volkswagen from five to three.

Toyota has announced a high-volume export programme for the Corolla and IMV to be launched in 2007, while Ford announced exports of Focus models and GM announced exports of the H3 from 2006 onwards. Nissan-Renault's plans will depend on the group's consolidated global strategy, which will evolve once the product and production consolidation has been finalized internationally. It is considered likely that the company will have to export vehicles from South Africa to remain competitive. Fiat's future is pinned on the Strada off the 178 platform but Nissan has already announced it's unwillingness to continue the assembly contract for Fiat beyond 2008. An opportunity for a new assembly plant beckons here.

COMPONENTS MANUFACTURED

The South African component industry has undergone major changes over the past ten years. Up until 1989, all vehicles produced in South Africa had to have local content of 66% by weight. This resulted in a local industry centred around body stampings, chassis, axles, engines, seats and other trim, while high-value, low-weight components were imported. This was unfortunate, as most of the technological development took place in these high-value components.

In 1989, the local content requirements changed and were measured by value, with a minimum of 55% being required. This began a shift towards some high-value parts, but usually those with little capital investment required, as the low volumes could not justify significant investments. Also the programme rewarded exports through duty credits, resulting in the beginning of component export programmes. Also during this period new models were introduced without the OEMs having to tool up for the high body-stamping investments previously required. This enabled the introduction of many new models at low volume with low investment. However these models still required reasonably high levels of local content by value, which added complexity to the suppliers who now had to produce a wider range of components than before, many at low volumes with little profit.

When the MIDP was introduced in 1995, there was no minimum level of local content required. Instead, OEMs had maximum flexibility, and could choose to pay duty, to export or to add local content. Many decided on reducing unviable local content, as well as dropping local production of low-volume vehicles. This caused further disruptions among suppliers who increasingly found themselves losing business, or being required to compete with the prices of imported components produced in very high volumes.

Several suppliers simply closed their operations, others diversified out of the automotive sector, and some were bought out or entered into joint ventures with foreign suppliers being brought into the country at the insistence of the mainly German OEMs to support their vehicle export programmes.

The local suppliers still produce a wide range of components, but gradually there is a trend by OEMs towards focusing on a narrower group of high-value components which can be used in domestic production as well as exported to parent or associated companies in other countries. Nevertheless, there will continue to be demand for a broad range of components because the higher the local content of vehicles exported, the higher the export credits which can be used to import vehicles and components.

As shown in the previous section, component exports are projected to continue growing at a high rate. The component exports listed below provide a good idea of the focus of component production for the future. However, future growth will include not only the traditional exports, but will also include some new types. The only major categories not reflected presently are those where logistics make the export difficult, namely exterior body panels as well as interior moulded assemblies, such as the centre console, instrument panel and door assembly. Also, newer technology components, such as airbags and lightweight metals, have not traditionally been exported but are considered possibilities.

SUPPLIER EXPORTS

Major component exports (Rm)

Component category	2000	2001	2002	2003	2004	% of total (2004)
Catalytic converters	4 683	8 989	9 204	8 104	8 289	38,1%
Stitched leather components	1 926	2 391	3 184	2 899	3 113	14,3%
Tyres	682	781	1 379	1 278	1 285	5,9%
Engine parts	409	520	771	843	894	4,1%
Road wheels and parts	551	725	955	809	753	3,5%
Engines	76	88	623	564	701	3,2%
Silencers/exhaust pipes	377	282	340	327	407	1,9%
Automotive tooling	362	441	363	529	383	1,8%
Wiring harnesses	319	391	457	427	359	1,7%
Transmission shafts/cranks	127	149	236	263	332	1,5%
Automotive glass	171	241	328	307	311	1,4%
Car radios	89	115	171	332	257	1,2%
Ignition/starting equipment	128	195	231	270	230	1,1%
Filters	118	114	184	142	164	0,8%
Radiators	72	70	199	191	162	0,7%
Brake parts	95	118	215	198	146	0,7%
Gauges/instruments/parts	64	77	119	128	142	0,7%
Axles	63	81	129	119	140	0,6%
Body parts/panels	84	107	140	168	116	0,5%
Batteries	100	116	150	106	114	0,5%
Other components	2 144	2 595	3 505	3 265	3 435	15,8%
Total component exports	12 640	18 586	22 883	21 269	21 733	100%

Note: Complete disaggregating of Customs data is not always possible and certain categories, such as tooling, may contain a small percentage of non-MIDP exports.

Source: the DTI/TISA

The strong rand has taken its toll on the total exports value in rand and created uncompetitive pricing for most exporters. However, most exporters would like to see a stable currency which supports their exports in future. Already, SA has become a leading converter of PGM's and stainless steel into catalytic converters, exporting about 14% of world demand. The SASSDA (SA Stainless Steel Development Agency) aims to increase the local catalytic converter and exhaust stainless steel usage from 40 000 tonnes to 120 000 tonnes by 2005. Consider the magnitude against the background of only 500 tonnes being used in 1995. The spectacular growth has enabled ceramic substrate manufacturers NGK and Corning to invest in Cape Town and PE along with a host of canners scattered over SA. The bulk of these catalytic converters are exported by airfreight to enhance JIT capability, cut holding costs and avoid exorbitant wharfage fees levied by Portnet.

Similarly, automotive stitched leather kits have shown dramatic increased exports, to such an extent that local hides supply is becoming exhausted. Local hides are generally of lower quality due to environmental problems like tick bites, barb wire scratch marks, branding marks, poor abattoir handling and smaller yields, so good quality hides are at a premium. Likewise, airfreight is the preferred method of transport.

Engine parts and components and alloy wheels are the next preferred component group with huge export potential as they benefit from scale economies brought about by exports and cheap energy. Ford has taken the lead in announcing major volume increases from its PE engine plant.

MAJOR COUNTRY EXPORTS from 2000 to 2004

The next table indicates a 5 year historical automotive trade flow pattern by country and also highlights the major trading nations. Germany and Japan together accounts for 50% of all trade over the last five years. The next 10 countries only account for 35% of total trade and SA has a favourable trade balance with USA, UK, Australia and Belgium.

Annexure 1: Quick Reference to South Africa's Bilateral Automotive Trade

Rank:	Country	SA Imports	SA Exports	Total Trade	SA Exports as % of Bilateral Total	% of Overall Trade
1	Germany	87,465,217,391	44,126,226,890	131,591,444,281	33.5	32.9
2	Japan	50,416,271,922	19,714,667,743	70,130,939,665	28.1	17.5
3	United States	12,986,872,702	22,450,786,343	35,437,659,045	63.4	8.8
4	United Kingdom	10,063,667,147	22,371,930,063	32,435,597,210	69.0	8.1
5	France	7,701,671,560	7,486,903,904	15,188,575,464	49.3	3.8
6	Australia	1,471,949,565	11,677,449,759	13,149,399,324	88.8	3.3
7	Spain	6,290,318,108	4,735,481,957	11,025,800,065	42.9	2.8
8	Italy	5,547,420,354	3,545,952,938	9,093,373,292	39.0	2.3
9	Brazil	6,902,629,082	437,381,642	7,340,010,724	6.0	1.8
10	Belgium	852,414,469	4,617,737,832	5,470,152,301	84.4	1.4
11	Austria	5,076,245,677	255,074,539	5,331,320,216	4.8	1.3
12	Korea Rep South	4,125,222,758	489,032,532	4,614,255,290	10.6	1.2
13	Thailand	4,387,821,219	148,402,976	4,536,224,195	3.3	1.1
14	Sweden	3,133,649,602	1,175,562,394	4,309,211,996	27.3	1.1
15	China	2,486,248,874	1,434,909,333	3,921,158,207	36.6	1.0
16	Netherlands	1,747,214,984	2,137,238,497	3,884,453,481	55.0	1.0
17	Taiwan	2,425,520,300	1,402,663,994	3,828,184,294	36.6	1.0
18	Zimbabwe	155,808,710	3,590,647,759	3,746,456,469	95.8	0.9
19	Mozambique	113,517,209	2,882,885,165	2,996,402,374	96.2	0.7
20	Zambia	27,039,498	2,639,038,024	2,666,077,522	99.0	0.7
21	India	1,242,889,189	704,406,485	1,947,295,674	36.2	0.5
22	Singapore	205,249,935	1,660,708,224	1,865,958,159	89.0	0.5
23	Hong Kong, China	411,989,072	1,164,462,790	1,576,451,862	73.9	0.4
24	Hungary	1,425,361,452	58,838,387	1,484,199,839	4.0	0.4
25	Malawi	8,022,174	1,432,391,623	1,440,413,797	99.4	0.4
26	Turkey	922,344,437	485,643,945	1,407,988,382	34.5	0.4
27	Czech Republic	936,928,643	298,745,874	1,235,674,517	24.2	0.3
28	Malaysia	690,108,095	363,149,587	1,053,257,682	34.5	0.3
29	Angola	6,357,053	1,007,006,311	1,013,363,364	99.4	0.3

30	Poland	583,145,297	405,380,134	988,525,431	41.0	0.2
31	Argentina	857,762,785	48,432,645	906,195,430	5.3	0.2
32	New Zealand	48,576,474	789,181,925	837,758,399	94.2	0.2
33	Mexico	542,044,387	270,212,658	812,257,045	33.3	0.2
34	Switzerland	657,657,575	94,598,364	752,255,939	12.6	0.2
35	Kenya	5,437,582	715,181,185	720,618,767	99.2	0.2
36	Canada	326,054,426	389,533,852	715,588,278	54.4	0.2
37	Indonesia	681,760,667	29,326,861	711,087,528	4.1	0.2
38	Mauritius	11,687,062	627,734,301	639,421,363	98.2	0.2
39	Tanzania	3,038,386	618,007,189	621,045,575	99.5	0.2
40	Portugal	439,467,323	92,471,336	531,938,659	17.4	0.1
41	South Africa	525,420,389	974,477	526,394,866	0.2	0.1
42	Ghana	542,786	460,788,783	461,331,569	99.9	0.1
43	United Arab Emirates	82,805,869	358,121,162	440,927,031	81.2	0.1
44	Slovak Republic	417,394,424	623,507	418,017,931	0.1	0.1
45	Philippines	361,738,277	39,102,413	400,840,690	9.8	0.1
46	Nigeria	16,949,173	381,251,964	398,201,137	95.7	0.1
47	Denmark	304,585,889	44,944,286	349,530,175	12.9	0.1
48	Israel	213,065,426	109,515,972	322,581,398	33.9	0.1
49	Russian Federation	22,069,689	289,730,594	311,800,283	92.9	0.1
50	Tokelau Is	9,047,920	293,389,929	302,437,849	97.0	0.1
51	Uganda	1,218,386	260,459,691	261,678,077	99.5	0.1
52	Finland	237,488,009	21,848,939	259,336,948	8.4	0.1
53	Ireland	167,169,351	86,108,923	253,278,274	34.0	0.1
54	DEM REP Of CONGO	675,275	249,029,550	249,704,825	99.7	0.1
55	Luxembourg	168,095,651	15,555,711	183,651,362	8.5	0.0
56	Slovenia	166,965,328	8,793,956	175,759,284	5.0	0.0
57	Saudi Arabia	3,711,485	163,448,154	167,159,639	97.8	0.0
58	Greece	24,437,461	141,477,475	165,914,936	85.3	0.0
59	Madagascar	720,906	149,609,416	150,330,322	99.5	0.0
60	Algeria	478,011	148,956,314	149,434,325	99.7	0.0
61	Cameroon	323,565	137,866,726	138,190,291	99.8	0.0
62	Egypt	26,948,621	104,059,483	131,008,104	79.4	0.0
63	Neth Antilles	1,000,443	97,615,295	98,615,738	99.0	0.0
64	Norway	79,353,789	19,206,083	98,559,872	19.5	0.0
65	Mali	1,888,333	96,162,242	98,050,575	98.1	0.0
66	Ship Stores	-	82,967,431	82,967,431	100.0	0.0
67	Gabon	390,987	81,978,793	82,369,780	99.5	0.0

68	Malta	50,684,681	30,423,243	81,107,924	37.5	0.0
69	Morocco	8,764,134	60,758,767	69,522,901	87.4	0.0
70	Benin	11,297	66,728,835	66,740,132	100.0	0.0
71	Ivory Coast	2,856,634	58,041,056	60,897,690	95.3	0.0
72	Seychelles	334,459	57,644,961	57,979,420	99.4	0.0
73	REP OF CONGO	443,014	55,214,228	55,657,242	99.2	0.0
74	Venezuela	6,625,787	48,232,930	54,858,717	87.9	0.0
75	Iran	3,941,666	50,272,147	54,213,813	92.7	0.0
76	Chile	7,031,270	46,857,969	53,889,239	87.0	0.0
77	Guinea	271,032	51,046,162	51,317,194	99.5	0.0
78	Sierra Leone	37,914,872	12,545,811	50,460,683	24.9	0.0
79	Senegal	221,588	49,242,632	49,464,220	99.6	0.0
80	Pakistan	3,199,036	44,494,649	47,693,685	93.3	0.0
81	Afghanistan	492,776	46,053,082	46,545,858	98.9	0.0
82	Reunion	146,477	36,437,653	36,584,130	99.6	0.0
83	Romania	8,963,537	26,854,212	35,817,749	75.0	0.0
84	Mauritania	255,234	34,943,794	35,199,028	99.3	0.0
85	Yugoslavia	25,922,982	8,461,560	34,384,542	24.6	0.0
86	Tunisia	29,111,005	5,159,117	34,270,122	15.1	0.0
87	Sudan	2,327	32,656,519	32,658,846	100.0	0.0
88	Rwanda	123,091	30,412,656	30,535,747	99.6	0.0
89	Jordan	507,960	29,987,831	30,495,791	98.3	0.0
90	Ethiopia	985,666	29,273,302	30,258,968	96.7	0.0
91	Kuwait	57,014	30,182,834	30,239,848	99.8	0.0
92	Jamaica	232,709	29,951,003	30,183,712	99.2	0.0
93	Gambia	2,903	29,722,794	29,725,697	100.0	0.0
94	Origin Of Goods Unknown	28,522,112	924,442	29,446,554	3.1	0.0
95	Sri Lanka	1,489,526	26,295,148	27,784,674	94.6	0.0
96	Yemen	23,865,052	3,668,970	27,534,022	13.3	0.0
97	Cyprus	7,756,084	16,573,258	24,329,342	68.1	0.0
98	Burundi	181,998	21,985,377	22,167,375	99.2	0.0
99	Peru	705,009	19,758,362	20,463,371	96.6	0.0
100	Colombia	853,098	19,571,536	20,424,634	95.8	0.0
101	Djibouti	79,302	20,299,575	20,378,877	99.6	0.0
102	Niger	230,122	18,891,304	19,121,426	98.8	0.0
103	St Helena	53,841	18,681,583	18,735,424	99.7	0.0
104	Trinidad & Tobago	3,129	18,472,445	18,475,574	100.0	0.0
105	Libya	29,762	16,879,102	16,908,864	99.8	0.0

106	Puerto Rico	6,502,427	9,690,580	16,193,007	59.8	0.0
107	Gibraltar	5,740	15,881,639	15,887,379	100.0	0.0
108	Estonia	1,804,092	13,730,833	15,534,925	88.4	0.0
109	Lebanon	219,467	14,874,806	15,094,273	98.5	0.0
110	Burkina Faso	3,709	14,597,540	14,601,249	100.0	0.0
111	Oman	496,013	13,612,271	14,108,284	96.5	0.0
112	Central African Rep	5,822	13,853,538	13,859,360	100.0	0.0
113	Brunei	44,861	13,698,462	13,743,323	99.7	0.0
114	Croatia	11,982,869	1,590,148	13,573,017	11.7	0.0
115	Eritrea	1,555	13,008,156	13,009,711	100.0	0.0
116	Syria	1,063,501	11,374,691	12,438,192	91.4	0.0
117	Iraq	-	12,370,226	12,370,226	100.0	0.0
118	Nicaragua	10,600,942	758,642	11,359,584	6.7	0.0
119	Chad	653	11,208,497	11,209,150	100.0	0.0
120	Togo	3,457	11,144,567	11,148,024	100.0	0.0
121	Bosnia & Hercegovina	9,647,223	1,091,671	10,738,894	10.2	0.0
122	Barbados	56,322	9,327,497	9,383,819	99.4	0.0
123	Bulgaria	829,922	8,342,983	9,172,905	91.0	0.0
124	Panama	85,211	8,798,674	8,883,885	99.0	0.0
125	Surinam	9,987	8,872,370	8,882,357	99.9	0.0
126	Bahrain	179,383	8,442,395	8,621,778	97.9	0.0
127	Iceland	1,999,146	6,088,670	8,087,816	75.3	0.0
128	Uzbekistan	10	7,525,545	7,525,555	100.0	0.0
129	Lithuania	195,550	7,190,224	7,385,774	97.4	0.0
130	Ecuador	4,624,794	2,056,834	6,681,628	30.8	0.0
131	Unallocated	61,024	6,505,488	6,566,512	99.1	0.0
132	Georgia	1,188,748	5,075,911	6,264,659	81.0	0.0
133	Equatorial Guinea	889,941	4,618,932	5,508,873	83.8	0.0
134	Liechtenstein	3,526,317	1,961,960	5,488,277	35.7	0.0
135	Qatar	202,434	5,207,760	5,410,194	96.3	0.0
136	Guinea-Bissau	-	5,167,217	5,167,217	100.0	0.0
137	Albania	42,741	4,946,089	4,988,830	99.1	0.0
138	Liberia	301,717	4,378,576	4,680,293	93.6	0.0
139	Comoro Is	2,521	4,550,275	4,552,796	99.9	0.0
140	Kazakhstan	-	4,485,984	4,485,984	100.0	0.0
141	Andorra	38	4,429,232	4,429,270	100.0	0.0
142	Uruguay	1,458,085	2,941,968	4,400,053	66.9	0.0
143	Bangladesh	16,153	4,333,971	4,350,124	99.6	0.0

144	Ukraine	2,899,921	1,168,132	4,068,053	28.7	0.0
145	Guadeloupe	1,674,206	2,113,448	3,787,654	55.8	0.0
146	Costa Rica	1,701,323	2,044,558	3,745,881	54.6	0.0
147	Cuba	644,128	2,969,192	3,613,320	82.2	0.0
148	Dominican Rep	379,109	3,152,447	3,531,556	89.3	0.0
149	New Caledonia	985,255	2,507,786	3,493,041	71.8	0.0
150	Antigua	1,030,228	2,081,963	3,112,191	66.9	0.0
151	Antarctica	41,281	2,955,998	2,997,279	98.6	0.0
152	Viet-Nam Rep	962,654	1,860,836	2,823,490	65.9	0.0
153	Cape Verde Is	1,567	2,654,345	2,655,912	99.9	0.0
154	Maldives	40,394	2,564,779	2,605,173	98.4	0.0
155	Sao Tome & Principe	189,376	2,283,950	2,473,326	92.3	0.0
156	Guatemala	16,533	2,315,992	2,332,525	99.3	0.0
157	Monaco	1,971,384	294,177	2,265,561	13.0	0.0
158	American Samoa	3,963	2,172,003	2,175,966	99.8	0.0
159	North Korea	1,654,212	492,781	2,146,993	23.0	0.0
160	Br Virgin Is	1,855,418	211,072	2,066,490	10.2	0.0
161	Grenada	18,363	1,709,820	1,728,183	98.9	0.0
162	Bahamas	-	1,721,583	1,721,583	100.0	0.0
163	Kyrgystan	732,643	960,374	1,693,017	56.7	0.0
164	Macedonia	720,259	967,586	1,687,845	57.3	0.0
165	Macao	805,699	863,251	1,668,950	51.7	0.0
166	Czechoslovakia	-	1,577,774	1,577,774	100.0	0.0
167	Somalia	188,656	1,335,017	1,523,673	87.6	0.0
168	Martinique	-	1,482,757	1,482,757	100.0	0.0
169	Dominica	675,032	638,093	1,313,125	48.6	0.0
170	Papua New Guinea	-	1,267,343	1,267,343	100.0	0.0
171	Moldova	57,157	1,189,210	1,246,367	95.4	0.0
172	Lesotho	-	1,121,647	1,121,647	100.0	0.0
173	Marshall Is	903,400	135,653	1,039,053	13.1	0.0
174	Fiji	51,008	928,570	979,578	94.8	0.0
175	El Salvador	11,390	967,329	978,719	98.8	0.0
176	Nepal	4,539	965,992	970,531	99.5	0.0
177	Myanmar	48,155	863,483	911,638	94.7	0.0
178	Paraguay	78,119	712,084	790,203	90.1	0.0
179	Belize	475,815	308,965	784,780	39.4	0.0
180	Honduras	54,071	725,625	779,696	93.1	0.0
181	Belarus	665,797	-	665,797	-	0.0

182	St Lucia	373	628,869	629,242	99.9	0.0
183	Guyana	700	584,177	584,877	99.9	0.0
184	East Gemany	320,772	197,960	518,732	38.2	0.0
185	Armenia	5,480	465,808	471,288	98.8	0.0
186	Azerbaijan	3,121	450,367	453,488	99.3	0.0
187	Guam	-	453,247	453,247	100.0	0.0
188	Tajikistan	233,168	162,105	395,273	41.0	0.0
189	N Mariana Is	-	305,802	305,802	100.0	0.0
190	Latvia	125,305	156,372	281,677	55.5	0.0
191	Faeroe Is	272,380	-	272,380	-	0.0
192	Namibia	28,996	240,847	269,843	89.3	0.0
193	Tonga	-	235,413	235,413	100.0	0.0
194	Bolivia	159,675	67,030	226,705	29.6	0.0
195	Laos	97,411	87,003	184,414	47.2	0.0
196	St Kitts-Nevis	107	181,132	181,239	99.9	0.0
197	Micronesia	-	174,870	174,870	100.0	0.0
198	Mayotte	-	169,627	169,627	100.0	0.0
199	Cayman Is	15,995	124,134	140,129	88.6	0.0
200	Botswana	108,442	26,509	134,951	19.6	0.0
201	Cook Is	60,140	68,956	129,096	53.4	0.0
202	East Timor	74,525	49,909	124,434	40.1	0.0
203	St Vincent	20,340	96,641	116,981	82.6	0.0
204	Haiti	65,196	50,400	115,596	43.6	0.0
205	Mongolia	106,205	-	106,205	-	0.0
206	Fr Polynesia	-	101,695	101,695	100.0	0.0
207	Turkmenistan	-	87,034	87,034	100.0	0.0
208	Montserrat	21,354	64,645	85,999	75.2	0.0
209	Swaziland	41,460	42,246	83,706	50.5	0.0
210	Anguilla	14,365	14,700	29,065	50.6	0.0
211	Niue Is	14,511	3,570	18,081	19.7	0.0
212	Heard & Mc Donald Is	-	17,487	17,487	100.0	0.0
213	Bermuda	1,353	14,555	15,908	91.5	0.0
214	Aruba	-	13,614	13,614	100.0	0.0
215	U S Virgin Is	3,049	6,620	9,669	68.5	0.0
216	Truks & Caicos Is	727	7,480	8,207	91.1	0.0
217	Nauru	7,299	-	7,299	-	0.0
218	St Pierre & Miquelon	6,481	-	6,481	-	0.0
219	Vatican City	6,095	-	6,095	-	0.0

220	San Marino	-	5,920	5,920	100.0	0.0
221	Karibati	3,453	-	3,453	-	0.0
222	Cocos (Keeling) Is	2,483	-	2,483	-	0.0
223	Western Samoa	2,404	-	2,404	-	0.0
224	Br Solomon Is	1,852	-	1,852	-	0.0
225	Greenland	1,137	-	1,137	-	0.0
226	Bhutan	643	-	643	-	0.0
227	Bouvet Is	245	-	245	-	0.0
228	Fr Guiana	201	-	201	-	0.0
229	Br Indian Ocean Terr	6	-	6	-	0.0
	Total	226,551,381,653	173,979,953,259	400,531,334,912		100.0

Source: Blueprint International 2005, TISA statistics supplied by SARS

MAJOR GROUPINGS, LOCAL AND REGIONAL ALLIANCES

In evaluating the South African automotive industry, it is important to examine regional and other groupings.

Regional spread of the South African Industry

Eastern Cape

Port Elizabeth/Uitenhage/ELIDZ – GM, VW, Ford engine plant, many suppliers
East London – DaimlerChrysler, few suppliers

Gauteng

Rossllyn – BMW, Nissan, Fiat and many suppliers
Pretoria East – Ford, few suppliers, (also SABS, CSIR/AIDC, DTI/TISA)
Benoni/Germiston – some suppliers

KwaZulu-Natal (KZN)

Durban area – Toyota, some suppliers

Western Cape, others

Few suppliers

As can be seen the two major centres of component manufacture are Pretoria and Greater Port Elizabeth, while these two plus Durban produce the majority of vehicles.

Other Groupings and Clusters

During 1999, a regional initiative took place in the Eastern Cape, called the Fish River Cluster. This brought together all the major OEM and supplier companies to examine where they could co-operate in non-competitive areas in Logistics, Human Resource Development, Strategic Investments and Supplier Development. The major result was the establishment of the MIC (Motor Industry Cluster), which has achieved some rationalization of logistics and resultant savings for the participants. A further spin-off of the Cluster was the establishment by the DTI of an ad-hoc

group of Purchasing managers from all the OEMs to identify strategic investments required to support OEM export and production of world-class vehicles. The results of this group's deliberations are discussed later in this report.

Another important group is the German company purchasing group, comprised initially of BMW, DaimlerChrysler and VW. Their objective has been to explore opportunities for the local OEMs to pool volume requirements to encourage new suppliers, mainly from Europe, to set up production in South Africa, the logic being that the combined volumes will be more attractive than only one OEM's volume. Delta was later invited to join this group. There has been some success in obtaining new supplier investment, although how much resulted from the group's influence is unknown.

Other regional groups exist, some more structured than others, such as the Rosslyn motor cluster and the KZN benchmarking group, which collaborates on improving operations based on research conducted by academic and private sector consultants.

A recent development has been the establishment of the AIDC (Automotive Industry Development Council), an offshoot of the CSIR. The AIDC was established to facilitate and assist the process of improving the international competitiveness of the South African vehicle manufacturing and associated industries. Areas identified as requiring attention include supplier development, logistics, e-commerce and the development of small and medium enterprises in the automotive industry. The AIDC is supported by the DTI as well as the Gauteng BlueIQ initiative and Eastern Cape Government. It recently signed an agreement with the University of Pretoria to establish two automotive-related Chairs. It is currently involved in the ELIDZ and busy with a feasibility study for Durban Metro for a supplier park for Toyota.

D. POSSIBLE FUTURE CHANGES IN SOUTH AFRICA'S AUTO INDUSTRY

INTERNATIONAL FORECASTS

PricewaterhouseCoopers have updated their global automotive industry forecasts following the events of September 11th. Their perspective on the African and Middle East region are shown in the charts below.

Chart: Africa and Middle East Business Environment

Middle East & Africa Business Environment

Middle East & Africa is characterized by economic, political and social disparities

- Overall, the region remains under-developed, economically weak and politically unstable
- Stronger economies dependant on international oil and mineral prices
- Weaker economies are internally orientated and, where stable, depend on limited primary commodities for external trade
- The region as a whole has failed to live up to the economic growth prospects of other emerging markets in South Asia & Latin America and creates a mixed picture for automotive-related commercial opportunities

Downside Scenario: Instability prevails in the region. Zimbabwean crisis (especially post 2002 elections) could degrade further to undermine hard-won gains in South African investor confidence. HIV/AIDS epidemic remains unchecked - worsening labour productivity throughout the region. Primary commodity prices continue to drive the majority of economies and foreign investment remains constrained as reforms to diversify and externalise economies move slowly. Retaliation from the US-led coalition following the September 11th terrorist attacks could severely disrupt economic activity within the Middle East region.

Upside Scenario: Selected economies across the region continue long term structural economic adjustment and create favourable conditions for foreign investment, trade agreements and increased regional/international trade. Continued export agreements maintain stability in South Africa's automotive industry fostering further investment - despite local labour market problems and the ongoing crisis in neighbouring Zimbabwe. Continued confidence in South Africa would also further aid the rational development of an integrated national and international supplier industry.

Middle East & Africa - Region in Focus

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The “Upside Scenario” is, we believe, the most likely, as it confirms our scenario of a disciplined local economy, several new trade agreements (discussed later), and growing vehicle export programmes.

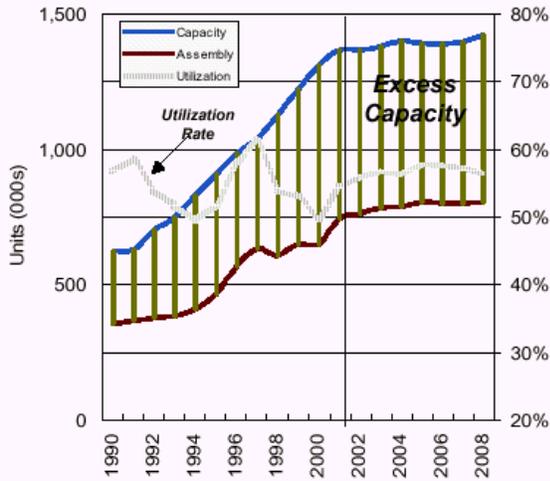
The volume forecast by PWC for South African production is, however, relatively flat between 2001 and 2008 at just over 400,000 (see chart below). We disagree with this, and believe it does not recognise the export potential from Toyota and other manufacturers, and also it is not in line with the Upside Scenario for the country.

The projections by CSM Worldwide Consultancy are more optimistic, with volumes growing steadily to 513,000 by 2005, up 44% on 2000's production levels, increasing South Africa's worldwide share by 0,2% .

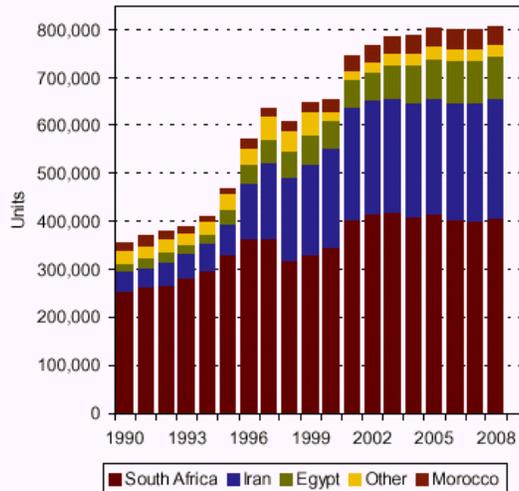
Chart: Africa and Middle East Market Outlook

Middle East & Africa Market Outlook

Middle East & Africa Light Vehicle Assembly & Capacity



Middle East & Africa Assembly by Country

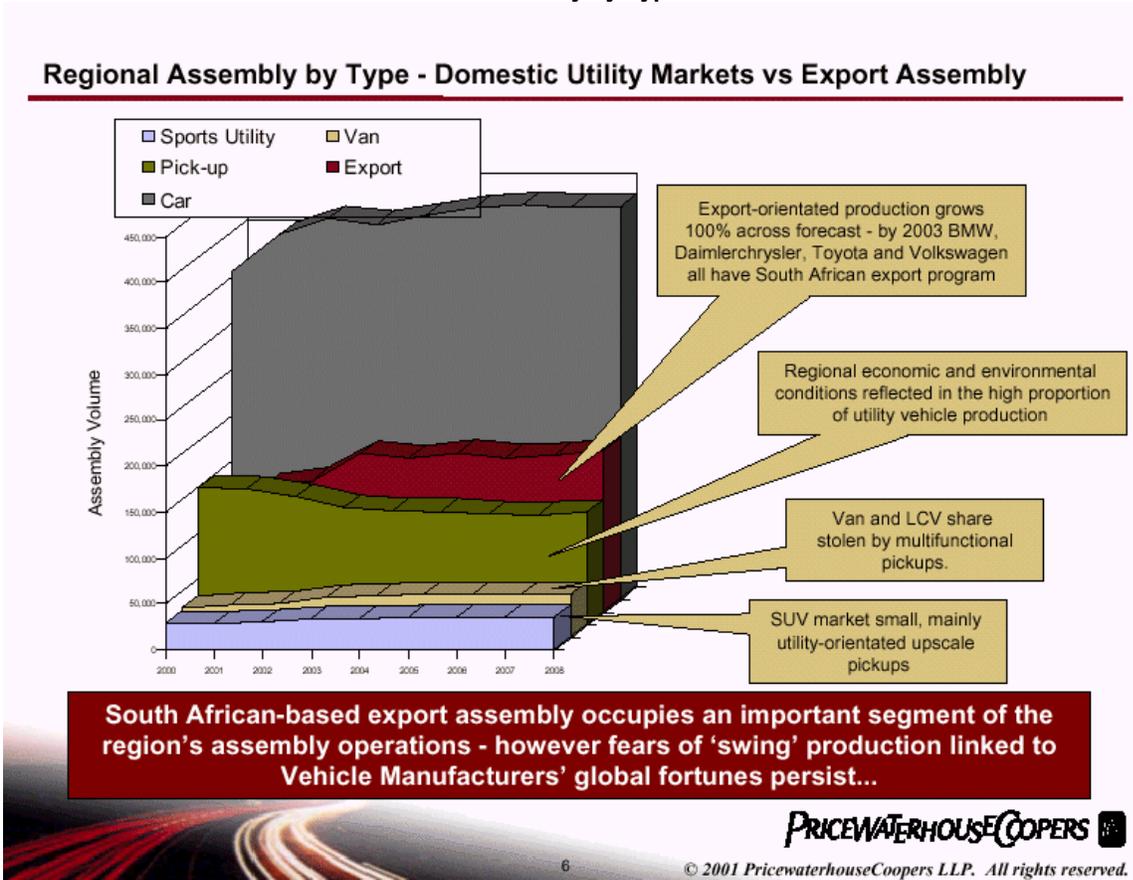


While the majority of regional light vehicle output will continue to be from South Africa, Iran's output is also expected to increase to meet growing demand over forecast period.



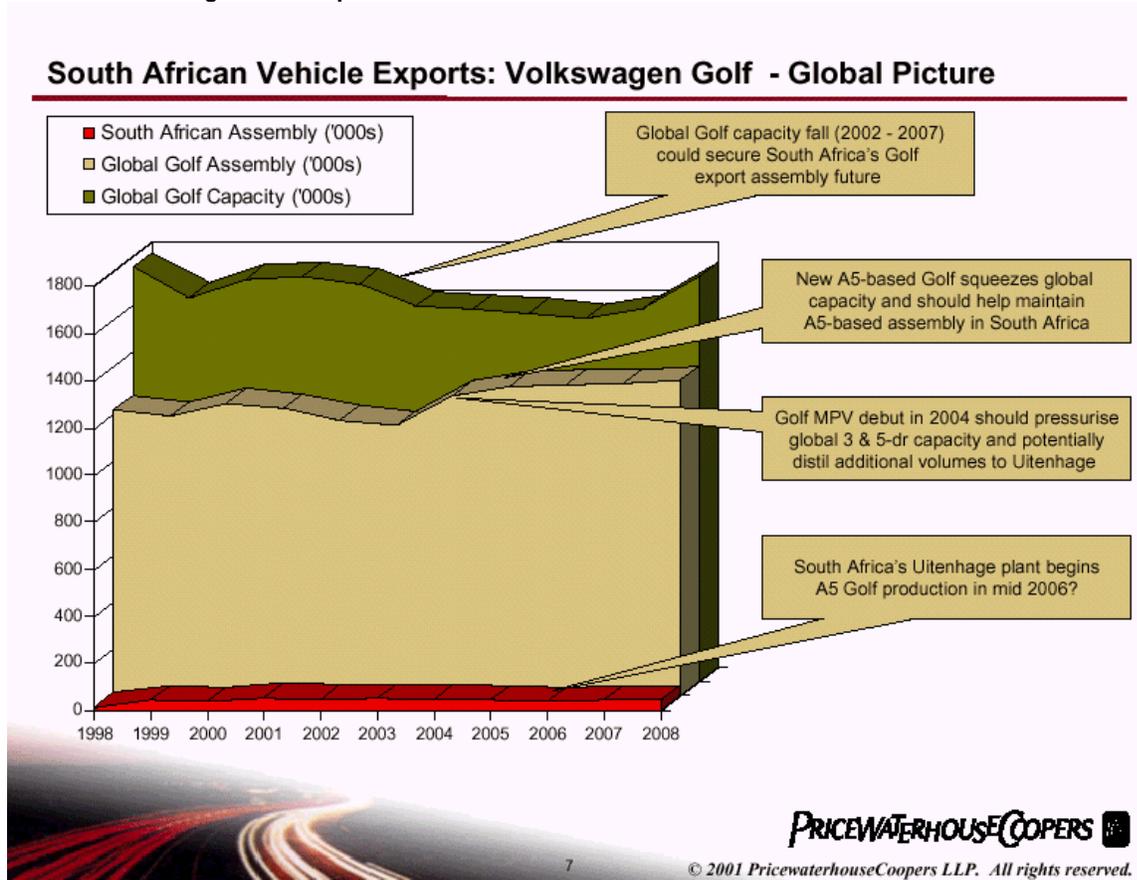
PWC's pessimism is partially explained in the next chart which expresses fears that some of the vehicle export programmes, described as "swing production", may be temporary in nature and may reduce as capacity is freed up in other countries following lower than expected volume achievements which would result from a global slowdown.

Chart: African and Middle East Vehicle Assembly by Type



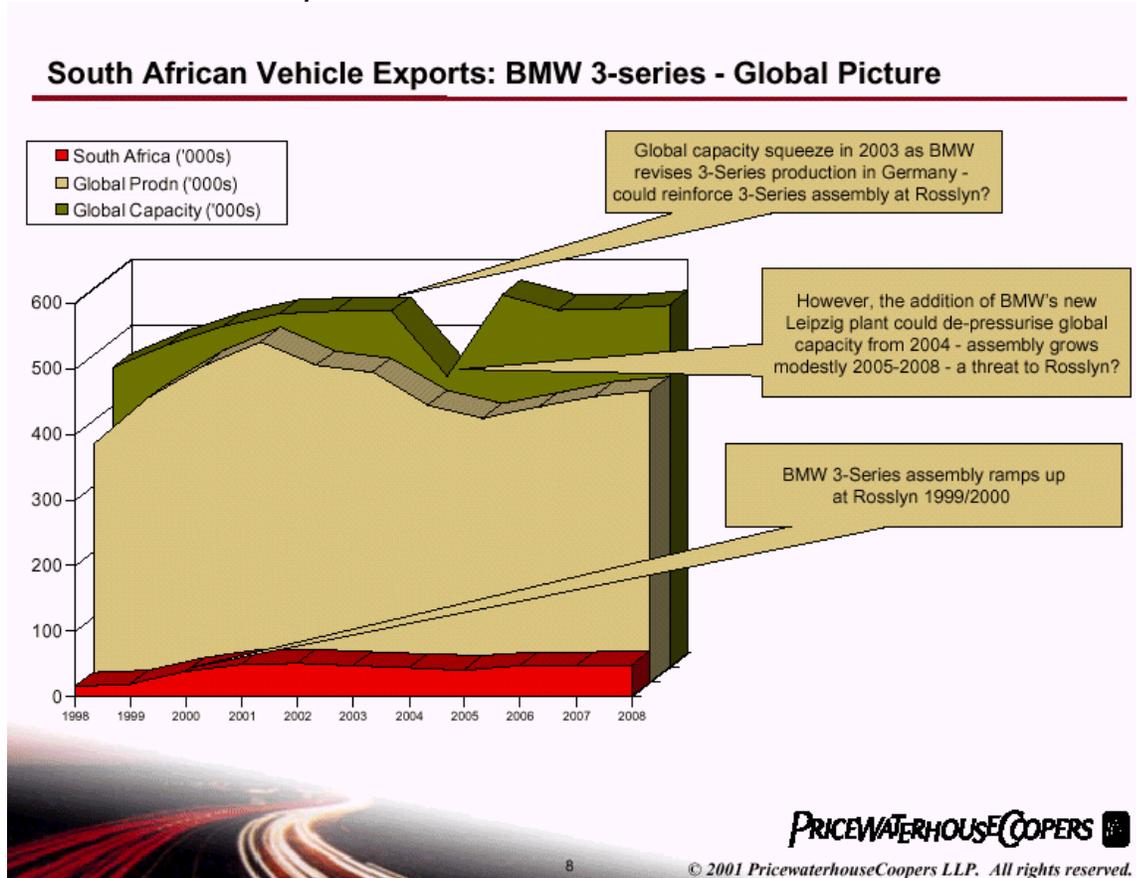
The next chart puts the size of the South African market into perspective by comparing VW's Golf export volumes with global production and capacity for Golfs. The present and projected world volumes range between 1.2 and 1.4 million – South Africa produces less than 3% of this.

Chart: Volkswagen Golf Exports in the Global Picture



The following chart provides the same comparison for the BMW 3-Series. The picture is slightly more impressive than that of the Golf, with South Africa expected to produce some 10% of the global demand for 3-Series.

Chart: BMW 3-Series Exports in the Global Picture



OEM VEHICLE RATIONALISATION

South Africa's automotive industry has grown over the last eight decades to become a robust supplier of products at the right quality and price, able to withstand considerable global pressure from imported competition. For such a small market of 500 000 vehicles sold per annum locally, we believe that the only option for OEMs to survive is to export or exit from the assembly of vehicles. Similarly, most component suppliers will need to be connected into the global sourcing networks of the major OEM's to achieve critical mass to compete globally. Since the introduction of the MIDP in September 1995, the new democratic government, bound by its commitment to the WTO to free up the economy, reduced tariffs and encouraged imported competition which shed some jobs but managed to avert massive lay-offs.

In order to encourage production rationalisation, an investment instrument was created to reduce the number of light vehicle platforms produced from 39 to a potential 15, thereby at least doubling the average volume per platform. The eight assemblers are all wholly owned subsidiaries (except Toyota) of foreign parent companies with the promise of increased investments as SA becomes a low cost producer and an emerging market already exceeding mature markets like Austria, Denmark, Ireland, Finland, Greece, Norway, Portugal, Sweden and Switzerland. Three German companies are leading the export drive with large export orders selling more than 70% of their respective model's production off-shore, namely BMW, VW and DCSA. But encouraging is the announcements by Ford, GM and Toyota to also export in large quantities to foreign markets.

It is expected that at least 500 000 vehicles will be exported by 2014, equalling 50% of total local production. This ratio compares favourably with countries like Japan, Korea and Spain, which export roughly 50% or more of their capacity.

The increased OEM export activity will force more integrated tier 1 suppliers to locate closer to these plants in supplier villages to facilitate JIT deliveries. As this global footprint spreads through the SA automotive industry, major opportunities for 2nd and 3rd tier suppliers will open up for local firms and FDI will increase.

The vast amounts of investments in technology transfer and plant modernisation will ensure that the competitiveness of local suppliers are enhanced, constrained only by large distances to off-shore markets and inadequate investment support from local, regional and national government. As the developed economies gravitate towards knowledge based industries capturing innovative and technologically advanced system providers, the vast majority of commodity converters will gravitate to low cost countries such as SA with its huge mineral and cheap energy capacity.

OEM/SUPPLIER RELATIONS

As the productivity improvements in local assemblers continue to secure more CBU exports, suppliers will be awarded more longer-term contracts as system suppliers but also as commodity converters. The two most powerful driving forces are the ability for importers of CBUs and CKD to rebate import duties based on local content exports of CBUs and components and the deterioration of the Rand against the traditional hard currency source country. In order for OEM's to be duty neutral and foreign currency balanced, sufficient exports needs to be generated to achieve such status. Increased levels of foreign investment will be directed at those component groups or niche CBUs that will swiftly allow an OEM to achieve a stable sustainable position. Radical changes to the MIDP could severely impact these relationships being developed over the last half decade and are likely be avoided at all cost. A golden opportunity is looming in the extension of the MIDP to 2020 as Minister Mpahlwa has mooted, which will send an even stronger message to the parent companies of the local OEMs.

One of the most interesting aspects of the exports of components is that the majority (at least 70%) are initiated and controlled by the OEMs and independent vehicle importers, not the component suppliers. The typical pattern is that an OEM would give a supplier a target price for the manufacture of a component in volumes sufficient for local use and exports. This target would be based on the European delivered price. This often provides a significant challenge for the local supplier, as their levels of automation are generally lower than in Europe, and therefore the costs higher. Recently, however, the strong Rand has hampered the achievement of world costs by the South African suppliers. Their ability to sustain current export levels, particularly in the face of a likely global automotive downturn and increased competition from other emerging markets, may be at risk. It is likely that certain types of components will succeed, while others are likely to cease being exported.

COMPONENT MANUFACTURER CONSOLIDATION/OPPORTUNITIES

As mentioned earlier, the local OEM's and the DTI have formed a Strategic Investment group which was designed to assist the assemblers towards consolidation and optimisation in the supplier industry and to encourage further beneficiation of generic raw materials. A summary of the presently identified opportunities is shown in the table below.

Table of Desired Strategic Investments for the South African Automotive Industry

	Priority	Local Suppliers	Recommended Investors	Job Potential	Export Potential
Generic Investments					
Aluminium castings	1	Gemtech (M&R)	Teksid (I)	med	med/high
Gravity Foundry	1	M&R Foundries, Salcast	Bruhl (G), Teksid (I), VAW (G)	med	med/high
Mini Steel mill (Cold Rolling)	1	Isacor	Thyssen (G),	med	in vehicles
Aluminium Forging	1	None	CDP (G)	med	Depends on cost structure
Component Groups					
Airbags	2	None	TRW(US), Autoliv (S), Takata-Petri (G)	med	low/med and in vehicles
Aircon compressors	1	none	Sanden (J), Denso (J), Calsonic (B)	med/high	Med
Centre console	1	Venture	SAL (F), Plasti- Omnium (F)	low/med	in vehicles only
Instrument panels	1	Various	SAL(F), Plasti - Omnium (F)	med	in vehicles only
Door locks	3	Baisch (Kiekert)	Kiekert (G), Meritor (US)	med/good	Good
Electric connectors & terminals	3	none	AMP (), Yazaki (J)	low	med/high
Electronic modules	2	Bosch (low volume), Shurlock	Bosch (G), Siemens(G)	limited/good	Good
Glass	1	Shatterprufe (Pilkington & Asahi)	St. Gobain (F), Pilkington (B), Splintex, SIV, Sekurit, Asahi (J)	med	Aftermarket and in vehicles
Lamps	2	Hella (limited)	Hella (G), Valeo (F), Bosch (G)	med	Aftermarket and in vehicles
New generation manifolds	1	none	Magnetti Marelli (I), TYC(Taiwan), Arvin (G)	med	High
Electric Power Assisted Steering Systems (EPAS)	1	Dorbyl (TRW)	TRW (US), GKN (US)	med/high	in vehicles only
Plastic component mouldings (bumpers)	2	Venture, Plasti Omnium	Visteon (MNC), Delphi (MNC), Reydell (US)	Low	After-market (Med/High)
Plastic Painting	1	Venture, AK Stoneguard	Visteon (MNC)	High	in vehicles only

Sub-Sectors

Paint

Paint Product Quality	2	Dulux (BASF, ICI, PPG), Plascon (DuPont)	Herberts (G), PPG (G), BASF (G)	low	on vehicles only
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Plastic Materials

Plastic materials	1	Plastomark (Hoechst)	Hoechst (G), Bayer (G), BASF (G)	low/med	in vehicles only
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Competence Building

Tool and die shop	1	August Laepple, Pico, Toyota, Surface Modelling & Machining	Notherfer (G)	highly skilled only	linked to plastics materials - med/high
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Natural Fibres

Door trim panels	1	Autoplastics (SAL), Pianfei/Strapazzini (now Lear), Gruppo Antonil (I)	SAL (F)	med	in vehicles only
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Other Investments

Rubber metal components	N/A	none	Lemforder (G)	med/high	High
Springs	N/A	Supreme (Krupp)	Krupp Hoesch (G), Allevard (B), Muhr & Bender (G)	med	low and in vehicles
Transmissions & Transaxles	N/A	none	Getrag (), ZF (G)	med/high	med/high
Aluminium castings (HP)	1	Belmec	Almech (I), Bellessex (SA)	med	med/high

While only a few of these may eventually invest in South Africa, a comparison with the projected component sector growth identified by the EIU and [reported earlier](#) throws up some real opportunities.

These would include in particular:

- Airbags, particularly curtain-type used at the side
- Air-conditioning systems
- Headlamps
- Transmissions

E. THE MIDP AND POTENTIAL IMPLICATIONS FOR INVESTMENTS

IMPACT OF THE MIDP TO DATE

The Minister of Trade and Industry in his statement in TISA's CSP supports the industry as follows:-

Foreword By The Minister

We have discovered that formulating a sector development strategy is not a simple undertaking. It has been an enriching experience, but one that has once again made us aware of our own limitations in delivering against the National economic policy goals and objectives outlined in the Micro-economic Reform Strategy of 2002.

Priority sectors¹ matter to South Africa. They account for over twenty-two per cent of the Gross Domestic Product, employ twenty-three percent of South Africa's total employment, and contribute over fifty-five per cent to South Africa's foreign exchange earnings. Therefore, the success of the priority sectors is critical to our economy and a better life for all.

The changing nature of the relationship between government and stakeholders in priority sectors means that we need to shift the dialogue from lobby to understanding and synergy. What we are experiencing through the Customised Sector Programme development and sector summit processes is a powerful and encouraging new way of working together, thus giving concrete content to the often rhetorically touted partnership between government and stakeholders. There are bound to be problems as we grapple with this learning. We are, however, excited by the prospect of jointly tackling South Africa's economic challenges.

The fact-driven process employed within Customised Sector Programme, in our experience, represents the first attempt at generating a common understanding, rooted in objective analysis around key strategic challenges and opportunities facing the South African priority sectors, that leaves the path open to move 'beyond planning to action', jointly and/or independently, for all parties, but based on a common vision.

This document outlines our sector development strategy for increasing competitiveness, exports and investments as well as employment and equity, in the priority sectors of South Africa. On the basis of objective analysis, strategic themes over the next five years have been identified. Each strategic theme demands government and other stakeholders to jointly seek the key action programmes and related interventions that must be implemented to deal with key strategic challenges facing the priority sectors. This sector development strategy is neither hard nor fast nor a formula for instant success. Instead, we offer it as the basis for continuing to forge constructive engagement with stakeholders – a partnership based on best practice that must be effective at the national, provincial and sectoral levels.

Long standing challenges of competitiveness, exports and investments as well as employment and equity will not be solved overnight. However, concrete time frames to achieve our aim have been put firmly into place. Maximum cooperation from our stakeholders is a key condition to achieve our goals within this time frame. Firmer benchmarks against which to measure and report on progress have also been developed.

There are mistakes the government should avoid. Any attempt to manipulate the exchange rate would put our hard-earned macroeconomic stability at serious risk. Whilst we understand the strength of Rand relative to the US dollar makes life difficult for our exporters, in practice we have to recognise that it is not possible for the Reserve Bank to pursue an exchange rate target at the same time as an inflation target.

Likewise, we reject solutions based on attempts to defend the economy from fair competitive pressures through restriction on trading with the World or subsidies to domestic companies. Such actions would detract from the market framework, which brings major competitiveness improvements. They would also run counter to the World Trade Organisation (WTO) and the benefits it brings to our exporters. As the opposite side of the same coin, we take robust action against countries that seek to deny our firms

fair access to their markets. That's why we, in conjunction with other developing countries, fought strongly for a new world trade round in Doha.

Although Customised Sector Programme is nationwide, there is an important role for the provinces, we recognise that provincial leadership is essential in creating dynamic provincial economies and closing the gap between and/or within provinces. Hence the importance we attach to the provincial economic departments.

This document has been developed on the basis of discussions within the Customised Sector Programme Project Team that we established at the beginning of the year, including the positive work of the partnership forged through the inter-Government and external stakeholder workshops. Customised Sector Programme must deliver real outcomes, underpinned by real commitment from all stakeholders. Above all we hope that this sector development strategy and programmes will form the basis for an even stronger partnership and more effective action in support of priority sectors in South Africa.

MANDISI MPAHLWA, MP

MINISTER: TRADE AND INDUSTRY

The MIDP, introduced in September 1995 has had a profound affect on the automotive industry through it's gradual phased support limits as is reflected below by the reduced tariff protection over time.

Year	CBU Duty Light Vehicle	CKD Duty	Small Vehicle Incentive Additional DFA	Qualifying Value of Eligible Export Performance	Components, heavy duty vehicles & tooling exported : CBU light vehicles imported	Qualifying Precious Metal Content in Catalytic Converters
2003	38,0%	29,0%	WITHDRAWN	94%	100:60	40%
2004	36,0%	28,0%		90%	100:60	40%
2005	34,0%	27,0%		86%	100:60	40%
2006	32,0%	26,0%		82%	100:60	40%
2007	30,0%	25,0%		78%	100:60	40%
2008	29,0%	24,0%		74%	100:60	40%
2009	28,0%	23,0%		70%	100:60	40%
2010	27,0%	22,0%		70%	100:60	40%
2011	26,0%	21,0%		70%	100:60	40%
2012	25,0%	20,0%		70%	100:60	40%

MIDP Regulations to 2012

In addition, the Productive Asset Allowance grants a 20% duty credit spread over 5 years based on Fixed Assets investments.

LIKELY CHANGES TO THE MIDP

The Minister of Trade & Industry has agreed to the extension of the programme from 2007 to 2012 in order to provide a clear framework within which the OEM's and component manufacturers could take long term investment decisions. It is expected that the current review of the programme will be announced around the middle of 2006. The industry is busy preparing a proposal to the Minister by the end of 2005 in order to provide a framework for the debate with labour and government aimed at achieving the extension within the basic architecture of the programme as discussed above. The previous mid term review changes were quite onerous and saw the demise of the Small Vehicle Incentive, a continued reduction in duty protection and a drastic phase down in the required import: export ratio as well as the PGM qualifying value in catalytic converters.

Given the importance of the automotive industry to SA as a provider of economic growth through exports, new FDI and job stability/growth, it is crucial to build on the recent successes and encourage further integration of the industry in global sourcing networks of the global OEM's and tier 1, 2 & 3 suppliers. In order to achieve this common objective the programme could look essentially the same with the changes motivated as follows.

DUTY REDUCTION – In line with our WTO commitment to reduce protective tariffs we foresee pressure for a gradual phase down of up to 1 % annually in both CBU and CKD duties. However, in view of the fact that the implications of the considerable duty reductions which took place from 2001 to 2007 will only become evident in a few years time, it is likely that certain parties, in particular the industry and trade unions, will request that duties be frozen at 2007 levels.

DUTY FREE ALLOWANCE – In order to encourage and preserve continued assembly of passenger and light commercial vehicles we believe that the DFA should be maintained to avoid an exodus of assemblers to CBU imports on the back of lower import tariffs. The DFA benefits only local OEMs and provides an incentive for local manufacture. With the continuing reductions in tariffs as well as the phasing down of the export benefits, there is a risk that some OEMs might decide to cease local production in favour of imported vehicles. However, the component supplier industry will resist increases in DFA, seeing it as reducing the incentive to increase local content. Should tariffs on imported vehicles and components remain at 2005 levels, it is likely that the DFA will also be unchanged.

IMPORT: EXPORT RATIO AND QUALIFYING VALUE OF EXPORT PERFORMANCE – The reduction from 100% to 70% of the value of exports as import credits could possibly have unforeseen effects. As these will only become evident in future, it is too early to propose that higher levels be restored. No change is therefore likely to these ratios.

However, in the case of CBU vehicle complementation the industry is adamant that this should be retained at 100% for the following reasons:

- Exports of CBU vehicles benefit a wide range of component suppliers as well as OEMs
- The local content of CBU exports is significantly lower than the content of component exports and, for example, at a 50% CBU export local content, two vehicles would have to be exported to enable one to be imported.

Any reduction in the complementation ratio of vehicle exports would make these less attractive and could jeopardize their continued growth.

PRODUCTIVE ASSET ALLOWANCE (PAA) – The potential increased globalisation of the local industry will increase the volumes per model platform produced which will encourage plant modernisation and further production rationalisation from the current 25 platforms to an estimated 15 platforms over the next 5 years. Since the parent OEM's have several options to locate to emerging low cost countries closer to markets in Europe, Japan and North America, the attraction of suitable investment allowances often has a positive impact on the project IRR's. SA needs to increase its offering in this regard to a total of 45% as the governments of emerging countries are also

chasing the same FDI objectives as the SA government. This was the reason for the introduction of the PAA, but we believe more may be required. In addition we expect that the PAA may be de-linked from production rationalisation in future as most OEM's have achieved this objective by 2005 anyway and the need for rationalisation linkage would have been satisfied. The PAA's future role would be to encourage plant modernisation and attracting more global tier 1, 2 and 3 suppliers to SA. Consideration is likely to be given to increasing the PAA percentage to compare favourably with SA's competing countries.

MEDIUM AND HEAVY COMMERCIAL VEHICLES

Since these vehicles are considered to be a capital input cost to the economy, we believe that the rate of duty on CBU imports will remain at 20% nominal and only on tyres imported a 15% protective tariff. However, large scale investments in more localisation needs to be incentivised via a PAA and DFA which can be off set against import duties. The exports of M&HCV components and CBU's will still be allowed under the MIDP in future. In addition, trailers and bodies currently excluded from the MIDP should be incentivised in future.

The regulations for the MIDP to 2012 will only be finalized by government during 2006. However we have attempted to predict the direction of these changes.

Possible MIDP Regulations to 2012

Year	CBU Duty Light Vehicle	CKD Duty	DFA	Qualifying Value of Eligible Export Performance	Compo- nents, heavy vehicles & tooling exported : CBU light vehicles imported	Qualifying Precious Metal Content in Catalytic Converters	PAA as % duty credit to import CBU (De-linked from rationalisation of platforms)
2007	30.0%	25.0%	27%	78%	100:60	40%	45%
2008	29.0%	24.0%	27%	74%	100:60	40%	45%
2009	28.0%	23.0%	27%	70%	100:60	40%	45%
2010	27.0%	22.0%	27%	70%	100:60	40%	45%
2011	26.0%	21.0%	27%	70%	100:60	40%	45%
2012	25.0%	20.0%	27%	70%	100:60	40%	45%
ALTER- NATIVE	THERE MAY BE NO CHANGES AFTER 2012						

CALCULATION OF THE EFFECT OF CHANGES

<u>Export activity required versus 2001</u>	<u>2007</u>	<u>2012</u>
An OEM (45% LC) exporting components	1.9	2.1
Cars imported exporting components	2.3	2.9
Cars imported exporting Cars assembled	2.1	2.5
Component importer exporting components	2.1	2.5
Cars imported exporting Catalytic convertors	3	3.8

Assumptions:-

Assembly local content = 45%; Component local content = 75% ; PGM content in catalysts 60 %.

Various opportunities and permutations can be followed to participate in the local market as assemblers, independent importers of cars, CKD importers, component exporters , etc. The above table indicates what could be expected as importers and exporters to achieve duty neutrality.

An assembler will be able to rebate all CKD import duties using the DFA and component export option. The above changes to the MIDP will force them to export 1.9 times as many components by 2007 and 2.1 times by 2012, compared to 2001. **An independent car importer** has no DFA and needs to achieve exports of components of 2.3 times in 2007 and 2.9 times in 2012. **A car assembler importing cars** and exporting cars needs to export 2.1 times as much by 2007 and 2.5 times by 2012. **A car importer**, with no DFA, exporting catalytic converters needs to export 3 times as much by 2007 and 3.8 times by 2012.

POSSIBLE FUTURE IMPACT OF CHANGES ON INDUSTRY

In an attempt to “model” what the future scenario will be to accommodate the changes above, external factors such as world growth rates, local GDP growth, and local currency devaluations needs to be taken into account. Production is directly related to local market growth, export growth and import penetration.

Whilst the government has achieved some great success in macro economic terms since 1994, SA is classified as one of the emerging markets that are constantly plagued by some form of economic problem impacting on its growth objective of 6% as stipulated in the GEAR policy framework.

Our view from an automotive perspective is that we have the MIDP and a growing economy that is increasingly linked to the global sourcing networks of the major players. As we increase our competitiveness as a low cost modern economy, export sales will probably continue to grow, imports will be increasing albeit at a slower rate than exports due to currency devaluations and the modest growth rate of the local market. The table below is an attempt to predict what could realistically be expected in the local industry.

Year	Domestic Production of vehicles	Imports Vehicles (all units)	Exports Vehicles (all units)	Exports Comp. (Rb)	Trade Deficit (Rb)	Employment			Investment (Rb)
						Component	Retail	Naamsa	
1995	388 442	27 289	15 764	3,3	(12,2)	60 800	178 000	38 600	0,8
1996	385 252	47 377	11 553	4,1	(14,1)	64 100	180 000	38 600	1,2
1997	361 316	57 528	19 569	5,1	(10,6)	64 300	180 000	37 100	1,3
1998	310 333	66 373	25 896	7,9	(9,8)	64 400	170 000	33 700	1,3
1999	325 222	60 269	59 716	9,7	(8,0)	64 700	175 000	32 000	1,5
2000	356 250	66 413	68 031	12,6	(9,7)	67 600	180 000	32 300	1,6
2001	406 149	84 673	108 293	18,6	(8,0)	69 700	182 000	32 700	2,1
2002	404 441	84 049	125 306	22,9	(10,1)	72 000	185 000	32 370	2,7
2003	421 335	87 926	125 661	21,3	(9,1)	73 000	191 000	31 700	2,3
2004	455 052	136 975	110 507	21,7	(18,8)	76 900	192 000	33 000	2,2
2007*	646 500	183 300	205 500	26,0	(10,0)	77 500	195 000	34 000	6,0
2014*	1 000 000	400 000	500 000	40,0	(0)	82 000	200 000	38 000	10,0

Table of Key statistics 1995 - 2014

Source : TISA

It is clear that the DTI would like to see a growing competitive automotive sector as is indicated by the above key statistics forecast to 2014.

Given the slow growth rates predicted for the developed economies, it is encouraging to see such significant growth rates for SA's emerging automotive industry. Alongside this growth we will need capacity upgrades, technology partnerships through M&A from the global major players and upliftment of skills at a scale not seen in any other sector of the SA economy.

Herein lies the opportunity for ELIDZ to make the future changes and to market ELIDZ as an investment destination equal to the best the world can offer.

F. IMPACT OF SA'S FREE TRADE AGREEMENTS ON THE AUTOMOTIVE INDUSTRY

EU FTA

DETAILS OF THE SA – EUROPEAN UNION AGREEMENT ON ADDITIONAL PREFERENCES FOR AUTOMOTIVE PRODUCTS

During the course of negotiations in Brussels between the European Commission and South Africa, agreement was reached which involves the following concessions by both parties, namely –

- The EU agreed to transpose the GSP benefits into the trade, development and cooperation agreement with effect from 1st January, 2006. This averts the GSP graduation and the potentially higher duties on SA exports into the EU.
- The EU agreed to eliminate, over a period of five years, duty on cars exported by South Africa into the EU.
- The EU agreed to eliminate duties on all other automotive products effective 1st January, 2006.
- The EU agreed to drop its insistence on a preferential duty on original equipment components into South Africa and also to drop the duty free quota proposals.
- South Africa agreed to a 7% duty preference on cars starting 2006 and phased in at an additional 1% per annum.
- South Africa accepted further liberalisation on certain aftermarket components.
- South Africa agreed to an additional 3% preference on trucks and buses (not light commercial vehicles), phased in at 1% per annum starting in 2006.

The following SA and EU duty regime will apply from 2006 through 2012 -

	S A General Tariff on CBU's		S A Tariff on EU CBU's			EU Tariff on SA CBU's	
	Cars & LCV's (MIDP)	Trucks & Buses (MIDP)	Cars	LCV's	Trucks & Buses	Cars	Commercials
2005	34%	20%	34%	29%	15%	6,5%	0% - 22%
2006	32%	20%	31%	27%	14%	5,0%	0%
2007	30%	20%	28%	25%	13%	4,0%	0%
2008	29%	20%	26%	24%	12%	3,0%	0%
2009	28%	20%	24%	23%	12%	2%	0%
2010	27%	20%	22%	22%	12%	0%	0%
2011	26%	20%	20%	21%	12%	0%	0%
2012	25%	20%	18%	20%	12%	0%	0%

Additionally, exports of South African automotive components into the EU will be duty free with effect from 1st January, 2006.

The rules of origin, as per the agreement, apply to all trade between South Africa and the EU and is pegged at 60%. Components sourced from the EU will be counted at part of the 60%.

NAAMSA has adopted the following position for public consumption –

- The agreement will facilitate and strengthen increased trade between South Africa and the EU and should benefit both the EU and SA automotive industries.
- The progressive reduction in tariffs into the EU will enhance the competitiveness of South African automotive products into one of the world's major markets, particularly those exports that had become marginally viable due to the stronger Rand. Currently about 51% of South Africa's total exports of components and vehicles are destined for EU countries.
- The agreement will provide South African exporters with long term certainty and a stable base from which to plan future export projects.

AGOA

The African Growth Opportunity Act promulgated in December 2000, offered SA exporters of automotive vehicles and components an opportunity to export to the USA duty free as per the categories listed below. This is a non-reciprocal agreement that also protects the integrity of the MIDP in the period up to 2008. These concessions will ensure that parent OEM's utilise the SA assembly and OE component plants to export more from SA to the USA. Already some German assemblers are using this opportunity to increase the local capacity utilisation of their plants.

Again as we suggested previously, ELIDZ as a Free Trade Zone, could position itself in a manner that will be conducive to attracting a company like GM to develop an investment opportunity on one platform for export to the USA thereby saving duties up to 25% on these exports.

Likewise, various tier 1 suppliers could be attracted in a close proximity to such an assembly plant similar to the DCSA plant in East London.

US HS	USA GENERAL		
SUBHEADING NO.	RATE OF DUTY	AGOA RATE*	PRODUCT
3926.30.50	5,3%	Free	Fittings for furniture, <u>coachwork</u> or the like
3926.90.55	5,1%	"	V-belts of plastics containing textile fibres
3926.90.59	2,4%	"	Belts and belting (except V-belts) of plastics
4010.21.30	3,4%	"	Transmission V-belts of vulcanised rubber, etc.
4010.22.30	3,4%	"	Transmission V-belts of vulcanised rubber, etc.
4010.23.50	1,9%	"	Endless synchronous transmission belts of
4010.24.50	1,9%	"	vulcanised rubber, etc.
4010.29.10	3,4%	"	Transmission belts of vulcanised rubber of
			trapezoidal cross section, combined with textile
			materials
4010.29.50	1,9%	"	Belting of vulcanised rubber
7320.10.60	3,2%	"	Iron or steel leaf springs and leaves therefore
			suitable for motor vehicles suspension other than those with a GVW
			over 4 metric tons
8302.30.60	3,5%	"	Base metal (other than iron/steel/aluminium/zinc)
			mountings, fittings and similar articles suitable motor
vehicles and base metal parts thereof			
8482.10.50	9,0%	"	Ball bearings other than those with integral shafts
8482.20.00	5,8%	"	Tapered roller bearings including cone and tapered

8483.20.80	4,5%	"	roller assemblies
8483.30.80	4,5%	"	Housed bearings (including ball or roller bearings)
8483.90.30	4,5%	"	Bearing housings nesoi: plain shaft bearings
8483.90.70	5,5%	"	Parts of bearing housings: and plain shaft bearings
8701.20.00	4,0%	"	Parts of articles of subheading 8483.20
8703.10.10	2,5%	"	Road tractors for semi-trailers
			Motor vehicles specially designed for travelling on snow
Motor cars and other motor vehicles for the transport of persons with spark ignition internal combustion reciprocating piston engines:			
8703.21.00	2,5%	"	with cylinder capacity not over 1000 cc
8703.22.00	2,5%	"	with cylinder capacity over 1000 cc not over 1500 cc
8703.23.00	2,5%	"	with cylinder capacity over 1500 cc not over 3000 cc
8703.24.00	2,5%	"	with cylinder capacity over 3000 cc
			with compression ignition internal combustion reciprocating piston engine
8703.31.00	2,5%	"	with cylinder capacity not over 1500 cc
8703.32.00	2,5%	"	with cylinder capacity over 1500 cc not over 2500 cc
8703.33.00	2,5%	"	with cylinder capacity over 2500 cc
8703.90.00	2,5%	"	other than with spark or compression ignition reciprocating piston engine, nesoi
Motor vehicles for the transport of goods with compression ignition internal combustion piston engines –			
8704.32.00	25%	"	with GVW not over 5 metric tons
8704.22.10	4%	"	cab chassis with GVW over 5 but not over 20 metric tons
8704.22.50	25%	"	other than cab chassis with GVW over 5 but not over 20 metric tons
8704.23.00	25%	"	with GVW over 50 metric tons
Motor vehicles for the transport of goods with spark ignition internal combustion reciprocating piston engines –			
8704.31.00	25%	"	with GVW not over 5 metric tons
8704.32.00	25%	"	with GVW over 5 metric tons
8704.90.00	25%	"	Motor vehicles for the transport of goods other than with compression or spark ignition reciprocating piston engines
8706.00.03	4%	"	Chassis fitted with engines for motor vehicles for the transport of goods of 8704.21 or 8704.31
8706.00.05	4%	"	Chassis fitted with engines for motor vehicles of 8701.20, 87.02 and 87.04 (except 8704.21 and 8704.31)
8706.00.15	2,5%	"	Chassis fitted with engines for motor vehicles for the transport of persons of 87.03
8706.00.25	1,6%	"	Chassis fitted with engines for the motor vehicles of 87.05
8707.10.00	2,5%	"	Bodies (including cabs) for motor vehicles for the transport of persons of 87.03
8707.90.50	4,0%	"	Bodies (including cabs) for motor vehicles (Other than tractors for agricultural use) of headings 87.01 to 87.05 (except 87.03)
8708.92.50	2,5%	"	Parts and accessories of motor vehicles of 87.01 nesoi. and 87.02-87.05 mufflers and exhaust pipes

In addition to the AGOA concessions listed above, a broad range of South African automotive products enjoys duty free access into the United States as part of the generalised system of preferences (GSP) dispensation. Importantly, products enjoying GSP zero duty rating were previously subject to annual review. It has now been confirmed that, in the case of AGOA eligible countries, which includes South Africa, the GSP benefits will apply through 2015. This provides significant scope and certainty, from a planning and investment perspective, for South African exporters.

Table: Major Duty-free automotive components subject to GSP

- Bumpers and parts
- Body stampings
- Seat belts and airbags
- Door assemblies
- Gearboxes and axles
- Brake linings, mounted
- Brakes and servo brakes and parts
- Road wheels and parts
- Shock absorbers
- Radiators
- Clutches and parts
- Steering wheels and columns
- Steering boxes
- Suspension parts, shock absorbers
- Rubber mountings
- Half shafts and drive shafts

MERCOSUR

The SA government and Mercosur have signed a memorandum of agreement whereby the intention is that a FTA will be concluded in the next year or so. As a large market that produces six times more vehicles than SA, Mercosur is an attractive market for SA exporters. The problem is that due to larger scale economies their manufacturers are generally producing at a significant cost advantage over their SA counterparts, many of whom also operate in SA. Fiat, GM and VW are the market leaders in Brazil, which is by far the largest car market in Mercosur.

In order to protect the integrity of the MIDP, NAAMSA and ANFAVEA (Brazil automotive manufacturers association) have agreed to try to develop a bi-lateral agreement outside of the MIDP that could be a quota system similar to the agreement Brazil has with Mexico. The aim of such an agreement would be that a limited-volume preferential-duty trade balance between the two countries be explored in order to increase trade flows both ways. During 2000, Brazil had a favourable automotive trade balance of R 500 million with SA and the main objective would therefore be for Brazil to source more automotive products from SA to achieve equilibrium first before SA needs to increase sourcing from Brazil. From a practical point of view, Mercosur is a Left Hand Drive market, which does make it difficult for assemblers in both countries to “swap” vehicles. The focus will therefore be on components. Since both GM and VW are presently trading with Brazil, the opportunities for investment in the Port Elizabeth-ELIDZ region are good.

INDIA

The SA and Indian governments have also committed themselves to develop a FTA. This should suit SA more as the market sizes are much the same and India is a Right Hand Drive market, which makes vehicle exchange programmes much easier. India also has a high level of protection on automotive products and historically a less-developed auto industry. Tariffs recently were in excess of 90% , although these will reduce as part of their WTO commitments. SA has effectively little duty protection if the drawback facility in the MIDP is used. A strong case could therefore be developed for closer relationships. Two of India’s automotive giants, TATA and Mahindra & Mahindra entered the passenger car, light commercial vehicle and SUV market with fully imported but low cost products.

Many SA assemblers are also represented in India through parent or associated companies and a carefully constructed FTA could be beneficial to both countries. The result would be additional investment by local and Indian component companies to manufacture products for the SA and export markets.

UNDERLYING PRINCIPLES OF FTA's

The SA government's objectives of the MIDP, introduced in September 1995, are aimed at the development of an internationally competitive and growing industry that will be able to :-

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

These national objectives are to be achieved by:-

- Encouraging a phased integration into the global automotive industry;
- Increasing the volume and scale of production through the expansion of exports and gradual rationalisation of models produced domestically;
- Encouraging the modernisation and upgrading of the automotive industry in order to promote higher productivity and facilitate the global integration process.

The above objectives the MIDP will be assisted by FTA's. Market dominance and technology sharing seem to be the main driver for the recent M&A activity and this is good news for SA assemblers who have already achieved a low cost assembly base. FTA's also strengthen trade flows between non-traditional trading partners such as SA, Mercosur and India and further develops trade flows between SA, USA and EU countries. For this reason, it is necessary to ensure the delicate balance of the MIDP should not be disturbed by the reduction in nominal duties in isolation. It would be far better to promote the convenience of increased duty free access to SA's small market through the IRCC duty draw back facility (which in itself encourages exports and imports between trade partners) in exchange for duty free access to the other partner's market.

Our view is that FTA's are regimes that carefully set in place a set of rules with the aim of increasing trade flows between trading partners and are based on fair market sharing principles. Larger and saturated markets offer no growth opportunity to smaller developing markets if the former dominates the latter. The basis on which such FTA's should be constructed would be to focus on developing core competencies in both countries. It makes sense for SA which is richly endowed with minerals and most raw materials and lowest cost energy provider to "absorb" more energy intensive components for global consumption and for developed countries with a high cost base to become technology providers to the translocated local converters of raw materials owned by them. Manufacturing is a very expensive exercise and if one looks at the low margins made by assemblers and component manufacturers, it makes sense for the large international corporations to continue to be compensated via technology transfer royalties mostly around 5 to 6% of turnover in the local subsidiary.

The opportunity to transplant a non-viable operation to SA as part of an FTA therefore becomes more appealing in their global strategy.

ANALYSE THE STRATEGIC APPROACH BY OTHER IDZ's TO ATTRACT INVESTMENTS

The AIDC was tasked to do an analysis on the impact of IDZ legislation on the MIDP and vice versa. The ELIDZ also contracted the services of KPMG to advise possible legislative changes in the Common Customs Area. A full AIDC report on these important matters follows below. It is our understanding that the Enterprise Organisation in the DTI are now tasked to finalise the CCA legislation and that any delays will greatly hamper ELIDZ's ability to market to second tier suppliers in the automotive industry.

Complimentary Use of MIDP & IDZ for Automotive Suppliers in the East London IDZ

Proposal No: INI 107

Phase 3

Concluded 01-06-2005

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Executive Summary

IDZ operators and their potential foreign automotive investors could find themselves in a catch 22 situation between incentives offered by government for Industrial Development Zones (IDZ's) and Import Rebate Credit Certificate (IRCC) available through the Motor Industry Development Programme (MIDP).

Industrial Development Zones are areas designated by government that aim to uplift the economy by providing incentives that favours exporters. IDZ legislation will allow companies that establishes in an IDZ to apply for special benefits or incentives offered by the Republic of South Africa. In order to qualify for incentives provided through specific legislation, companies must operate from within a designated area within an IDZ. Legislation declares the so called "Customs Secured Area" (CSA) as the "duty-free" and "VAT-free" area within an IDZ and shall be deemed to be an "export country" for customs purposes (extra-territoriality of CSA).

When the automotive sector investigates this option in greater detail, they find the following problem. Manufacturers and exporters of vehicle components are supported through incentives provided within MIDP. A significant incentive under MIDP is the Import Rebate Credit Certificate (IRCC) and these credits are based on local content value of goods that is exported. The IRCC credits are used to offset duties on the import of specified materials. However, to benefit from this IRCC incentive, companies must adhere to two main rules. Firstly, they must export from within the Customs Union and secondly, they need to export local content value.

Manufacturing in an area outside the Customs Union doesn't create any local content.

Consequently, operators of IDZ's can therefore not offer the opportunity to their potential automotive investors to locate within their prime area, the "duty- and VAT-free area". This is a major weakness for IDZ's wishing to attract automotive investors within a globally competitive environment.

In the meanwhile government institutions have published a new definition for the IDZ's "duty-free and VAT-free" area. This is now deemed as "Customs Controlled Areas" (CCA) and is no longer seen as outside the Customs Union. This is a first step towards the goal of solving the contradiction between IDZ and MIDP.

The concept of locating automotive suppliers within a CCA of an IDZ while benefiting from both MIDP and IDZ incentives should be confirmed and implemented. Therefore the IDZ and MIDP laws and regulations should be reviewed and a new legal interface for the complimentary use of these incentives should be created.

History

The 6th of December 2004 marks the date of a meeting that was held at DCSA with the topic of: "Possible Collaboration Opportunities between DCSA and ELIDZ". DCSA invited the ELIDZ to explain in detail what their incentives for automotive suppliers are and what the ELIDZ concept of an Automotive Supplier Park contains.

Within the presentation the following was presented as a collaborative approach between ELIDZ and DCSA:



The approach in these days was to offer DCSA a comprehensive solution for their whole supply chain with regard to their logistics planning for the new W204 series. The solution contained the following elements:

- I-Park solution for their JIS/JIT suppliers inside DCSA
- Automotive Supplier Park (ASP) inside Zone 1a of the IDZ

And to overcome potential sequencing problems within further JIT/JIS delivery a

- Supply Centre next to DCSA.

The idea of locating the ASP within the duty-free zone of the ELIDZ is seen as an additional and new incentive that could be utilised by the automotive industry.

The reaction on the idea of 'Organizing MIDP and IDZ in one area' however, was a disaster. Strong resistance from the automotive sector came to light and some DCSA managers verbally said: **'You can not locate an automotive supplier in an IDZ. Locating automotive suppliers inside an IDZ makes only business sense if they can run under MIDP. But that is not the case.'**

If this statement turns out as true the whole business idea of attracting automotive suppliers to invest into the Automotive Supplier Park of the ELIDZ would be a farce. It is due to this reaction that investigations regarding the complimentary use of IDZ and MIDP incentives were initiated by the AIDC.

Basic Information about MIDP & IDZ

What is the Motor Industry Development Programme (MIDP)?

The Motor Industry Development Program (MIDP) is an initiative of the Department of Trade and Industry (DTI) with the objectives of:

- Developing an internationally more competitive South African automotive industry,
- Providing sustainable employment through increased production,
- Making a greater contribution to economic growth and achieving an improved sectoral trade balance.

The current laws and regulation of the Motor Industry Development Program (MIDP) are the elements of Phase VII of the “Local Content Programme for the Motor Industry” and published by government in the report “Revised Customs Dispensation for The Motor Industry.”

The Motor Industry Task Groups was appointed in 1992 by the former Minister of Trade and Industry to advise government on long and short-term strategies for the future development of the Motor Industry. This investigation was considered necessary as a result of developments/changes which occurred locally and abroad since the implementation of Phase VI of the Local Content Programme for the Motor Industry in 1989. Phase VI, which measures local content by value, was preceded by various phases of the local content programme as from 1960, during which period local content was measured in terms of mass. As a result the Minister of Trade and Industry implemented the revised tariff dispensation of the light and heavy motor industry in 1995.

This revised tariff dispensation incorporates the following:

- Motor vehicle manufacturers may import components for the manufacture of motor vehicles under rebate of the customs duty. The duty on components can be reduced in conjunction with the *Import Rebate Credit Certificates* and a *duty free allowance (DFA)*.
- Motor vehicles manufactured locally are subject to an excise duty. The excise duty is rebated according to the local content incorporated in such motor vehicles. The main elements of these excise dispensation are that there is a minimum local content requirement of 25% in order to qualify for excise rebates and that the excise duty is rebated in full (except for 2,5 percentage points that are not rebatable) if a local content of 75 per cent is achieved.

What are Industrial Development Zones (IDZ's)?

Industrial Development Zones are government initiatives to position South Africa within the global economy. It aims at encouraging economic growth through export manufacturing industries, at creating jobs and generating sustainable local and foreign direct investment.

The Industrial Development Zone and is one of several incentives provided by the Department of Trade and Industry (DTI). “The idea behind the IDZ is to encourage export-related investments by providing a duty-free customs secure area and associated industrial park, manned by full-time customs officials, in close proximity to good quality transport infrastructure (port and railway) and allowing duty-free imports and VAT-free purchases of SA goods combined with major investment incentives. The IDZ will provide a one-stop shop for all regulatory, licensing and local government liaisons, making it a streamlined and easy place to do business. – IDZ's provide world-class infrastructure and excellent access to global markets.”

Are MIDP and IDZ only contradictory?

From the outside it might seem that IDZ and MIDP are two different incentive schemes of the DTI with nothing in common, however, both are:

- Government initiatives to position South Africa within the global economy,
- Aimed at increasing local content and exports,
- Aimed at creating jobs and
- Generating sustainable local and foreign direct investment.

Both incentives are under the same pressure of attracting more direct foreign investors. Firstly, the IDZ's on its own have not attracted the necessary amount of foreign investors as yet to achieve the above mentioned goals. Secondly the MIDP in itself asks for a constantly increasing local content of locally produced parts.

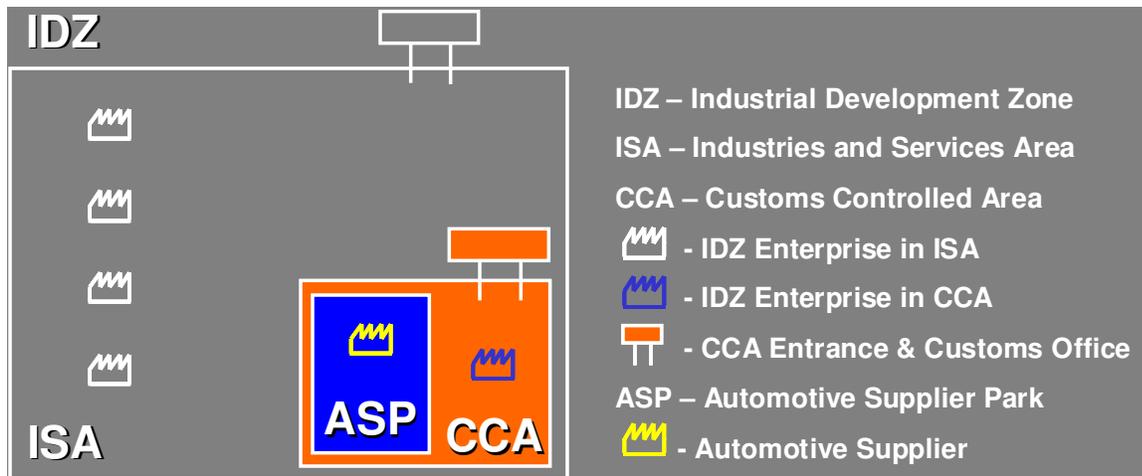
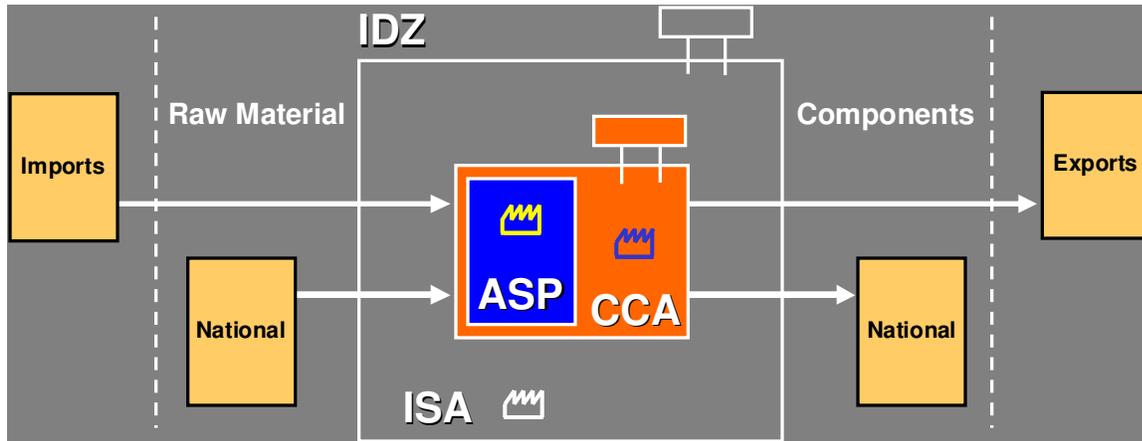
Additional to MIDP, some OEM's, e.g. DCSA, are confronted with further trade agreements, e.g. with Northern America, where the local content should be at the level of 35%. This can only be achieved by getting more international suppliers to locate in South Africa. In order to attract foreign investment, especially from automotive suppliers, a world class business environment and new incentives are required.

The original idea

Based on the information that both the MIDP and the IDZ share, in principle, the same targets, the original idea of the complimentary use of MIDP and IDZ incentives was born:

An automotive supplier, established in a CCA of an IDZ, should be able to supply components into South Africa and use the MIDP incentives, whilst at the same time have the opportunity to gain from IDZ incentives through the exporting of components into world markets.

Automotive Supplier Parks are latest state of the art developments within the automotive industry and could provide additional cost advantages through the optimisation of the value chain. The principle is based upon sharing in synergies obtained through increased economies of scale. The result is highly efficient supply chain operations with reduced logistics costs.



Problem: No local content in a “Extra Territorium”

Any resistance against locating an automotive supplier in an IDZ is immediately understandable once you understand the two relevant principles which are contradictory.

The MIDP is the current Phase of the “Local Content Program for the Motor Industry”. The objective of this investment program is to enhance the local content of added value within the manufacturing of automotive components or motor vehicle. Therefore component manufacturers or OEM's can rebate their excise duty for imported goods according to the local content incorporated in exported automotive components or motor vehicles (IRCC's).

Component manufacturers or OEM's can only produce local content if they are located within South Africa, particularly within the South African Customs Union.

The original concept of a duty free zone of an IDZ contains that it is seen as outside of the borders of the South African Customs Union, as described in Regulation 37 of DTI's original IDZ regulations:

'Regulation 37: Extra-territoriality of CSA for Customs Purposes'

- (a) The customs secured area of an Industrial Development Zone shall be deemed to be an export country for customs purposes.
- (b) The Customs and Excise Act and related legislation shall be enforced in respect of the entry of goods into and exit of goods from the customs secured area.
- (c) The Commissioner for the South African Revenue Services may make rules in terms of section 120 of the Customs and Excise Act to provide efficient and expedited customs procedures for Industrial Development Zones consistent with the purposes of this Regulation and the rules of this Chapter.

The Problem:

Any idea of locating an automotive supplier within a CSA of an IDZ is irrelevant, because any manufacturing within an IDZ doesn't create local content added value. Therefore this supplier or each OEM he supplies can not claim IRCC's.

Process: Way to the Complimentary use of MIDP & IDZ

The process of 'achieving the complimentary use of MIDP & IDZ' should incorporate the following milestones:

- 1. Local Content for IDZ's Duty Free Zone**
The IDZ's Duty Free Zone should not be seen as outside of the borders of South Africa.
- 2. Create Interface between IDZ (CCA) and MIDP**
An automotive supplier located in an IDZ should be able to deliver his products to the domestic OEM's and make the use of MIDP.
- 3. Guarantee Customs requirements**
Guarantee within the whole supply chain of automotive suppliers that the movements of material, components and goods especially into, through and out of the IDZ's are in accordance with customs and excise requirements.
- 4. Get the buy-in from the automotive industry**
The support of the whole automotive industry is crucial for the success of this idea.

Local Content for IDZ's

First it is necessary to clarify that any kind of production or manufacturing within the IDZ is creating local content value in accordance to MIDP.

As we started the investigations towards the complimentary use of MIDP and IDZ we contacted several government institutions, like DTI, ITAC, TISA, SARS etc. Within this period especially Mr. Mike Poverello from SARS Customs gave detailed answers:

"For your information the DTI's original IDZ Regulations are currently under review. This is as a result of the regulations being found ultra vires. The position of 'extra-territoriality', as dealt with under Regulation 37, Chapter XI of the original regulations, is therefore under review by the DTI. SARS advised the DTI that in the light of objections raised against the proposed structure of the IDZ, the CSA (now CCA) could never have been considered to be extra-territorial.

SARS has in the interim published legislation (Section 21A which at this point in time forms part of the Revenue Laws Amendment Act)². This section details Customs' administration and controls in Customs Controlled Area (CCA) of an IDZ. This legislation can only be enacted once amendments to the DTI's IDZ Regulations come into force.

In addition, SARS is preparing Rules to Section 21A that will specify the extent of Customs administration in the CCA. This will explain the roles and functions of Customs and its expectations of IDZ operators and CCA enterprises. It is envisaged that like Section 21A, publication of the Customs Rules will occur simultaneous to the promulgation of the DTI's IDZ Regulations

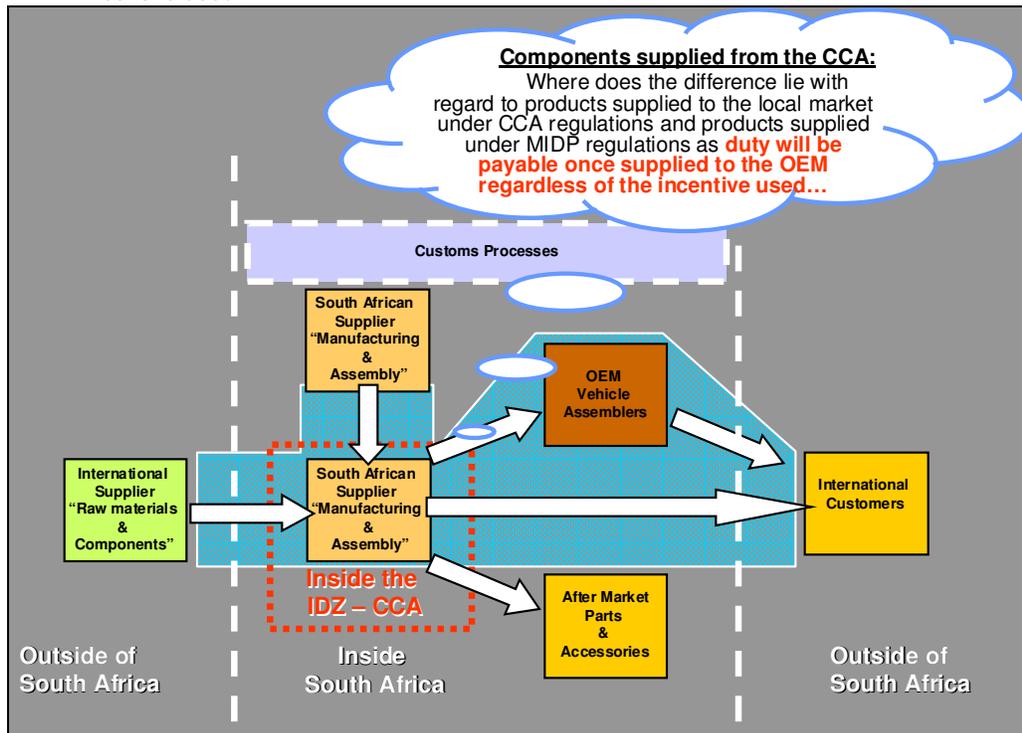
The change in terminology from CSA to CCA came about as a result of deliberations between the SARS Commissioner and the Director General DTI. While the DTI's regulation deems a CSA to be an export country, this is in fact not so. The CCA will be subjected to all the laws of South Africa."

This statement indicates that the DTI has already been on its way to delete the fact of extra-territoriality for the duty-free zone of IDZ's. The important question which remains unanswered is: **When will these changes to a Customs Controlled Area (CCA) be gazetted?**

Create Interface between IDZ and MIDP

Due to the fact that the status of extra-territoriality is going to be deleted, we introduced to the relevant government departments the need of a potential interface between IDZ (CCA) and MIDP. The concept is depicted in the picture below and results in the following question:

- Where does the difference lie with regard to products supplied to the local market under CCA regulations and products supplied under MIDP regulations as duty will be payable once supplied to the OEM regardless of the incentive used?



² Go to URL: <http://www.sars.gov.za> > Legislation > Acts > Amendment Acts > Revenue Laws Amendment Act (Act 45 of 2003) (Promulgation date 22 December 2003) (GG No 25864)

In addition we challenged Regulation 34 of the original IDZ regulation,

Regulation 34 of the Manufacturing Development Act no. 187 of 1993:

'Eligibility for benefits and incentives'

An IDZ operator or IDZ enterprise shall be entitled to apply for any other benefits or incentives offered from time to time by the Republic of South Africa,

with two straight forward questions

- Does Regulation 34 include MIDP incentives?
- Can the MIDP incentives be complementary to the CCA incentives provided by the IDZ's?

To this, Mr. Mike Poverello from SARS Customs responded as follow:

*"In regard to duty and VAT suspension – **goods imported** for the purposes of processing, manufacture or distribution **will not attract duty and VAT** on importation, **provided the goods or end product are exported**. In addition, **SARS will allow companies in the domestic market to provide zero-rated VAT inputs, on certain goods**, to enterprises operating in the CCA. SARS VAT legislation is being amended to provide for this. The conditions under which all imports and inputs will be dealt with will be covered in the Customs Rules.*

Concerning IDZ/CCA vs. MIDP options, this is a matter that best be raised with ITAC, via the DTI. SARS Customs is essentially the administrator of customs formalities governing such arrangements and does not determine the extent of economic incentives."

As recommended we requested for a meeting at DTI with all relevant government institutions. This meeting convened on Friday the 22nd of April 2005 at the DTI offices and was chaired by Gustav Meyer, DTI and facilitated by the ELIDZ's AIDC-Team.

The target of that meeting was to achieve a common point of view and a common agreement on the way forward with all participants from the DTI, ITAC, TEO, SARS, ECDC, ELIDZ, COEGA, KPMG and AIDC.

Focused on the complimentary use of MIDP and IDZ we challenged the audience with the key question:

- **Can we use IDZ (CCA) and MIDP processes complimentary?**

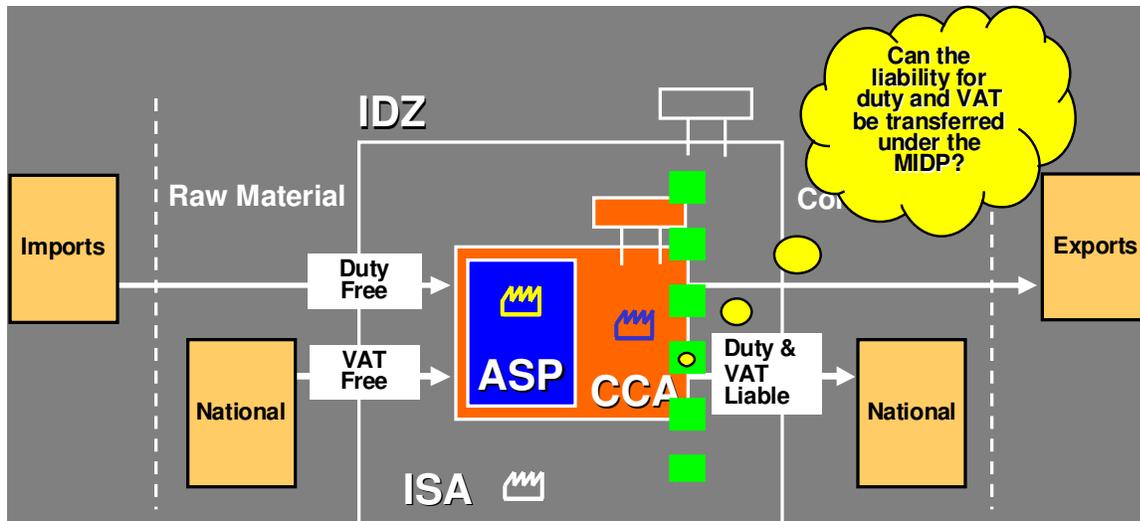
Whilst ensuring the:

- Control of the processes in accordance with Customs and Excise requirements and
- Exclusion of double dipping.

For discussion purposes we reduced this broad question down to the idea of having a clear interface between IDZ and MIDP. As shown in the picture below, the concept of having an automotive component manufacturer within a CCA of an IDZ and supplying his products to the local market was explained in detail to the audience.

The critical question about the complimentary use of MIDP and IDZ was discussed extensively:

- **Can the liability for duty and VAT be transferred under the MIDP?**



The picture above shows a rough concept on possible delivery processes developed from an automotive supplier's point of view within a CCA environment. **Note that when components or products leave the CCA for the national market, duty and VAT must be paid and this interface, handover/control point, becomes the critical point where the MIDP incentives might complement the CCA incentives.** At this point under MIDP, VAT and duty liability is transferred to the national OEM via a DA190. This approach assumes that the CCA is seen as within the borders of South Africa and goods that is manufactured within the CCA is deemed as local content.

As a result different government institutions were informed simultaneous in detail about the IDZ's original problem within the automotive sector and their need of further incentives to gain more investors. Even the experts within the responsible government institutions couldn't answer these questions immediately.

With regard to the complimentary use of MIDP and IDZ the following was tabled as issues that would be looked at as a matter of extreme urgency:

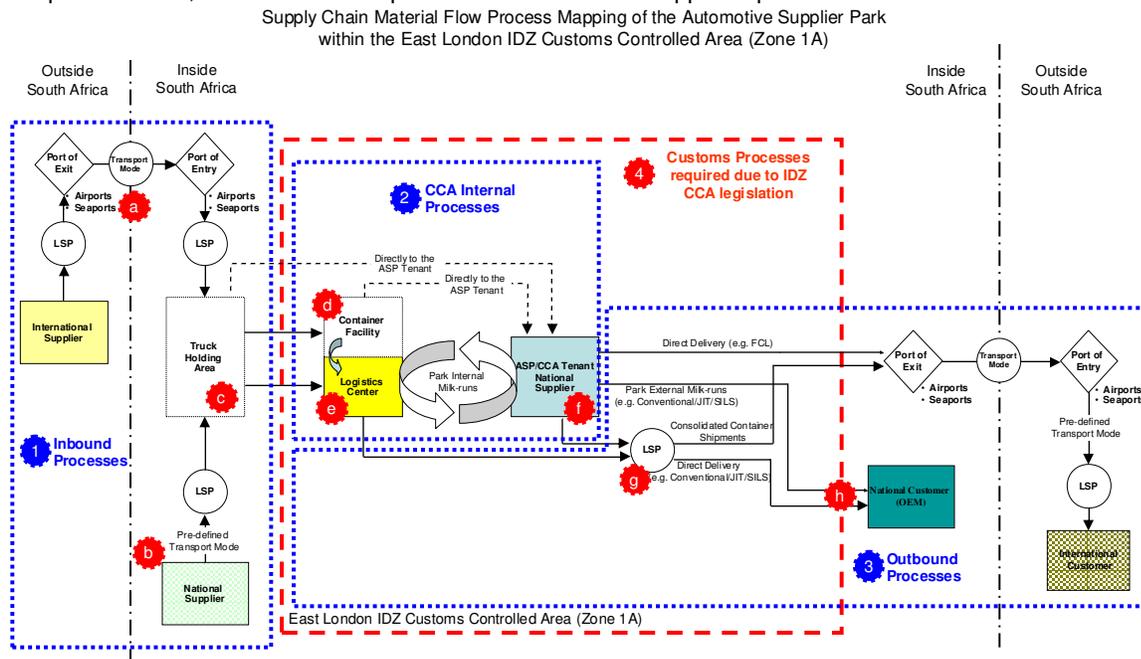
- Clarification with regards to VAT treatment of the supply of goods and/or services to and within the CCA (resp.: SARS VAT Division),
- Will there be a rebate item specifically for the CCA and how will customs be able to handle it if two rebate items are applicable in a CCA? (resp.: SARS),
- How would a CCA be handled under the MIDP review? (resp.: The DTI TISA/ ITAC / SARS),
- What are the qualifying benefits and disincentives of locating into a CCA vs. outside an IDZ? (resp.: The DTI / TEO),
- Position statement on open issues such as, Bonded warehouses vs. a specific CCA as one bonded area. (resp.: SARS)
- What will the relationship be between the different rebate warehouses in the movement of goods? (resp.: SARS)
- Would there be only one type of warehouse allowed within a CCA (i.e. 360.01 type)? (resp.: SARS)
- How does customs legislate the movement of goods from a CCA to National (to a bonded warehouse, i.e. 470.03, or any other enterprise without a bond and visa-versa)? (resp.: SARS)

- Clarity on what rate of duty will be applicable to a CCA enterprise who will be selling some “finished” products to the local market / national – will duty be levied on the value of imported input material or levied on the value of the finished product? (resp.: The DTI)
- An answer is needed within 2 months whether MIDP and CCAs can coexist. (resp.: All)

It was decided that the next meeting should take place within a month, and that it will be arranged by Gustav Meyer’s office. (resp.: The DTI/TISA)

Guarantee Customs requirements

Based on customs requirements due to the IDZ CCA Legislation the following Customs Control Points (a-h), shown in the picture below, have been developed from an automotive supplier’s point of view within a CCA environment.



Customs control points of raw materials and components:

- International imports into the CCA – VAT and Duty Exemption
- National raw materials and components into the CCA – VAT Exemption
- Audits can be done on trucks held at the truck holding area to check whether they are sealed or not.
- Containers within the container facility must be sealed at all times
- Audits can be done on raw materials and components handled within the Logistics Center
- Audits can be done on raw materials and components handled within the ASP tenant facilities
- Containers and trucks leaving the CCA area must be sealed and proof of destination must be on specified on the “Bill of Lading”
- VAT and Duty transaction/liability to customs should parts go to the national market, to the OEM. (Liability transferred through DA190).

Note:

With regard to more streamlined processes, latest IT technologies like bar coding etc., may support customs to assure their requirements.

Get the buy-in from the automotive industry

The most important milestone along the process of “getting the complimentary use of MIDP and IDZ done” is to achieve the buy-in from the whole automotive industry, especially from the OEM.

The following should be envisaged:

1. Positive Changes within MIDP:

The changes within MIDP should be to the advantage of the automotive industry.

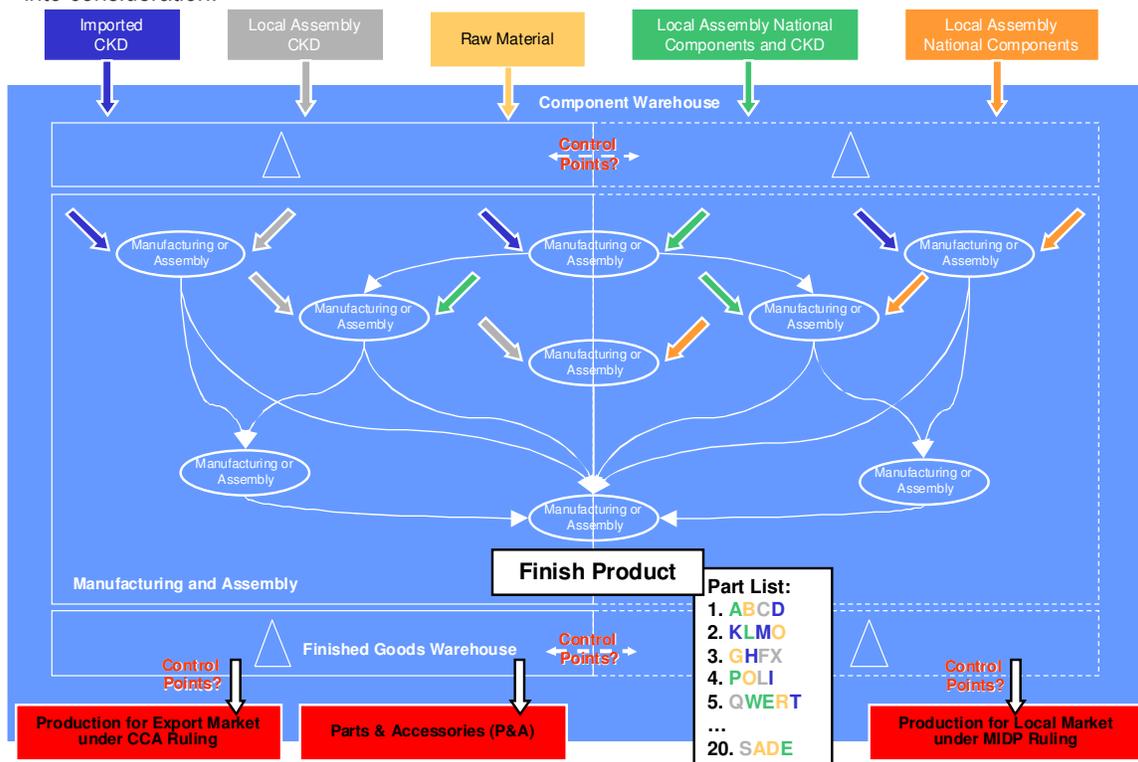
2. Stick to Automotive Standards within IDZ:

Automotive Suppliers must stick to the standards of the automotive industry. Therefore an IT systems within IDZ's, should cover both customs requirements and automotive standards.

3. Create more IRCC's:

First of all the complimentary use of MIDP and IDZ should not lead to the loss of IRCC's. This would be killer criteria for the whole concept. Above that, the long term results of this concept should create more local content added value and therefore more IRCC's.

For the tracking of local content a system which is recording the material flow through a CCA, might be taken into consideration:



4. Fair business towards automotive suppliers who are not located in an IDZ:

Automotive suppliers, who are already located in South Africa but not in a CCA should be provided with the same or similar advantages in an effort not to disturb the competitive balance within the local market.

Solution: Interface between MIDP & IDZ

The solution for the complimentary use of MIDP and IDZ is built upon two pillars:

- Firstly, manufacturing within an IDZ result in local content added value,
and
- Secondly, there must be a legal interface between the laws of MIDP and IDZ.

Whereas it seems that through Section 21A the first pillar is already solved, the second pillar can only be build by certain specialists. Currently DTI is reviewing the original legislation of MIDP as well as IDZ regulations and incentives.

The following elements should be taken into consideration while reviewing the relevant MIDP and IDZ laws and regulations and creating the interface:

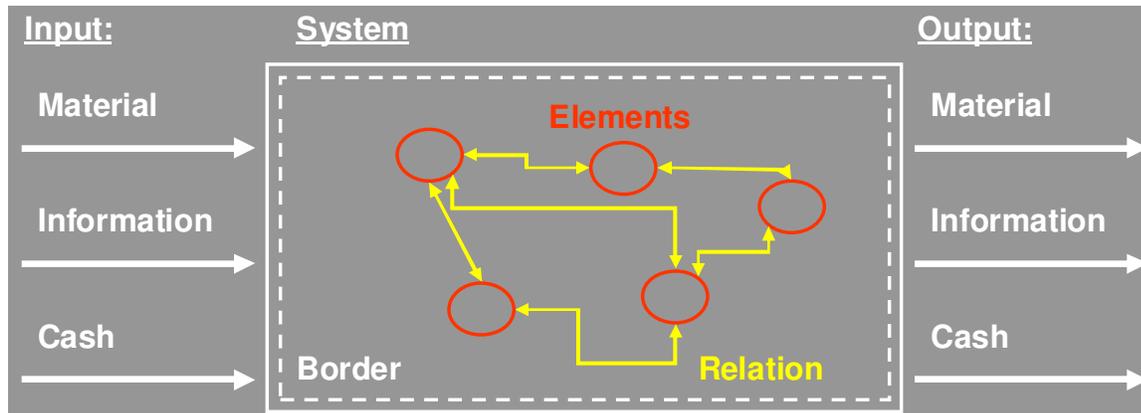
- 1. Positive Interaction between MIDP and IDZ laws and regulation**
Firstly there should be no disadvantages, especially with regard to IRCC's, and secondly there might be the possibility of giving potential automotive investors for an IDZ special incentives within MIDP.
- 2. Clear identification of the process of transferring duty-liability**
Duty liability and or when duty has to be paid should be clarified and easy understandable.
- 3. Clear determination of the extent of economic incentives within an IDZ**
The extent of economic incentives should be fully identified and easy understandable.
- 4. Clear identification of customs requirements within MIDP and IDZ**
What exactly are the customs requirements and why are they necessary?
- 5. Provide the industry with competitive customs processes**
Most efficient at lowest costs customs processes through a minimal amount of physical control points and by using state of the art technologies (bar coding) and IT Systems (MISCCIP).
- 6. Meet national government policy goals**
Duty-free zones are primarily designed to support export oriented industries. It should be kept in mind that the original idea of import duties is to protect the local market.
- 7. Put in place an incentive system that is acceptable in terms of international trading practice**
Make sure that there will be no problems with the WTO.

Monetary Value of the complimentary Use of MIDP & IDZ

To identify the extent of the monetary value of using MIDP and IDZ complimentary the following approach, based on the principles of systems engineering, was chosen.

Systems engineering:

A system is identified through its borders, elements and the relationship between the elements. The processes inside a system are determined through input and output. The basic rules “What goes in must come out”, “You can not waste energy” and “Nothing comes from nothing” must be considered.



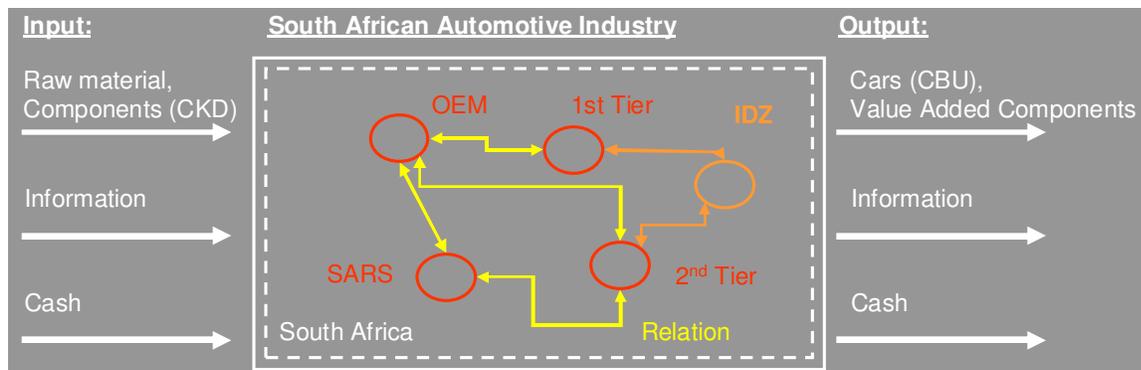
Taken this approach into consideration the important business question is **“What is the exact monetary value of the complimentary use of MIDP and IDZ?”** This question kick starts the following questions:

- **What is our system and where do we fence our border?**
- **Who or What are our elements, participants?**
- **What kind of relationship do these elements have?**
- **What goes in and what goes out?**

Once agreed on answers to these ‘systems questions’, especially in situation with different stakeholders and competitive interests, an important common platform for discussion of overall important business questions has been built.

With regard to the monetary value of the complimentary use of MIDP and IDZ, the following simplified system can be build:

- Our system is focused on the South African Automotive Industry and we fence our border around South Africa.
- Our elements or participants are SARS, as representative for all relevant government institutions, OEM, 1st Tier suppliers, 2nd Tier suppliers and IDZ.
- Our relationships between these elements are given through material, information and cash flows based on business practice as well as laws and regulations, especially MIDP, IDZ and Customs requirements.
- The input consists of raw material and components (CKD), information and cash. The output consists of value added components, modules or cars (CBU) as well as information and cash.



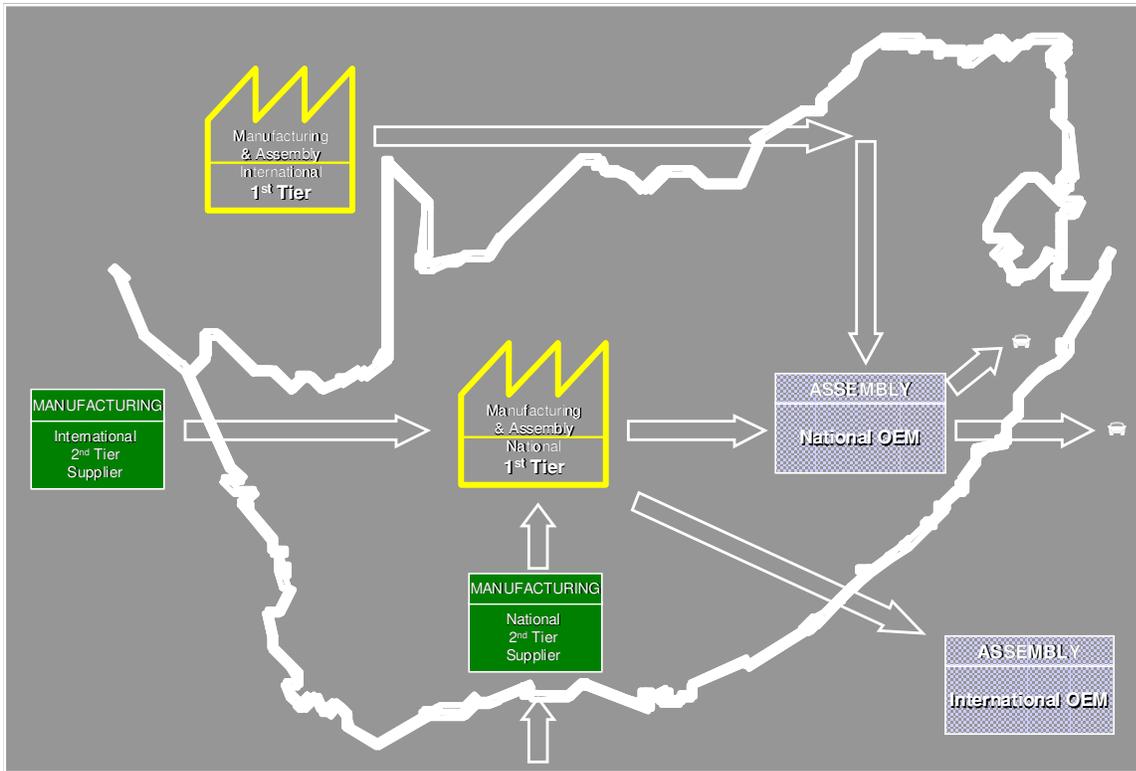
The current process under MIDP without IDZ

Looking at our simplified system in more detail and focus on the material flow, as shown in the picture below, you will be able to recognize that in principle a 1stTier Supplier located in South Africa is

- Importing raw material and components from international 2nd Tiers,
- Buying further raw material and components from national 2nd Tiers,
- Adding value to these materials and components through production and assembly,
- Supplying his 'finished products', automotive components or modules, to a local OEM, and/or
- Supplying his 'finished products', automotive components or modules, to an international OEM.

And an OEM located in South Africa may:

- Importing components or modules from international 1st Tiers,
- Buying further components or modules from national 1st Tiers,
- Adding value to these components or modules through production and assembly,
- Supplying his 'finished products', cars, to a local Customers, and/or
- Supplying his 'finished products', cars, to a international Customers.

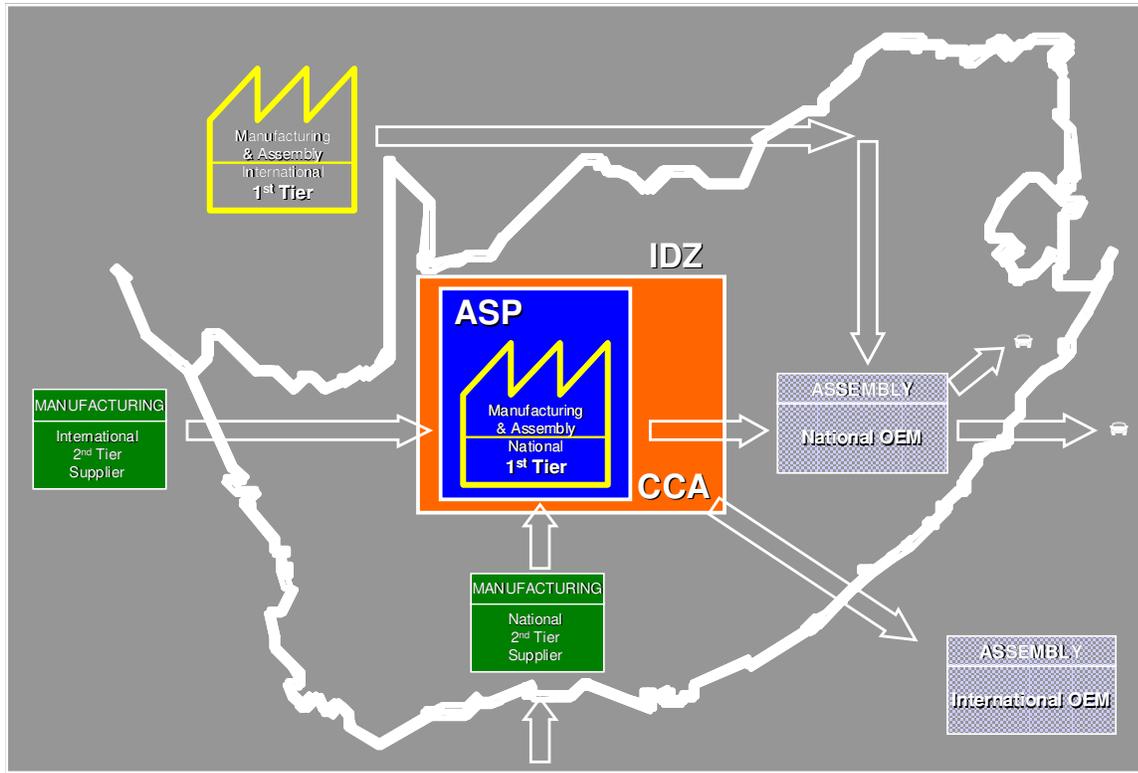


This material flow is linked to certain information and cash flows which are indicated in the table below. A positive cash flow (+) is seen as income, whereas negative cash flow (-) identifies costs:

Materialflow	Information flow	Cash flow					
		1st Tier		National OEM		SARS	
		primary	secondary	primary	secondary	primary	secondary
Imagine a 1 st Tier Supplier located in South Africa is...							
Importing some raw material and components from international 2 nd Tiers	ordering						
	delivery to South Africa	duty (-)	interests on duty (-)			duty (+)	interests on duty (+)
	delivery within South Africa						
	arrival and storage	price (-)					
Buying further raw material and components from national 2 nd Tiers	ordering						
	delivery within South Africa						
	arrival and storage	price incl. VAT (-)				VAT (+)	
Adding value to these material and components through production and assembly	production						
	assembly						
	identifying local content value						
Supplying his 'finished products', automotive components or modules to a local OEM	selling	price S incl. VAT (+)		price S incl. VAT (-)		VAT (+)	
	delivery						
	transferring duty liability	duty (+)		duty (-)	interests on duty (-)		
Supplying his 'finished products', automotive components or modules to an international OEM	selling	price S incl. VAT (+)				VAT (+)	
	delivery within South Africa						
	delivery to overseas						
	identifying IRCC's	IRCC's (+)				IRCC's (-)	

The new process MIDP and IDZ complimentary

Through changing the original IDZ regulations, adapting CSA to CCA, and creating an interface between MIDP and IDZ we implement a new element within our system 'South African Automotive Industry': the Industrial Development Zone (IDZ). This changes the relationship between the elements while input and output stays the same.



The material flow stays the same, but information and cash flow will be influenced:

Material flow	Information flow	Cash flow					
		1st Tier		National OEM		SARS	
		primary	secondary	primary	secondary	primary	secondary
Imagine a 1 st Tier Supplier located in South Africa is...							
Importing some raw material and components from international 2 nd Tiers	ordering						
	delivery to South Africa						
	delivery within South Africa						
	arrival and storage	price (-)					
Buying further raw material and components from national 2 nd Tiers	ordering						
	delivery within South Africa						
	arrival and storage	price incl. VAT (-)				VAT (+)	
	production	savings (+)					
Adding value to these material and components through production and assembly	assembly						
	identifying local content value						
	optimized supply chain	savings (+)		savings (+)			
	selling	price S incl. VAT (+)		price S incl. VAT (-)		VAT (+)	
Supplying his 'finished products', automotive components or modules, to a local OEM	delivery						
	identifying duty liability			duty (-)	interests on duty (-)	duty (+)	interests on duty (+)
	selling	price S incl. VAT (+)				VAT (+)	
	delivery within South Africa						
Supplying his 'finished products', automotive components or modules, to an international OEM	delivery to overseas						
	identifying IRCC's	IRCC's (+)				IRCC's (-)	

What are the differences between now and then?

The advantages through the possibility of the complimentary use of MIDP and IDZ are:

- The suppliers' duty cash flow falls away and with that the interests on duties
- All role players might have additional savings through a new process of only paying duty, and interests thereof, for imported materials and components which are supplied into the local market. The savings are therefore generated on no duties paid for export products, as shown in the table below.

Cashflow Model						Illustrative example of periodic cash flow
	(Rand)	VAT (14%)	Interests (10%)	(Rand)		
Average, Constant Material & Component-Cash flow:	100	14	11.4	125.4	86%	R 3,000,000.00,-
thereof local:	35	4.9	3.99			
imported:	65	9.1	7.41			
Duty on imported value (28% - 2004)	18.2		1.82	20.02	14%	
Total Cash Flow				145.42	100%	R 4,362,600.00,-
Production within a duty free zone						
Cashflow Saving Potentials				20.02	14%	R 610,764.00,-

Additional advantages, given through suppliers located within a CCA of an IDZ, are:

- The suppliers will have savings within production through IDZ incentives provided for rental of buildings, land, water & electricity, etc...
- The suppliers will have additional savings through optimized logistics provided through the Automotive Supplier Park. The ASP will streamline the whole supply chain and therefore even provide the OEM with certain savings, especially through more robust processes.

Benefits of the complimentary Use of MIDP & IDZ

The strategic goal of the complimentary use of MIDP and IDZ is to create in South Africa world class incentives and business environment that will be conducive to attract foreign investment.

This world class business environment could be achieved through a combination of the following incentives:

- IDZ general incentives:
 - Low development costs for new factory buildings or
 - Low rental prices for new factory buildings
 - Reduced costs for water, electricity, sewage,

- IDZ special incentives:

- VAT- & Duty-free imports,
- VAT-free purchases of local goods,
- One-Stop-Shop for all regulatory, licensing and local government liaisons,
- Automotive Supplier Park (ASP) – Reduced Logistics Costs,

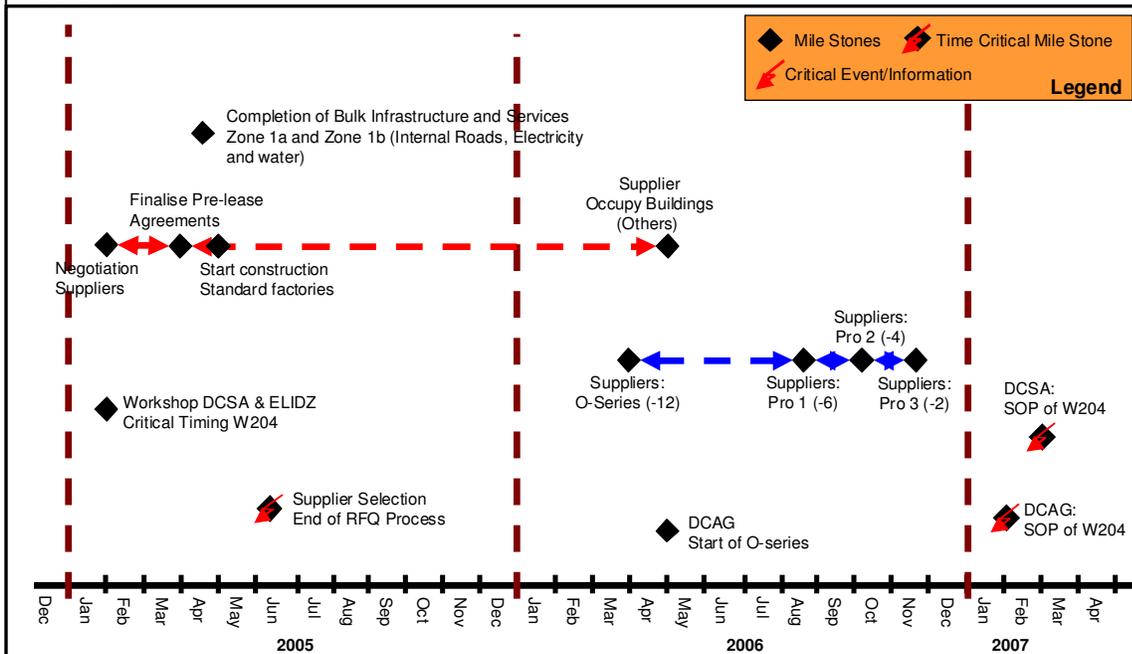
- Additional incentives for the automotive sector:

- MIDP incentive – Import Rebate Credit Certificates (IRCC),
- MIDP incentive – Productive Asset Allowance (PAA).

Ideal for the Industrial Development Zones would be to maximise the offer to potential automotive suppliers and to provide a business case through the combination of incentives.

Risks Towards the complimentary use of MIDP & IDZ

The buy-in of the automotive industry is crucial for the success of this concept. The extent of this element gets clearer as you focus on the planning cycles of the automotive industry, e.g. the time planning of DCSA for the W204 production.



Within the overall planning of the complimentary use of MIDP and IDZ are two major concerns:

1. Government legislation and procedures are not in line with the 7 year planning cycles of the automotive industry:

If government is legislating after an investment decision has been done, then it would be just too late with regard to a particular 7 year production cycle.

and

2. Ability of IDZ's to comply with customs and excise requirements may be secured too late with regard to the planning of the automotive industry:

If IDZ's are not able to comply with the requirements of customs towards material flow control and customs stops any material movement within the IDZ, while in the same time the automotive industry is starting their ramp up phase or even running their processes on high volume, this might cause a huge problem within the production.

Chances out of the complimentary use of MIDP & IDZ

The chances are to expand the possibility of the complimentary use of MIDP and IDZ along the automotive supply chain as new market potentials.

- After allocating 1st Tier suppliers, this concept should lead to locate the whole automotive supply chain within the IDZ's.
- Especially on 2nd Tiers, 3rd Tiers, BEE etc. should be focused.
- IDZ's could become "the benchmark" within the development of the supplier's infrastructure of the automotive industry.
- Additionally wherever it seems to be possible such a hybrid incentive might be created for other industry sectors.

Conclusion and Way Forward

This report summarizes the main ideas, concepts, models and approaches towards the complimentary use of MIDP and IDZ. Beginning with analyzed original IDZ regulations and their contradiction with MIDP, a potential new relationship between MIDP and IDZ, and the way to achieve that, has been designed. This relationship might turn out as the new incentive which IDZ's operators are longing for on their way to approaching investors, especially in the automotive sector.

This work stops on a more conceptual level. The above mentioned models need to be verified upon realistic figures, confirmed and finally implemented. Therefore especially the following is required:

- **Work out in detail what exactly the monetary value of that new incentive is;** based upon analyzed cash flows within the industry, and
- **Create a legal interface between MIDP and IDZ.** This should be done by Customs and Trade Specialists, especially now while DTI is reviewing both MIDP and IDZ regulations and incentives. Therefore it is absolutely necessary that the started process of 'getting the complimentary use of MIDP and IDZ done' will be continued. The outcome of the first meeting at DTI, described in chapter 5.2., is a perfect platform to start.

The way forward for the IDZ's is to support government institutions within their internal procedures so that their decisions will be more in line with the planning cycles of the automotive industry. This should result in incentive schemes which immediately attract the interest of potential automotive investors.

With regard to the concept of using MIDP and IDZ complimentary, in the light of DCSA's W204 time planning, the most time critical questions remain unanswered:

- **When will, in terms of the MIDP, local content be possible within an IDZ?**
- **When will the interface between MIDP and IDZ be gazetted?**

Nevertheless the real decision factors which make a potential investor, automotive supplier, move into an IDZ is, that **it must be a business case**. The identification of a real business case requires a detailed analysis of the current business situation compared to a potential future business environment. A business case will not be made through one incentive only, but should be an entire business decision.

The complimentary use of MIDP and IDZ could build the platform to attract more foreign investment within the automotive industry into South Africa.

Appendix: Extract of Relevant Laws & Regulations

Motor Industry Development Programme

The following is based on the 'Revised Customs Dispensation For The Motor Industry' Report No. 3625 of the Board on Tariffs and Trade from the 15th of August 1995.

Chapter 2. Current Tariff Structure:

- 2.1 The customs duty in respect of completely built-up motor vehicles which fall in the ambit of motor vehicles manufactured in terms of Phase VI of the Local Content Programme, has recently been reduced in three phases from 100 per cent ad valorem to the current rate of duty of 70 per cent ad valorem. (Annexure C)

Motor vehicle manufacturers may import components for the manufacture of motor vehicles under rebate of the customs duty, provided that they comply with the rebate provision of item 317.03 of Schedule 3 to the Customs and Excise Act, 1964. (Annexure C)

Motor vehicles manufactured locally are subject to an excise duty of 40 per cent. The excise duty is rebated according to the local content incorporated in such motor vehicles. The main elements of these excise dispensation are that there is a minimum local content requirement in order to qualify for excise rebates and that the excise duty is rebated in full (except for 2,5 percentage points that are not rebatable) if a local content of 75 per cent is achieved.

Chapter 5. Outline of the Light Motor Vehicle Customs Dispensation:

- 5.2 It is proposed that the customs duty on light motor vehicles,, be reduced to 65 per cent ad valorem and a phased reduction thereafter to 40 per cent ad valorem.
- 5.3 the Board calculated that a duty-free allowance (DFA) of 27 per cent of the net ex-factory selling price of locally manufactured light motor vehicles will enable motor vehicle manufacturers to import a large number of those components that can not be sourced locally at a competitive price. This will impact positively on the competitiveness of the local Motor Vehicle Manufacturing Industry and it would still provide protection to local component manufacturers.
- 5.4 ... 5.10.
- 5.11 It is foreseen that motor vehicle manufacturers that participate in the revised customs duty dispensation for light motor vehicles will have to calculate their liability to the Customs and Excise authorities annually, but that interim quarterly returns and provisional payments will be required, with an annual reconciliation. Imports of original equipment automotive components and motor vehicles should be offset against the proposed DFA of 27 per cent of the nett ex-factory selling price of locally manufactured motor vehicles, and the excess value of imports become liable to the rates of duty.
- 5.12 In addition to the above, it is proposed that imports and exports of automotive components and CBU motor vehicles be facilitated by means of Import Rebate Credit Certificates. The intention is that by exporting certain (eligible) locally manufactured automotive components and motor vehicles, such exports may be used to offset the duty on imported automotive components and motor vehicles.
- 5.13 The monetary value of the local content of automotive components that have been approved in terms of this facilitation, and tooling as well as the monetary value of the local content of CBU motor vehicles that have been exported, may be used to import an equivalent monetary value of automotive components and motor vehicles in accordance with the following ratio:

- (a) The local content value of exported CBU light motor vehicles against the imported value of CBU imported light motor vehicles.
 - (b) the local content value of either motor vehicles, tooling or eligible automotive components exported against the imported value of original equipment or replacement market automotive components...
 - (c) ...
 - (d) ...
- 5.19 The Board proposes that eligible exports of automotive components qualify for the Import Rebate Credit Certificates if –
- (a) the components have been wholly or partly manufactured in the common customs area; and
 - (b) not less than 25 per cent of the production cost, excluding packaging, is represented by –
 - (i) the cost of labour in the common customs area; and/or
 - (ii) the cost of raw materials and subcomponents produced in the common customs area; and/or
 - (iii) the direct factory overhead expenses incurred in the common customs area to manufacture such automotive component; and
 - (iv) the final process of manufacture of such automotive component is carried out in the common customs area, and if the final process of manufacture is undertaken in the country to which the component is exported, the automotive component still be considered to qualify, if the export thereof can be justified in terms of the value added in the common customs area.

IDZ - Customs Secured Area (CSA)

The following is based on the Manufacturing Development Act No. 187 of 1993: Industrial Development Zone programme No.R. 1224 from the 1st of December 2000.

'Regulation 1: Definitions' contains the following:

- (f) "customs secured area" or "CSA" shall mean a designated area within an Industrial Development Zone subject to special customs legislation.
- (j) "industries and services area" shall mean the area of an Industrial Development Zone that is not designated as a customs secured area.

This defines clearly that not the whole IDZ can be seen as a Customs Secured Area.

'Regulation 26: The Industrial Development Zone Enterprise'

An IDZ enterprise permit shall be required for a company to operate a trading concern from within an IDZ.

This regulation defines that you have to operate from within the IDZ.

'Regulation 33: Entitlement to Industrial Development Zone Benefits'

- (a) All IDZ operators and enterprises are entitled to the benefits and incentives of the South Africa IDZ programme...
- (b) All IDZ operators and enterprises conducting business in the customs secured area shall also enjoy the benefits and incentives attaching to business in the CSA...

This regulation defines that you are entitled to different IDZ incentives and benefits dependent on where you are located within the IDZ.

'Regulation 34: Eligibility for Benefits and Incentives'

An IDZ operator or IDZ enterprise shall be entitled to apply for any other benefits or incentives offered from time to time by the Republic of South Africa.

This regulation defines clearly that each IDZ enterprise can apply for any other incentives offered by South Africa. This should also be valid for MIDP.

'Regulation 37: Extra-territoriality of CSA for Customs Purposes'

- (a) The customs secured area of an Industrial Development Zone shall be deemed to be an export country for customs purposes.
- (b) The Customs and Excise Act and related legislation shall be enforced in respect of the entry of goods into and exit of goods from the customs secured area.
- (c) The Commissioner for the South African Revenue Services may make rules in terms of section 120 of the Customs and Excise Act to provide efficient and expedited customs procedures for Industrial Development Zones consistent with the purposes of this Regulation and the rules of this Chapter.

This regulation defines that

- customs secured area within an IDZ is seen as outside the borders of South Africa,
- the movement of goods into and out of a CSA must stick to the Customs and Excise Act, and
- SARS provide the IDZ with efficient and effective customs procedures.

Customs Requirements within the CSA - Duty liability:

'Regulation 36: Import/Export Incentives'

The following import/export incentives shall apply within each customs secured area subject to the rules provided in this Regulation and other applicable law –

- (a) customs duties, levies, fees or similar financial obligations,...., shall not apply to imports to a customs secured area from outside the customs territory and exports from a customs secured area to a destination outside the customs territory,....
- (b) For the purposes of the Value-Added Tax Act (Act no. 89 Of 1991), (the "VAT act"):
 - (1) goods imported into a customs secured area of an IDZ by a registered vendor situated therein shall be exempt from value-added tax ...
 - (2) the supply under sale or installment credit agreement of goods consigned or delivered by a vendor in the Republic, to a registered vendor in the customs secured area of an IDZ shall,...., be subject to value-added tax at the rate of zero percent...

- (3) goods supplied under sale or instalment sale agreement and removed by a registered vendor situated in the customs secured area of an IDZ shall be subject to a refund of value added tax...
- and
- (4) supplies of goods out of an IDZ into the Republic shall be subject to value-added tax... .
- (c) Sales from a customs secured area to the customs territory shall be deemed to be imports... .
- (d) Sales from the customs territory to a customs secured area shall be deemed to be exports from South Africa... .

This regulation defines that customs secured area within an IDZ is

- a duty free zone,
- VAT free for imported and local purchased goods, and
- that the supplies of goods into the Republic is subject to value added tax.

Operational requirements within a CSA:

The following is an extract of the Gazette with regards to particular “operational requirements” to run an IDZ, either from an IDZ operator or an IDZ enterprise point of view:

Regulation 19 Responsibilities of an IDZ Operator

- (a) An IDZ operator must
 - (1) install and maintain an information system to record the movement of material and components imported into and exported from the CSA for the purposes of reporting to the South African Revenue Service;
 - (2) obtain authorisation from the South African Revenue Service to establish a licensed warehouse and provide guarantees for duties payable on imports into the CSA;
 - (3) ...
 - (4) ...
 - (5) maintain adequate and proper financial records and accounts and other records relating to the operation of the IDZ; and
 - (6) ...

Regulation 24 Physical Security and Safety Requirements

- (a) In order to protect the safety of persons and goods, each IDZ must be constructed in accordance with the following requirements:
 - (1) A barrier, approved by customs officers to provide physical security shall be built around the entire perimeter of any customs secured area.
 - (2) ... entrance and exit shall be guarded on a permanent basis...
 - (3) The IDZ customs office shall be located within the IDZ at the entrance of the CSA...
 - (4) All... buildings shall be constructed at least 5 meters from the CSA barrier.
 - (5) Entrances and roads ... shall be built ... to facilitate the expedient movement of vehicles, machines, persons and customs and security personnel.

- (6) Adequate lighting, ... must be operational at all times, ... and must illuminate the barrier surrounding the CSA.
- (b) Access into the IDZ shall be controlled by IDZ security personnel... . Access into the CSA shall be controlled by IDZ security personnel and by the customs officers assigned to that zone by SARS.

Regulation 38 Customs Offices within IDZ's

Up to

Regulation 48

New IDZ - Customs Controlled Area (CCA)

The following is based on the drafted version of the new IDZ Gazette, April 2005.

Regulation 1: Definitions

- h) "Customs control area" or "CCA" shall have a corresponding meaning as contained in the rules promulgated under Section 21 of the Customs and Excise Act, (no. 91 of 1964) as amended and specifically in these regulations shall mean an area within an Industrial Development Zone that is subject to the rules and which is designated as such with Customs and Excise.

Regulation 41: The CCA

- a) With regards to the CCA, the rules issued in terms of Section 21A of the Customs and Excise Act, no. 91 of 1964, as amended from time to time shall apply.
 - 1) All duties and requirements prescribed in the rules must be complied with by all IDZ Users and any non-compliance shall entitle the Adjudication Board to refuse or withdraw an IDZ Developers Permit, IDZ Operators Permit or IDZ Enterprise Permit as applicable

Regulation 42: Other Law

- a) In all their activities, omissions and commissions, all IDZ users shall comply with the laws of the Republic of South Africa and any contravention shall be dealt with in terms of South African Law.

Changed Customs requirements within a CCA - Duty liability within a CCA:

The following is based on the amendment of section 121 of Act 60 of 2001.

Extract of Section 21A:

Provisions for the administration of customs controlled areas within

Industrial Development Zones

21A. (1) For the purposes of this section, unless the context otherwise indicates—

'Customs Controlled Area' or 'CCA' means an area within an IDZ, designated by the Commissioner in concurrence with the Director General: Trade and Industry, which area is controlled by the Commissioner;

'Industrial Development Zone' or 'IDZ' means an area designated by the

Minister of Trade and Industry in terms of any regulation made under section 10 (1) of the Manufacturing Development Act, 1993 (Act No. 187 of 1993);

'IDZ operator', 'CCA enterprise', 'Service enterprise' or any other expression as may be necessary, relating to any activity inside or outside an IDZ or a CCA shall have the meaning assigned thereto in any Schedule or rule.

2) Any reference in this section, any Schedule or any rule to 'regulations' or 'regulation' shall, unless otherwise specified, be a reference to the regulations made under section 10(1) of the Manufacturing Act 1993.

(3) Where any provision of the Manufacturing Development Act, 1993, or any regulation made thereunder for the purpose of the IDZ is inconsistent or in conflict with any provision of this Act governing the administration of the CCA, including any matter relating to the liability or levying of duty or any rebate, refund or drawback of duty, the provisions of this Act shall prevail over the provisions of the Manufacturing Development Act, 1993, or the regulations made thereunder.

(4) Notwithstanding anything to the contrary contained in this section or any other provision of this Act or in the Value-Added Tax Act, 1991, goods to which subsection (7) relates shall, subject to any exception or adaptation prescribed in any Schedule or rule—

(a) even if free of duty, be deemed to be goods liable to duty for the purposes of the application of any provision of this Act; and

(b) if removed from a CCA, be deemed to have been imported into the Republic.

(5) Any reference in this section to liability for duty or termination of liability for duty or in any Schedule or rule to which it relates shall, subject to any exemption or exception allowed in terms of the Value-Added Tax Act, 1991 (Act No. 89 of 1991), and notwithstanding anything to the contrary contained in that Act, be deemed to include a reference to the liability or termination of liability for value-added tax.

(6) A CCA shall be subject to such controls and procedures, as the Commissioner may prescribe by rule.

(7) Any goods to which this section or any other provision of this Act relates, whether or not such goods are free of duty, which are—

(a) brought into a CCA;

(b) produced or manufactured, stored, or moved for any purpose therein; or

(c) removed therefrom, shall, except to the extent that this section, any Schedule or any rule may otherwise provide, be subject to the provisions of this Act and any procedure that may be prescribed in terms of such provisions.

(8) Any person, including, where relevant, a CCA enterprise or an IDZ

operator, who for the purposes of any activity within a CCA—

- (a) brings any goods to which this section or any other provision of this Act relates into or receives any such goods in the CCA, including any licensed or registered premises therein;
 - (b) produces or manufactures any goods therein;
 - (c) removes any goods therefrom; or
 - (d) otherwise deals with goods to which this section relates,
- shall, except where any provision of this Act otherwise provides—

- (i) be liable for the fulfilment of all obligations imposed in terms of this section or any other provision of this Act in respect of such goods;

- (ii) in addition to any liability incurred by any other person in terms of the provisions of this Act, be liable for the duty on such goods.

(9) The liability for duty in respect of any goods to which this section relates of an IDZ operator or a CCA enterprise or such other person shall cease—

- (a) if the IDZ operator or CCA enterprise or such other person proves that, as the case may be—

- (i) the duty on the goods concerned has been paid;

- (ii) the goods have been duly consumed or otherwise used in the manufacture or production of any goods by the CCA enterprise in accordance with any CCA enterprise permit and any relevant provision of this Act;

- (iii) the goods have been duly exported;

- (iv) the goods have, where relevant, been removed and received in any other premises registered or licensed under the provisions of this Act; or

- (v) any goods brought temporarily into the CCA are removed therefrom in accordance with the provisions of this Act and any conditions imposed by the Commissioner;

- (b) where liability otherwise ceases in terms of any provision of this Act, including in terms of any provision of any Schedule or rule made for the purposes of this section;

- (c) where the goods are abandoned or destroyed under the provisions of this Act.

(10) Any goods manufactured or produced in a CCA shall, when removed therefrom for any purpose other than export, except if otherwise provided in any Schedule or rule, be deemed to be imported goods.

(11) Notwithstanding anything to the contrary contained in this Act or the Manufacturing Development Act, 1993 (Act No. 187 of 1993), or any regulation or any other law, the Minister may, at the request of the Minister of Trade and Industry, in respect of any goods produced or manufactured in or removed for home consumption or exported from or brought into or used in any activity in the CCA, by notice in the *Gazette*—

(a) in a schedule which shall be deemed to be incorporated in Schedule No. 1 as Part 9 thereof and to constitute an amendment of Schedule No. 1, specify the duty leviable on goods manufactured or produced in, or any other goods brought into a CCA on entry for home consumption;

(b) in any item in a separate Part of each of Schedule No. 3, 4, 5 or 6, as the case may be, which shall be deemed to be an amendment of such Schedule, provide for a rebate, refund or drawback of duty in respect of any goods brought into, produced or manufactured or used in or removed from a CCA, in the circumstances and for the purposes and on compliance with any conditions that may be specified in such Part or item.

(12) Any amendment contemplated in subsection (11) may be made with retrospective effect from such date as may be specified in such notice.

(13) Notwithstanding the provisions of sections 48 and 75(15) any amendment to the said Part 9 or Schedule No. 3, 4, 5 or 6 shall unless otherwise specified in any amendment to any Schedule be made under the provisions of this section.

(14) The provisions of section 48(6) shall apply *mutatis mutandis* to any amendment to which subsections (11), (12) and (13) relates.

(15) 'Manufactured or produced' shall have the meaning applied in terms of this Act to goods imported into the Republic, and in determining the duty leviable in Part 9 of Schedule No. 1, the Minister shall take into account the preferential rates of duty in operation in Part 1 of the said Schedule No. 1 in respect of goods originating in a country which is entitled to such preferential rates.

(16) The provisions of sections 65, 66 and 67 shall, subject to the rules, apply *mutatis mutandis* in respect of the valuation of such goods.

(17) The Commissioner may make rules—

(a) to designate a CCA;

(b) to ensure the security and control of a CCA;

(c) to regulate the customs and excise administration of a CCA in connection with goods received or removed or manufactured or produced or consumed or any other activity to which this section or any other provisions of this Act relates;

(d) notwithstanding anything contained to the contrary in this section or any other provision of this Act, requiring that—

(i) any person who participates in any activity within or having access to a CCA must be licensed or registered in terms of this

Act;
(ii) any premises or area in the CCA used for any activity specified in such rule must be licensed as a customs and excise warehouse;

(e) to prescribe after consultation with the Director-General: Trade and Industry conditions and procedures regulating the activities and registration or licensing in respect of any enterprise or any other person partaking in any activity in, or having access to a CCA;

(f) after consultation with the Director-General: Trade and Industry in addition to or in substitution of any power, duty or function relating to the South African Revenue Service or any officer thereof or any procedure or process prescribed in the regulations;

(g) after consultation with the Director-General: Trade and Industry regarding duties or functions of an IDZ operator or a CCA enterprise;

(h) in respect of all matters which are required or permitted in terms of this section to be prescribed by rule;

(i) regarding any other matter which may be necessary and useful for the purpose of the effective and efficient administration of a CCA.

(18) (a) The Commissioner may refuse any application for a licence or registration required in terms of this section or cancel or suspend any such licence or registration.

(b) The provisions of sections 59A (2) or 60 (2), as the case may be, shall apply *mutatis mutandis* for the purposes of paragraph (a).

(19) Any person who, in connection with any activity to which this section relates—

(a) makes any false statement or makes use of any declaration or document containing such statement; or

(b) contravenes or fails to comply with any provision of this section or any other provision of the Act, shall be guilty of an offence and liable on conviction to a fine or to imprisonment for a period not exceeding 5 years, or to both such fine and such imprisonment and the goods in respect of which the offence was committed shall be liable to forfeiture in accordance with this Act.”.

Operational Customs Requirements within a CCA:

The following is based on the drafted version of the new IDZ Gazette, April 2005 and on the drafted Customs and Excise Act amendments of rules for section 21A, 2004.

21A.01

Definitions:

“CCA Customs Office” means an office within a IDZ operating under the Controller for the area within which the IDZ is designated which has been established by the South African Revenue Service on premises provided by an IDZ operator for the purpose of performing its functions in relation to any activity carried on in that CCA;

“CCA enterprise” means any person located in a CCA holding a valid CCA enterprise permit ...;

“customs control” means measures applied to ensure compliance with customs and excise laws and procedures and the VAT Act;

“customs and excise warehouse” means a licensed customs and excise manufacturing or storage warehouse;

“manufacturing warehouse” means a licensed customs and excise manufacturing warehouse;

“storage warehouse” means a licensed customs and excise storage warehouse;

The operational customs requirements especially with regard to the material flow in the CCA are mentioned within the following chapters of Section 21A. Nevertheless to provide all potential industries with competitive Supply Chain Processes they need to be reviewed.

21A.04	Designation of CCA and requirements in respect of premises, equipment and security
21A.05	Functions of a CCA Customs Office
21A.07	Duties and Functions of the IDZ Operator
21A.10	Manufacture and storage in and removal of goods to and from a CCA and documentation required for such goods
21A.12	Liability for duty
21A.13	Keeping of books, accounts and documents

ANALYSE THE STRATEGIC APPROACH OF DEDICATED SUPPLIER PARKS TO ATTRACT INTERNATIONAL INVESTMENTS

South Africa has one supplier park operational at Rosslyn servicing BMW, Nissan/Fiat and Ford. Another park at Nelson Mandela Bay servicing VWSA and GMSA is in the final stages of implementation. In addition, Toyota has commissioned a feasibility study in Durban to establish the viability of such a park next to its Prospecton plant. All these parks were researched, studied and implemented by the AIDC. The strategic approach is sound as it follows global assembly patterns and are normally in close proximity to large OEM's. Italy started this trend with its Melfi plant in southern Italy, soon to be followed by other OEM's in Leipzig, Saarlouis, Chicago and many more.

A typical strategy is followed by the AIDC in South Africa and some of the main purposes and goals are highlighted below.

Section A: Logistic & Light Industrial Assembly Park Strategic Plan

1.1 Purpose/Aim of the Park

The main aim of the Logistic & Light Industrial Assembly Park (LLIAP) is to steer the local Automotive Industry and non-automotive sector (to be identified) towards long-term sustainability. It will provide the suppliers and service providers of the Original Equipment Manufacturing (OEM's) plants of the Nelson Mandela Metropolitan Municipality (NMMM) with a value proposition (logistics and non-logistics services).

The LLIAP will provide the environment for grouping of different technologies, suppliers and service providers, to achieve economies of scale, as well as a world-class logistics concept, infrastructure development, shared services and buildings by 2007.

1.1.1 Specific sectors which would benefit:

The local (national) Automotive Industry will benefit from the development of the LLIAP that will contribute to the industry remaining competitive internationally. Local OEMs, OEM suppliers of components, parts and tools, as well as service providers will likewise benefit from synergies provided through economies of scale.

Other relevant industries and sectors will directly/indirectly benefit from the establishment of the LLIAP. The SMME sector will benefit from a myriad of opportunities that could lead to further development and growth as outlined below:

1.1.2 Benefits to the various sectors:

OEMs, suppliers and service providers will benefit from effective and efficient application of a number of proven concepts:

- The logistics concept will be applied, including development of a Logistics Center;
- The shared services will be provided from the Central Hub and other specified infrastructure;
- Coordinated Education, Training and Technology Development (ETTD) services will be facilitated;
- Infrastructure and infrastructure services development will be applied at the LLIAP;
- Access to a state-of-the-art ICT infrastructure will be provided *and*
- Business opportunities (including BEE and SMME concepts) are to be developed.

1.2 The envisaged Development Company's (DevCo) Short and Long Term Goals

1.2.1 DevCo's overall objectives

The DevCo's overall objectives are to be aligned with the stated purpose and aim of the LLIAP, to ensure the long-term survival of the automotive and non-automotive industry in the region through the development of the LLIAP.

1.2.2 The DevCo's Goals

- The DevCo's financial model has to ensure that the objective of creating a sustainable park is supported;
- Potential government funding is to be optimally applied and managed;
- Investors are to be attracted;
- Relocation to the LLIAP is a viable option for clients;
- Elements of identified risk have to be effectively managed;
- Supplier tenants are located at the LLIAP in accordance with the defined timeline as agreed by the relevant role players;
- Service Provider tenants are to provide essential (initial) services to the LLIAP as agreed between the DevCo, supplier tenants and service providers;
- Logistic services support is to be provided to tenants from the LLIAP Logistics Center (LC);
- Services to support tenants and the DevCo will be provided at the Central Hub (CH);
- Co-coordinated education, training and technology development services can be provided at the ETTC (Education, Training and Technology Development Centre) once agreement is reached between the DevCo, the different parties to the ETTC, OEMs, supplier tenants and investors.

1.2.3 Operational functioning in the short term, medium and long term

- The Board of Directors of the DevCo directs LLIAP operations.
- The DevCo's Core Team manages the day-to-day activities of the DevCo (and the LLIAP).
- An Executive Committee must be formed, especially once the intended Management Company (ManCo) is instituted.
- Elements of the LLIAP operations and related topics are addressed in the short to longer term. These are shown in table 1.2.3.

1.2.5 Strategic short and long term goals

Strategic and short-term (high road) goals will provide impetus to the LLIAP development programme.

1.3 Strategy to achieve goals

1.3.1 All major stakeholders (local government, governmental bodies & automotive industry players) support the LLIAP. The LLIAP provide industry with a value proposition in the form of shared service provision (logistics and non-logistics services).

1.3.2 The vision and strategic intent of the DevCo are:

1.3.2.1. The grouping of different technologies, services and service providers for various customers (automotive and non-automotive), in order to achieve synergies and fiscal optimisation through economies of scale.

- 1.3.2.2. The LLIAP is designed to contribute to the long-term survival of the Uitenhage/Despatch region through sustainable job creation.
 - 1.3.2.3. The upliftment of socio economical environment through economic rejuvenation and the stimulation of entrepreneurship.
 - 1.3.2.4. To be complementary to the business triangle (COEGA → UDDI → NMMM) rather than competitive.
 - 1.3.2.5. To promote the Uitenhage region to become a center of excellence within the automotive industry.
 - 1.3.2.6. To create an attractive environment (“the place to be”) for both international and local investors.
 - 1.3.2.7. The LLIAP is a Uitenhage Despatch Development Initiative (UDDI) generated project and can be seen as an Economic Investment and Infrastructure project for the Uitenhage/Despatch region:
 - Flexible investment is to be arranged to ensure the viability of the project
 - 1.3.2.8. Buy-in and support from ECPG, ECDC, UDDI, VWSA and Suppliers to the industry.
- 1.3.3 Strategic purpose of the LLIAP
- 1.3.3.1 Purpose
 - The LLIAP is an application of a world-class logistics concept
 - The LLIAP provides unique value proposition to potential suppliers and service providers wishing to relocate to the Park, this distinguishes it from a normal industrial park development
 - Implementation of the various concepts will achieve significant macro economic benefits
 - The LLIAP will be instrumental in sustaining jobs in the automotive and related industries by creating an environment for future growth
 - It will strive to integrate and seek mutual benefit within the Industrial Park networks in South Africa
 - 1.3.3.2 Advantages
 - The automotive industry is currently in a phase that is driven by the needs of the export market
 - The automotive industry’s level of competitiveness means that even small incremental production and logistics advantages can justify significant investment
 - 1.3.3.3 The LLIAP strategy is to be developed by the structures within the DevCo which will consist of various components in interaction with each other:
 - Each level of strategy and planning will be documented within DevCo structures and shall be available for perusal by interested stakeholders
 - DevCo’s Corporate strategy:
 - Approved by the DevCo’s share-owners
 - Formulated and directed by the DevCo’s Board of Directors
 - Determines the LLIAP future goals and direction:

- Provides strategic direction and intent
- Establishes future-oriented goals
- A corporate strategic plan is developed for the DevCo for share-owner approval
- The corporate strategy and strategic plan is to be directed in accordance with sound principles of corporate governance:
 - Concerned with satisfying the legitimate expectations for accountability and regulation by interests (stakeholders) beyond the corporate boundaries
 - Refers to how management and employees regulate their behavior with reference to decision making and the business environment
 - Refers to organisational relationships and structures, articles of association, fiduciary responsibility, shareholder reporting, assessment of pure risk exposure and assessment of SHE performance
- Business strategy:
 - Approved by the DevCo's Board of Directors
 - Formulated and managed by the DevCo's Executive Committee
 - Sets out how corporate strategy is achieved and refers to:
 - Business definition
 - Business vision (5 years)
 - Business mission
 - Business goals
 - Business key performance areas and indicators
 - Business strategic plan and budget
 - Business rolling forecast
 - A business strategic plan is to be developed for the DevCo for Board approval
 - The business strategy and strategic plan is to be applied in accordance with sound principles of business governance:
 - Incorporates the overall strategic direction and the overseeing of management actions
 - Focuses on the reality of corporate power (i.e. ability to directly affect corporate direction and control)
 - Defines interrelationships between business interests as well as internal organisational layers
 - Defines the most appropriate business model for the company by focusing on the way (defined) businesses are anticipated to perform
 - Defines the most appropriate company structure by developing sets of building blocks that are used to configure the organisation
- Departmental / functional strategies:
 - Approved by the DevCo's Executive Committee
 - Formulated and managed by the DevCo's departmental / functional management

- Sets out how business strategy is achieved and refers to:
 - Departmental / functional area definition
 - Departmental / functional area strategy
 - Departmental / functional area key performance areas and indicators
 - Departmental / functional area planning, budgeting and rolling forecasts
- Types of departmental / functional strategy:
 - Marketing strategy
 - Financial strategy
 - Operations strategy
 - Communications strategy
 - Manpower strategy
 - Legal services strategy
 - Corporate and management support services strategy
- A functional plan is developed for each functional area for Executive Committee approval
- Each functional area strategy and plan is directed in accordance with sound principles of functional governance that is derived from the approved DevCo's corporate and business governance.
- For each functional strategy a set of sub-strategies may be developed, e.g. a marketing strategy for each of the customer groupings, including tenants and investors.
- Time and expenses incurred in developing and implementing each strategy is to be included in the DevCo's budget.

1.3.4 Strategic alliances are to be developed for each phase of the project:

1.3.4.1 In the scoping phase, representatives of various interested parties investigated the need for a park of this nature:

- UDDI
- VWSA
- AIDC

1.3.4.2 In the feasibility study phase (September 2003 to January 2004) a number of partners were involved

- Government and community partners
- Supplier partners
- OEM partners
- Service partners

Lack of understanding and interpretation of benefits / value proposition leading to additional cost to attract clients

- Cheap land and vacant buildings attracting clients
- Human Resource activities in the park that may influence the labour force of tenants during labour problems;
- Non-conformity to investor standards in pricing and rental of standard buildings that may lead to disgruntled investors;
- Environmental impact of the LLIAP that has to be monitored and managed;
- Socio-economic impact of the LLIAP in the Uitenhage area and other areas that has to be monitored closely;
- Informal settling on property that has to be prevented;
- Lack of trade union buy-in into the concepts of the LLIAP may lead to union action;
- Negative reactions by public and major stakeholders to impact that the LLIAP may have on the environment, the industry and the economy;
- Spending of funding not in accordance with agreed spending pattern and
- Delays in commencement of development and closure phases

1.3.6.1 It is important to ensure that the final objectives are achieved and that the concept stays flexible by managing the risk:

- The LLIAP risk model is a rolling model that is reviewed on a monthly basis
- Reinvestment of ECPG funding will be in accordance with approved agreements:
 - Difficult to obtain new funding
 - Limited control to achieve final objective
 - Difficult to manage changes in the environment
- A Board decision should be taken regarding ECPG investment in the Park:
 - Repayment in accordance with agreements (e.g. when project is stabilized)
 - Use investment to offset market competition
 - Use investment to manage risk
 - Some land may be sold
- All the land is sold to an investor or investors:
 - Difficult to manage changes in the environment
 - Investor is focused on short term returns
 - Limited control to achieve final objectives
- No land is sold to an investor
 - Increase in property holding
 - Difficult to get investor

1.3.6.2 Investment in the LLIAP is guided by characteristics of the Park that in themselves will aim at reducing the overall risk of investment:

- The Logistics & Light Industrial Assembly Park (LLIAP) is based on a world-class automotive supplier logistic concepts and design principles.
- The LLIAP has a value proposition that distinguishes it from a normal industrial park development:
 - It is expected to achieve significant macro economic benefits;
 - It will sustain jobs in the industry and
 - It will create an environment for growth
- Independent comparative studies have identified the Uitenhage site as being the most feasible for a LLIAP, deriving the most advantages and meeting all critical aspects.
- The LLIAP provides a unique and low risk niche investment in a growing export market. The characteristics of the nature of the investment
 - **The purpose is unique in South Africa and it provides a strong value proposition for potential users / tenants**
 - **The LLIAP concept is modeled on global best practice adapted for South Africa's circumstances providing cluster synergies, outsourcing of logistic processes, shared services / infrastructure, supply chain benefits, and manufacturer focus on core production and quality rather than logistical processes**
 - **Significant start-up investment in infrastructure and concept development is required by Government to minimize risk**
 - **Tenants and their customers derive synergies that induce participation and integration creating a convincing market endorsement and take-up of sites**
 - **Market interest has been extensively researched and canvassed**
 - **As a result of the cluster synergies direct mutual benefits flow to both the principal customers and the Park tenants**
 - **Integrated cost benefits are easily determined due to existing close relationships within the industry**
 - **The LLIAP concept has engendered strong stakeholder and political support**
 - **The land has been acquired and is held centrally**
 - **Development design and town planning aspects have been costed, are approved and initial stages are being implemented**
 - **Social and economic benefits are positive and strong (e.g. job creation and multiplier effects) creating and maintaining a sustainable environment for long-term growth**

- **The concept supports the latest manufacturing trends (JIT/JIS) – considered critical and therefore a necessity by the OEMs**

1.4 Delivery Vehicle

1.4.1 Legal form of company and registration details

- A company should be set up to co-ordinate, plan, oversee and manage the development of the proposed LLIAP as a strategic economic investment and infrastructural project advanced by partners.
- The name for the Park needs to be researched and approved by the Registrar of Companies prior to the Design Phase.
- A few directors will have to be appointed to a Board of Directors of the DevCo.:
 - Possibly ECDC (Director)
 - Possibly UDDI (Director)
 - Possibly AIDC (Director)
 - Possibly UDDI Appointed (Managing Director)
 - Possibly VW (Non-Executive Director)
 - Possibly Institutional investor (Director)
- The DevCo and its directors should affirm their commitment to the principles of openness, integrity and accountability in accordance with high standards of corporate governance and with local and internationally accepted corporate practice.

1.4.2 Shareholding and basic description of obligations

- Initially the major funder should have 100% shareholding in the DevCo.
- The proposed financing of the LLIAP over a twenty year period must be flexible to accommodate different investment models.
- A set of institutional and governance agreements should be put in place to facilitate the investor / shareholder process:
 - Draft shareholder Agreements, and where necessary compacts, will allow the investment of public funds to be tracked and accounted for (Public Finance Management Act) and will become final once an institutional investor is on board;
 - Clear obligations for stakeholders and appropriate/ respective equity participation (e.g. dividend policies, minimum performance levels and timeframes) *and*
 - Alternative corporate structures should be considered and the Board of the DevCo should be willing to review these

1.4.3 The LLIAP's organization structure (I think we should not distinguish between Manco and Devco, in our experience this does not work and creates confusion. Keep it functions in the same legal entity)

1.4.3.1. The development company (DevCo):

- LLIAP's project team must be directed by the DevCo and project managed by no less than two members.

- Officials manage development activities of the company during the early LLIAP phases. The officials will take responsibility for areas of the LLIAP's business.
- A Core Team must be formed to meet on a weekly basis to report on, and to manage, the latest project status and progress.
- Members of the Core Team are required to act as point-of-contact for each of the relevant project management and reporting areas:
 - Land & Infrastructure should be managed by Professionals with the following sub-units (managed by the institution as indicated):
 - Property;
 - Infrastructure;
 - Traffic;
 - Town Planning;
 - Environmental ;
 - Architects and
 - Urban Design.
 - Customer Processes can be managed by the AIDC
 - LLIAP non-logistical services can be managed by the AIDC
 - Logistics Concept can be managed by VW and the AIDC with two sub- units (managed by the institution as indicated):
 - Concept Development AIDC and
 - OEM Steering Community (VW).
 - Information and Communication must also be managed.
 - Legal advisory support should also be provided.
- A DevCo Executive Committee must be formed to apply corporate and business governance principles on behalf of the Board of Directors of the DevCo. Line management positions must be developed, advertised and filled for the effective and efficient day-to-day management of the LLIAP project within 2 to 3 years
- Functions of the DevCo's Corporate or Group Secretary must not be outsourced fully. Legal advisory support could still be outsourced although a single point of contact for legal and corporate governance matters must be maintained.
- The establishment of a separate DevCo and ManCo will call for a revision of the corporate governance, business governance, business model and structure of the DevCo.
- The proposed DevCo project structure for the LLIAP allows for typical project development and construction activities to be managed effectively and efficiently
- Options for the restructuring of the DevCo should be considered:
 - Base option:
 - Retention of the DevCo in its current structure to direct and manage developmental and operational activities even beyond 2007
 - Alternative 1:
 - Restructuring of the DevCo as a holding company for two companies, i.e. a ManCo and DevCo by February 2006
 - Alternative 2:

- Restructuring of the DevCo into two separate companies each with a separate shareholding model, i.e. a ManCo and DevCo by 2006
- o Alternative 3:
 - Combinations and permutations of the above options based on any number of issues and considerations. Timing and structuring considerations should meet investor / share-owner requirements
- o Other alternatives, based on stakeholder and share-owner preferences, must be considered,

1.4.3.2. The LLIAP management company (ManCo):

- In the event of the deployment of an LLIAP ManCo and a DevCo, the DevCo, will remain the primary development body with a ManCo to co-exist with the DevCo.
- The ManCo could be formed by February 2004 to manage the day-to-day operations of the LLIAP in Uitenhage on an interim basis until all the relevant day-to-day LLIAP management functions are transferred from the DevCo.
- A ManCo Board of Directors and a ManCo Executive Committee should be formed by the share-owners

1.4.3.3. Management support:

- The DevCo should use a Consultant Support Pool in those areas where it does not have either expertise or capacity.

1.4.4 Overview of internal monitoring mechanisms

1.4.4.1 An audit committee should exist for the DevCo as part of the duties of the Board of Directors

1.4.4.2 Signing powers for members of the Board of Directors, the LLIAP Project Team and the Core Team must be developed and promulgated

1.4.4.3 Data collection for relevant LLIAP development and management actions must be coordinated by regular Core Team and Project Team meetings and work sessions

1.4.4.4 The LLIAP project must be managed along sound project management principles with the appointment of responsible parties, attention to issue resolution and documentation of project reporting within the broader management system

1.4.5 Overview of financial prospects

1.4.5.1 Financial model

The DevCo's Board of Directors has to ensure that the LLIAP financial model is in line with ECPG Treasury's requirements, has to show risk and return and has to be structured based on the basis of a number of concepts:

- ECPG contribution
- Institutional investor contribution
- Investment in infrastructure, development and risk

- Return on investment

The financial model for the LLIAP is shown diagrammatically:

1.4.5.2 Assumptions

- Land assumptions.
 - The total area of the park is 100ha
 - The initial development will be in precinct A to an extent of 42 ha No further developments are taken into consideration in the Cash flow model.
 - 30% of the total park area can be developed
 - The total estimated land cost is excluded as indicated as a denotable portion as indicated by UDDI
 - A piece of land excluded in the center of the Park belongs to United Cement. It does not infringe on the development of Precinct A
 - The total transfer cost is assumed to be negligible
 - Full rates and taxes will be payable on the land
- Phase assumptions:
 - The phases in the park will be developed according to the demand
 - The model estimates that precinct 1 as a phase in the park development to be completed in 2 years
 - The land cost was estimated as zero as there are indications that the Metro will give the land for free
 - The cost exclude setup and administration cost
 - Economic assumptions:
 - Inflation was calculated at 9%
 - Annual inflation increases was calculated at 10%

1.4.5.3 Basic financial analysis and reporting

- Basic financial reporting and analysis results are provided here to support the LLIAP strategic plan and the business plan
- The full financial model for different scenarios for the LLIAP is available to support this business plan
- The model is very sensitive for changes in any of the stated parameters
- The model was developed based on market predictions
- The LLIAP cash flow analysis is shown diagrammatically for more than the required 36 months:
 - Three scenario's exist (detail Balance Sheets and Income Statements are attached):

- Scenario 1: The Government takes the risk of the development, and fund the total development, a total contribution of R 394 million. No external funding from Banking Institutions are obtained to cover a portion of the development. No interest is payable. Government can then earn the full return on investment, or even sell the company later to Investors.
- Scenario 2: The Government fund the Infrastructure plus a subsidy on the first building, a total contribution of R 100 million. Banking Institutions have to provide the funding to develop the rest of the park. There is however a risk in this approach, as it is unlikely that the Banking Institutions will make funding available without a deposit on the additional production buildings. Interest at 11.5% is payable to the banks.
- Scenario 3: The Government funds the Infrastructure, as well as a total subsidy of 45% on the production buildings, a total contribution of R 233 million. This will minimize the risk that the further funding of the buildings will not be received from banking Institutions. The Banking Institutions then fund the rest of the development.
- Basic Assumptions that are used in all three models:
 - The ECPG funding are capitalized as share capital and a share premium
 - The Banking Institutions funds are shown as a Current Liability under Cash and cash equivalents, although it will rather be a Non-current liability in the end.
 - Surplus cash are shown as a Current Asset under Cash and cash equivalents
- ECPG funding that must be acquired is assumed to be used to kick start the development of the LLIAP
- Institutional investment is critical to ensure development of the LLIAP beyond the first 24 month period, for further phases in the LLIAP.
- Steady and early movement of tenants into the park and the soonest possible involvement of institutional investors will improve the cash flow
- The timing and the extent of LLIAP development cost is influenced by the extent and the nature of development of OEM supplier buildings as well as service provider facilities and LLIAP infrastructure:
- Initial development cost is incurred to develop the first OEM logistic building
- Further development of OEM supplier facilities are provided as more tenants sign lease / buy agreements
- Service provider buildings are developed mostly during the first two years to support the relocation of OEM suppliers to the LLIAP
- Infrastructure cost is incurred to ensure the smooth relocation of tenants to the LLIAP
- Total income statements for the 12 years ending February 2005 until February 2016 respectively are provided to support the analysis of LLIAP cash flow information provided in this business plan:

- Potential ECPG investment of R 100 m is provided in each scenario by the end of the 2004/2005 period to kick start the development of the LLIAP
- Institutional investments are required to cover additional development cost requirements, as per the three different scenario's
- Tenant income from rental agreements will steadily increase across the first two years

The Logistic & Light Industrial Assembly Park (LLIAP) project:

2.1.1 Outcome of LLIAP project

The LLIAP's aim and delivery model will support the steering the South African Automotive Industry towards long-term sustainability whilst serving the Original Equipment Manufacturing (OEM) plants of the NMMM.

The development of the LLIAP Park will include application of a variety of concepts and will attract international and South African OEMs, suppliers and service providers.

A value proposition was developed for each interested supplier and service provider tenant that is interested in relocating to the LLIAP

2.1.2 Goal of LLIAP project

- The LLIAP project is to be aligned to the aims, objectives and goals of the DevCo
- The feasibility study conducted has highlighted advantages and benefits for tenants/OEM relocating to the LLIAP. The full feasibility study documentation is available. The study findings will be revisited during the intended value proposition study that is to be conducted during February 2004.

The real logistics benefits for a prospective supplier park tenant may be calculated by using the value proposition model and case study that is being developed.

An evaluation of all relevant cost structure improvements for a prospective tenant considering relocating or extending its business to the supplier park will provide the required inputs into a business case to be developed for that tenant.

- The main saving opportunities that have been identified are the following
 - Savings to the customer of the supplier;
 - Consolidation of incoming goods;
 - Consolidation of outgoing goods and
 - Effective and efficient management of the logistics infrastructure.
- Calculated savings for a supplier relocating or extending its business to the LLIAP are at least the following:
 - Rental cost will increase for new buildings;
 - Non-logistic cost will decrease (economies of scale and critical mass)
 - Logistic cost will decrease (Outbound transport cost) and the
 - Net effect will result in a saving
- Potential additional supplier savings (including savings form sharing of services) for a supplier relocating or extending its business were identified but were not calculated:
 - Indirect cost factors due to consolidation of two factories;
 - Consolidation of inbound logistics cost;
 - Centralize logistic activities provided by the LSP;
 - Consolidated ICT system;
 - Economies of scale:

- Canteen;
- Maintenance (general);
- Training;
- o Impact on the environment: long term stability and flexibility;
- o Sound infrastructure: roads, container yard and
- o Potential of optimizing plant layout (i.e. space requirements).
- Quantification of all goals of the value proposition study can be available by April 2004.
- During the construction, part of the LLIAP development phases the levels of employment and BEE involvement will be aimed at providing construction support. After the first three years employment and BEE involvement will support the operations of service providers and OEM suppliers.
- Due attention will be given to entrepreneurial and SMME opportunities during the development phases of the LLIAP project.
- Stakeholders will be involved in continually identifying quantified and qualified LLIAP relocation benefits.

Investment opportunities

3.1.1 List and brief description of investment opportunities

Specific investment opportunities are identified where an investor may decide to either get involved with part of the development of the LLIAP or with the full Park development:

- Phased infrastructure development:
 - An application can be submitted to DTI on the critical infrastructure fund to the value of 20% to 30% of the Infrastructure investment, which DTI will refund after the Investment has been made. This is however maybe a risky option and should be seen as the cherry on top, to be used for further development of the park. The CIF is currently frozen because of administrative problems between DTI and the World Bank.
- Phased OEM supplier facility development:
 - o Investment is required to develop facilities for OEM supplier tenants together with OEM suppliers and OEMs
- Phased service provider facility development:
 - o Investment is required to develop service provider facilities together with service providers
 - o Logistical Service Centre development:
 - As part of the identified R200m investment
 - o Investment is required to develop the Logistical Service Centre together with OEMs
 - o Investment is required to develop the Central Hub:
 - As part of the identified R200m investment

3.1.2 General characterization of who might be interested in such an investment:

- 3.2.2.1 A number of investors may be interested in investing in the LLIAP:
Institutional investors (to get involved with the full LLIAP development programme)
- 3.2.2.2 Requirements of institutional investors are normally:

- A strong legal entity with a strong Balance Sheet should be the owner of the park and the owner of the lease agreements.
- The leases should be watertight and should be signed by the operating entity generating cash flow, and not by a shell holding company.
- The lease agreement will be ceded to the Banks and they will discount the cash flow of the lease agreement and hedge the risk of the loan on the discounted cash flow.

3.2.2.3 Indications are that the banks will provide funding at Prime interest rate minus 1.25%.

3.2.2.4 Smaller institutional investors and other investors (to develop part of the facilities)

3.2.2.5 Private investment may be attracted (including supplier companies and developers).

3.2.2.6 A consortium of investors, who might consist of an Institutional Investor, a Property Developer, a Logistic Service Provider and a Facilities Manager, who can each derive benefit from the Park.

Sourcing tenants and investors

3.3.1 Strategy to attract commercialisation of infrastructure

A separate strategy each for marketing of the LLIAP to potential tenants, investors and other parties are being developed and formalized.

Local Government needs to provide significant start-up investment in infrastructure and concept development. Further requests for assistance should also be considered.

Individual supplier and service provider tenants may opt to buy their own facilities.

Interested institutional investors will be attracted from DevCo Board level (e.g. via governmental / share-owner representation).

Alternative sources of funding are identified, e.g. the DTI in developing a value proposition model for LLIAP tenants in close cooperation with OEMs, OEM suppliers and service providers.

3.3.2 Resources set aside for these activities (human and financial)

Core Team resources (human and financial) are provided to develop marketing and sales strategies and plans.

3.3.3 Channels, organizations and companies to be used

The process of identifying, analyzing and attracting LLIAP investors is formalized.

3.3.4 Timelines of the approach (commenting on lead times for key investments)

The most critical element of the investor attraction process is that the first service provider facilities must be available by September 2004.

Involvement of institutional investors is critical to reduce dependency on possible Local Government funding and to lower the risk when project uptake is higher than expected.

Tenant and investor options

3.3.5 Options in terms of type of contract or investment

3.3.6 Alternative contractual agreements are considered to govern the deployment of investment funds, e.g. Lease Agreements, Sale Agreements together with a Body Corporate agreement, and Shareholders Agreements Indications of price ranges or investment costs

Development cost is at about R2500 per m² for office and factory areas

3.3.7 Anticipated returns (where applicable)

Returns on the project (as calculated over a ten year period) are provided in the LLIAP's financial model .Rental prices that are used is market related. It seems that a significant Government Grant is necessary to subsidies the building cost in order to make it affordable for the tenants.

The DevCo's Relationship with ECDC and ECPG

3.3.8 Synopsis of proposed relationship

ECDC should seek representation on the Board of Directors of the DevCo.

Start-up investment for infrastructure and concept development must be provided by ECDC to minimize LLIAP project risk.

3.3.9 Possible areas of potential future collaboration

ECDC must continue to play a leading role in developing the DevCo into a possible future combination of a DevCo (a development company) and a ManCo (management company.)

ECDC could assist in improving the effectiveness and efficiency of LLIAP tenants, development of BEE and SMMEs and further infrastructure development are areas of possible future cooperation between the DevCo, ECDC and other LLIAP stakeholders.

5. IMPACT

Socio-economic impact

The LLIAP is aimed at stimulating economic activity in broad based economic sectors and therefore improves the quality of life for the Uitenhage/Despatch people.

The LLIAP is a new and pioneering concept in our country that will help to keep the domestic automotive and non-automotive industry globally competitive. It will also confirm the Eastern Cape as an emerging hub of the South African Automotive Industry.

Its success will encourage sustainable growth as well as further investment in the domestic industry. It will benefit neighbouring communities and the region through job creation and generating economic opportunities, e.g. for SMME's and emerging business generally. The LLIAP will also encourage the automotive industry to survive and prosper in difficult markets. This will in turn benefit neighbouring communities, The Nelson Mandela Metropolitan Area and the Eastern Cape citizens in general.

The social impact of investment in infrastructure development and the upgrade of facilities once companies move to the Park will be significant. The Park will attract further investment from both domestic and international sources and create job opportunities in both the development and operational phases. Importantly, there will be an increase in the pool for skilled people in the community and larger income per capita, with all the spin-off benefits for the local economy that it implies.

Other impact

The socio-economic impact of the relocation of automotive component manufacturers to the LLIAP of Uitenhage still needs to be investigated in further study. The first studies has revealed the following job creation contributors:

Employment type created	Activity	No. of jobs	Range of services
Construction	Construction	4650	Skilled, semi-skilled and unskilled labour
Full-time	Park Services	160	Park man., security, maintenance, medical, etc
Full-time	Tenants	500***	Direct, indirect, admin labour and future growth
Full-time	Tenants	1100***	Second phase growth, knock-on employment

***Source of the multipliers is courtesy of GTKF-NMBICC Feasibility Report;**

****Source of the employment is based courtesy of the Rosslyn ASP Benchmark**

*****Source of the expected growth is based on the Garnet Adams Socio-economic Report for the NMBLP**

*****Permanent staff in industry growth an additional 5 % potential increase**

The study should be based on samples of the nine earmarked companies that intend to relocate to the LLIAP. The combined workforce is in excess of 2000 employees.

The study should also assess how the development of the LLIAP would lead to the relocation of companies to Uitenhage:

- Social and economic impact of the relocation will be experienced:
 - In areas from where suppliers are relocated
 - In the Uitenhage area
- The scope and size of the socio-economic impact are driven by three factors:
 - Geography:
 - 60% of companies relocate within their current geographic area of operation

- 40% of companies relocate from different geographic areas (e.g. from Brits to Uitenhage)
- Cost structure:
 - 79% of affected companies' cost base is for raw materials
 - Suppliers of raw materials will not be affected
- Transport infrastructure:
 - Appropriate public transport is lacking
 - A dilemma of either incurring considerable additional expenses (time and financial) or to relocate to an area less than 50km from Jagtvlakte needs to be investigated

Other areas that would be impacted by the relocation to the LLIAP cover the following areas of socio-economic interest:

- Security services;
- IT product and service providers;
- Cleaning service providers;
- Property leasing service providers;
- Facilities management;
- Canteen and catering service providers;
- Equipment maintenance;
- Financial and legal service providers;
- Transport service providers and
- Public service providers

The envisaged DevCo's awareness of the socio-economic impact of relocating suppliers to the LLIAP allows the DevCo and relevant stakeholders to manage the risk exposure thereby minimizing elements of negative impact.

G. SOUTH AFRICAN OPPORTUNITIES – VEHICLES

We have mentioned earlier the forthcoming export programmes expected from Toyota, Ford and GM.

In addition to these there are some other opportunities for vehicle production. These include:

The Taxi Recapitalisation Project

The government is going ahead with its programme to replace all minibus taxis in South Africa with 18 or 35 seat buses with a high-level design and safety specification. The successful companies (two or three) will therefore have two options. They will either produce vehicles in their own greenfield plant, or they could have their buses built by an existing OEM on a contract assembly basis. The first option would provide an opportunity for ELIDZ. This opportunity would also extend to local component companies, as the buses will have to comply with minimum local content requirements on a progressive basis, and some of the components required are not presently produced in South Africa. Where new component facilities are needed, these would be established in close proximity to the assembly plant. While the total volumes required are not very high, there would be export opportunities for the buses as well as for their components.

Lightweight, alternative power vehicles

There are at least two South African-designed vehicles which, although experimental at this stage, have the potential to be exported to first-world countries. They have lightweight moulded or fibreglass bodies, and partial or wholly electrically-generated power. One such example, the Electric Utility Vehicle, was exhibited in October 2001 at the EquipAuto show in Paris and aroused some interest from European buyers. Apart from electric power, the body is made from natural fibres (mainly sisal). This is a joint venture between Eskom and other partners. Since almost the entire volume would be exported, such vehicles should be produced at the coast. This would be another opportunity for ELIDZ, as there would be several suppliers of components also required.

Lightweight vehicles, alternative metals such as Magnesium

The CSIR's Manufacturing and Materials Technology centre and Mintek are of the opinion that magnesium could be manufactured competitively in SA in future. Currently OEMs are using magnesium alloys for some engine, gearbox and interior trim components ranging from 4 to 25 kgs per car. This is expected to grow to 100 kgs per car by 2010. As the price differential between aluminium and magnesium narrows, OEM's are expected to switch to magnesium at the cost of steel, cast iron, aluminium and plastics. In order to secure enough magnesium supply to their second tier suppliers, VW, Ford, GM, DaimlerChrysler, Hyundai, Fiat and Renault has formed JV relationships with various magnesium producers in Israel, Australia, Ukraine, Canada and Norway.

These developments affords SA the opportunity to attract at an early stage of the product development life cycle the raw material producer and related automotive component manufacturers as very little capacity is idle and supplies are becoming more available. The auto sector popularised PGM's and stainless steel for catalytic converters and magnesium is at that same point in its demand cycle.

Heavy Commercials and Buses

Despite the fact that protection in this segment has been reduced significantly, so that tariffs on imported trucks and buses is 20%, while all components except tyres are duty-free, the exports of these components and vehicles still

qualify for MIDP benefits. This means that the local production of built-up trucks and buses for export, either with or without the bodies, could be an opportunity.

In particular, the duty-free entrance into the United States offered by AGOA is particularly attractive, as duties are normally 25%, except for medium truck chassis cabs only, which are lower. The qualifying local content requirements are only 35%. It could therefore make sense for a third-country truck manufacturer to set up truck assembly at a local port for export to the USA and other countries.

New entrants

Although the reducing tariffs will make vehicle importation progressively more attractive, this is only the case if the vehicle producer is prepared to enter into component export programs from South Africa, with the associated investment requirements. A potentially easier way of entry is to assemble vehicles locally, some of which would be destined for export, as well as exporting some of the components sourced locally to support the vehicle production. While this requires a higher initial investment, it enables the manufacturer to import other models thus providing dealers with a full range of products, instead of just one or two. Establishing a proper dealer network has been a limiting factor in several of the fully imported brands, and is much easier with a full range of products.

Possible new entrants could be some of the existing importers, such as the French models, or new entrants from India looking to access new markets. The MIDP benefits could provide such an opportunity to these manufacturers, particularly from China and India, countries which the South African government would like to see invest here.

Since new entrants will undoubtedly include significant exports in their vehicle production plans, it will make most sense for any such companies to locate at or near a port.

AGOA

As mentioned earlier, the AGOA enables vehicles produced in South Africa, with at least 35% local (including U.S.) content, to obtain duty-free access to the United States. This, together with all the MIDP benefits, could be attractive for European and Asian manufacturers to consider investing in South African vehicle production. Again, it would be logical to produce these vehicles at a port that has easy access to the U.S.

SOUTH AFRICAN OPPORTUNITIES – COMPONENTS

As discussed earlier in the section on [Global Platform rationalisation](#), it is expected that as OEMs develop and produce high-volume global platforms opportunities will be created in emerging markets. These will be not only for a share of the vehicle production volumes for these models, but also to produce components that are more easily transported to other markets producing the same platform. The specific types of components produced in each market will be determined primarily by the respective OEMs in conjunction with their global suppliers. However, we believe that local incentives in the various countries and regions of the world will play a part in the sourcing decisions. With the assurance that the MIDP will continue to at least 2012, South Africa will become an increasingly favoured source of high-volume world-class components, an opportunity that the ELIDZ must not let pass by.

An often-overlooked opportunity is that of second tier and aftermarket parts. The vehicle population in first-world countries, in particular the USA and Europe, is at a level where it sometimes can be unattractive for first-world supplier plants producing components in the millions, to meet these requirements, but the volumes are still high by SA standards. It is often relatively simple to transfer specific tooling to another country, such as South Africa, for this ongoing production.

These aftermarket parts, particularly proprietary items, are often sold at prices higher than those for the equivalent OE component. With the benefit of the MIDP, returns on the relatively small investments required can be high. This

opportunity exists also for heavy trucks and buses, where the vehicle population is often hundreds of thousands, and aftermarket parts demand runs into tens of thousands of pieces annually.

Earlier, under “Component Manufacturer Consolidation/Opportunities”, we outlined the types of components as well as the desired companies identified by the OEM/DTI Purchasing Group.

We present below capsule summaries of the major component suppliers identified as possible candidates for future investment in South Africa, including the airbag manufacturers and Magna, identified elsewhere as potential investors.

- AMP. This company, part of Tyco Electronics, is the number one manufacturer of electrical connectors in Europe. Tyco’s well-known brand names include AMP, Raychem, Potter & Brumfield, Alcoswitch, and many others. Products include connectors/interconnection systems, relays and modules, circuit protection devices, fibre optic components, wire and cable, switches, wireless components, sensors, printed circuit boards, touch screens and application tooling. They also provide products to insulate, protect, hold, bundle and identify high-performance electrical businesses.
- Arvin Meritor. ArvinMeritor, Inc., became operational in July 2000 when Meritor Automotive Inc., a global supplier of components and systems for light, commercial and speciality vehicles, merged with Arvin Industries Inc., a leading world manufacturer of exhaust systems and ride control technology. The new group has over 150 plants in 26 countries. Through the merger of the two companies, ArvinMeritor aims to widen its product range and become a global provider of integrated solutions for light and heavy vehicle chassis, drivetrains and exhausts as well as roof and door modules and systems. The company, headquartered in Michigan, makes components for commercial vehicles (axles, brakes, transmissions, and clutches) as well as for light vehicles (door, roof, exhaust, and suspension systems). ArvinMeritor also offers light vehicle aftermarket products such as mufflers, filters (Purolator), and shock absorbers (Gabriel). The company sells private-label aftermarket parts through retailers such as Pep Boys, Midas, AutoZone, and Meineke. Existing South African subsidiaries do not make doorlocks or new generation manifolds.
- Autoliv. Based in Sweden, it’s the world’s #1 producer of car safety equipment. The company makes components such as airbags, seat belts, anti-whiplash systems, and safety electronics. Other products include rollover-protection systems, steering wheels (with airbags), and child seats. Customers include all major carmakers. Europe accounts for 53% of sales; the US accounts for 38%. Autoliv has 19 crash-test tracks, eight technical centres, and production facilities in more than 30 countries.
- Calsonic Kansei Corporation. Established in 1938 and is engaged in mainly the manufacture of heat-related car parts. Car airconditioning systems, ventilation systems, heat exchangers accounted for 89% of fiscal 1999 revenues; sales of communication and information systems and information services, 9% and other, 2%. The company has twenty five consolidated subsidiaries, eight in Japan, five in the United States, three in the United Kingdom, two each in South Korea and the Netherlands and one each in Australia, Spain, Mexico, South Africa and Poland. Overseas sales accounted for 36.7% of fiscal 1999 revenues. Nissan Motor Co., Ltd. is the major shareholder with 33.4% of issued stock. Calsonic in South Africa does not manufacture the airconditioning compressor.
- Delphi Automotive Systems. The world’s largest maker of auto parts, Delphi has been spun off from General Motors, the world’s largest automaker. With operations worldwide, Delphi makes virtually everything mechanical or electrical that goes into cars, including brakes, chassis, engines, and thermal, electrical, and steering systems. Delphi operates 190 manufacturing plants in 31 countries. More than 70% of Delphi’s business comes from former parent GM, but the company expects to broaden its customer base now that it is an independent company. To that end, Delphi is expanding the worldwide reach of its aftermarket business.
- Denso Corporation. Established as Nippondenso Co., Ltd. by separating from Toyota Motor Corporation in 1949 and changed name to Denso Corporation in 1996. The company is now one of the world’s largest

suppliers of automotive components and systems. Automotive related business including car air conditioners and systems, electrical automotive heating systems, electronic control products, fuel management systems, radiators, meters and filters accounted for 90% of revenues and non-automotive products 10%. Overseas sales accounted for 38.4% of fiscal 2000 revenues, while sales to Toyota Motor Corporation accounted for 33.1%. The company is affiliated to Toyota Motor Corporation, which holds 24.95% of issued stock.

- GKN. GKN plc(GKN). The Group's principal activities are divided into three core businesses: AUTOMOTIVE: GKN's Automotive Driveline Division (ADD) is a world leader in the design and manufacture of driveline system products with more than 37 per cent of the global market for constant velocity jointed driveshafts. ADD designs and manufactures driveline system products and provides worldwide driveline system integration support, and manufactures many transmission and engine components. AEROSPACE: Supplies structures, components, assemblies and engineering services to aircraft and aero-engine manufacturers. INDUSTRIAL SERVICES: Pallet and container pooling; waste management; pallet and container racking; undercar service franchise. Automotive systems accounted for 61% of 2000 revenues; aerospace, 33% and industrial services, 6%.
- Hella KG Hueck & Co. This privately owned German company is the number one light manufacturer in Europe, a global player with innovative products and systems in lighting technology and electronic modules for motor vehicles. Hella has been creating products for motor vehicles ever since 1899.
- Kiekert AG. Founded in 1857 and publicly traded since 1994, it is primarily engaged in the manufacturing of locks, central locking systems and other electronic components especially for the automotive industry. Kiekert supplies 35 car manufacturers worldwide, including Mercedes-Benz, VW, Ford and Opel. The company is the world's biggest manufacturer in its line of business, with its production output accounting for more than 50% of the European car lock production. The company has subsidiaries in Italy, France, Great Britain, Ireland, the Czech Republic, Mexico and the USA. The production of system locks accounts for 34% of revenues; locks, 22%; modules, 19%; central locking systems, 10%; electronic components, 7%. 2000 Revenue was \$670 million.

Magna International Inc. – Detailed Profile

Magna and its subsidiaries design, engineer and manufacture a diversified range of automotive parts, components, assemblies, modules and systems. The Company also engineers and assembles complete vehicles, primarily for sale to original equipment manufacturers (OEMs) of cars and light trucks in North America, Europe, South America and Asia. Magna's products include exterior decorative systems, interior products including complete seats, instrument and door panel systems and sound insulation, stamped and welded metal parts and assemblies, electro-mechanical devices and assemblies and navigation systems, a variety of plastic parts, including body panels, fascias and front rear-end modules through Decoma International Inc., various engine, powertrain and fuelling and cooling components through Tesma International Inc., a variety of drivetrain components and complete vehicle engineering and assembly.

As of December 31, 1999, the Company had 174 manufacturing facilities (including 12 joint venture facilities), comprised of 103 in North America, 66 in Europe, two in Korea, two in Brazil and one in China, as well as 33 product development/engineering facilities. In North America, Magna's primary customers are DaimlerChrysler AG, Ford Motor Company and General Motors Corporation, as well as certain North American subsidiaries of foreign-based OEMs, such as BMW, Honda, Isuzu, Mazda, Suzuki, Nissan, Toyota and Volkswagen. In Europe, Magna's customers include most significant OEMs, such as Volkswagen/Audi, BMW/Rover, DaimlerChrysler, Ford/Jaguar/Volvo, General Motors/Opel, Honda and Renault/Nissan.

The Company's SteyrSymatec group provides complete vehicle engineering and assembly services, supplies technologically advanced integrated automotive systems on a just-in-time and sequenced parts delivery basis, and provides a wide range of services for the design, development, program management and testing of integrated automotive systems for its European and North American customers. SteyrSymatec currently assembles the Mercedes Benz G-class and E-class four-wheel-drive vehicles, as well as the M-class four-wheel-drive sport utility

vehicle and the Jeep Grand Cherokee for DaimlerChrysler in Europe at its large vehicle assembly plant in Graz, Austria.

Tier One and Two automotive manufacturing divisions supply a variety of products. These include body products supplied by the Company's metallic body and chassis systems divisions, including divisions producing hydroformed components and assemblies and other exterior products supplied by the Company's wholly owned exterior systems divisions in Europe, interior products supplied by the Company's seating and interior systems divisions, four-wheel-drive powertrain products supplied by the Company's Steyr Powertrain division, and other automotive products supplied by the Company's closure and electronic systems divisions and exterior and interior mirror systems divisions.

Magna designs, engineers and manufactures a broad range of formed and welded metal automotive parts, components, assemblies, modules and systems primarily for sale to North American and European OEMs through Cosma. Cosma also sells, principally to OEMs, stamping tools and dies and assembly equipment, much of which it designs, manufactures and subsequently uses to manufacture products for such OEMs. Cosma's products include chassis stamping modules, hydroforming modules and systems, stamped exterior body parts, general stampings, engine and brake related stampings and body sheet metal modules and systems. In addition, Cosma paints, coats and finishes parts and assemblies manufactured by itself and others.

Magna's exterior systems operations include Magna Exterior Systems (MES), which supplies plastic and metallic exterior components and systems, including fascias (bumpers), grilles, body side mouldings, body side panels, plastic and metal trim products, drip mouldings, headlamp covers, radiator grilles, windshield mouldings, door frames and other exterior components for OEM customers. The MES Group, one of Europe's high-volume exterior systems manufacturers, introduced the use of gas injection moulding technology for bodyside trimming and has further enhanced the technology for thin-wall bumper fascias, which are featured on the Mercedes C-Class line of vehicles.

Magna's seating systems operations are conducted through Magna Seating Systems (MSS), a full-service supplier of seating systems and components. MSS is capable of managing the design, development, testing and final assembly of complete seating systems, as well as major seat components for its OEM customers.

Magna's interior systems operations are conducted through Magna Interior Systems (MIS), which designs, engineers, manufactures and sequences complete vehicle interiors and a variety of interior trim systems and components, including instrument panels, cockpit modules, consoles, package trays, overhead systems and sidewall systems.

Magna's powertrain operations include Steyr Powertrain, which produces a variety of axle, powertrain and chassis components and systems, predominantly for four-wheel-drive passenger cars, off-road and light commercial vehicles. Products include transfer cases, differentials and couplings, axle and chassis components and other components.

The Company's closure and electronic systems operations are conducted through Atoma International Corp., which designs, engineers and manufactures closure systems (including door hardware and window regulators) and electronic/electromechanical systems for the automotive industry. The Company's mirror systems operations are conducted through MMS. MMS designs, engineers and manufactures a variety of mirror systems, including exterior mirrors, integrated turn signal mirrors, mirrors with memory function, interior mirrors (including those with infra-red theft protection), interior lights, grab handles and other plastic components and assemblies.

Tier One and Two automotive manufacturing divisions supply a variety of products including exterior body products supplied by Decoma Exterior Systems (which includes Decoma International Inc., Decoma Exterior Trim and Bestop) and powertrain products supplied by Tesma International Inc., a supplier of engine, transmission and fuelling systems and components. Tesma is a global supplier of highly engineered engine, transmission and fuelling systems and components for the automotive industry, including North American and European OEMs, as well as other OEMs in the Asian Pacific and South American markets.

Decoma Exterior Systems is an independent North American supplier of automotive bumper components, assemblies and modules, and a supplier of plastic body panels and exterior appearance systems for cars and light trucks.

Decoma International Inc. is engaged in the manufacture and sale of plastic fascia systems and body panels.

Decoma Exterior Trim Inc. is a North American Tier One supplier of exterior ornamentation and sealing and

greenhouse systems products with seven manufacturing divisions. Bestop Inc. is a North American Tier One supplier of fabric tops, related framing systems and accessories for OEM and aftermarket applications.

- Magneti Marelli. The Italian auto parts maker has disposed of its lubricants, mechanical components, and thermal systems divisions. Thyssen-Krupp Automotive has agreed to buy Magneti Marelli's chassis systems unit. The company has formed a JV with GM for its powertrain systems and electronics systems divisions. Fiat decided to divest some of Magneti Marelli divisions in order to reduce debt and lessen its dependence on the automotive sector. The only two units to survive the Magneti Marelli sell-off will be the Midas Europe chain of service centres, and the company's 50% stake in Viaset, an onboard information and communications joint venture with Telecom Italia; these units will be taken over by Fiat.
- Pilkington PLC fits glass to almost 25% of the world's new vehicle production.
- Plastic Omnium. French Company, maker of fuel systems, auto interior and exterior panels, exterior trim, and bumpers. Its automotive parts account for the majority of sales, with major customers including GM and Nissan. There is a South African subsidiary in Brits making selected injection moulded components. The company also makes high-performance resins used in a variety of industrial applications to prevent corrosion, reduce wear, and provide sealing. Plastics Omnium also produces plastic medical equipment and playground equipment, and is engaged in waste collection and plastic packaging recycling. Its joint venture with Solvay, called Inergy Automotive Systems, produces auto fuel systems and has a subsidiary in Brits, South Africa. About 70% of sales are outside of France. Burrelle SA controls over 50% of the company
- Robert Bosch. Robert Bosch manufactures components for the world's automakers and the automotive aftermarket. OEM products include braking systems, ignition systems, fuel injectors, electrical motors and actuators, and engine management systems. Aftermarket products include spark plugs, starters, alternators, filters, and Blaupunkt car audio products. The company also makes packaging machinery, power tools, and home appliances.
Bosch was voted the most innovative supplier in Germany in 2000.
The South African subsidiary does not make electronic modules or lights.
- Saint-Gobain. One of Europe's oldest and largest enterprises, Saint-Gobain has operations in three sectors: housing products, glass, and high-performance materials. Housing product operations (45% of sales) include building materials distribution and manufacturing and pipe; glass operations (38% of sales) include containers, flat glass, and insulation and reinforcements; the high-performance materials unit includes ceramics, plastics, and abrasives businesses. Saint-Gobain is a world leader in many of its business segments. In the 1600s it provided glass for Versailles; today it insulates one in every two European homes and makes 30 billion glass containers a year.
- Sanden. A leading Japanese manufacturer of air-conditioning compressors, Sanden supplies extensively to European OEMs from local plants, and also has manufacturing facilities in the USA, Mexico and Australia, as well as nine plants in Asian countries outside Japan.
- Siemens Automotive. The electronics and industrial group has operations worldwide in the automation and control, information and communications, lighting, medical, power, and transportation sectors. It is also active in the semiconductor sector through a majority stake in chipmaker Infineon Technologies. Siemens is Europe's largest electronics and electrical engineering firm and the region's #2 mobile phone handset maker (after Nokia). Automotive products include electrical distribution systems, engine control modules, locking systems and fuel injections.
- SIV. Italian glassmaker now controlled by Pilkington
- Sekurit is part of the Saint-Gobain Sekurit international group
- Sommer Allibert (SAI). SAI Automotive AG, the former SOMMER ALLIBERT, controls a group of companies primarily engaged in the manufacturing of automobile parts and accessories. The products, especially for

interior and exterior trimming, are made out of plastic, textile and wood fibre. The company's customers are some of the biggest car manufacturers, amongst them VW, Opel, Volvo and Mercedes-Benz. SAI Automotive is also involved in the home furnishing sector. Under the branch name "ALLIBERT" it produces textile carpets and linoleum, garden furniture, sanitary and technical products. The company has subsidiaries in Germany, Luxembourg, Spain, Great Britain, Portugal and the USA. Dashboard, consoles, carpets, sound insulation and bumpers are the major automotive components made. SAI now owns Autoplastic in South Africa, makes full consoles and instrument panels for BMW.

- Takata-Petri AG. World Wide headquarters in Tokyo, after Takata acquired Petri AG. Takata-Petri AG has manufacturing plants in many countries, including the Far East, USA, South America, Europe including Eastern Europe and the UK. The existing South African subsidiary operation is located in Atlantis and makes only steering wheels. The Takata-Petri group product range includes Seat Belts, Airbags, Steering Wheels, Plastic Components, Clocksprings (used on Steering Columns to transmit electronic signals to the Steering Wheel) and Door Panel mouldings.
- Teksid. Owned jointly by Fiat and Renault is one of the largest second tier suppliers of a diverse range of automotive castings in cast iron, aluminium and magnesium utilising the most recent state-of-the-art casting technology. SA's low energy cost and availability of scrap which is presently being exported in large tonnages, makes this a viable option from Teksid's global point of view. Teksid supplies not only to Fiat and Renault but other OEMs, and has GM as it's largest customer.
- TRW. Based in Cleveland, Ohio, this large company serves the auto market with airbags, antilock brake and traction-control systems, seat belt systems, and steering and suspension systems. TRW's space and defence products include spacecraft and satellite technology, defence communications equipment, and high-energy lasers. TRW also provides computer systems to government and private-sector clients through its information technology unit. About 60% of sales come from its automotive parts business. To pay down debt incurred from TRW's purchase of UK-based auto parts maker LucasVarity, the company plans to sell off several non-core automotive operations.
- Valeo. This French company is one of Europe's largest car parts suppliers, making components for most major car and truck manufacturers. The electronics and electrical systems unit (about 55% of sales) makes wiper systems, motors and actuators, security systems, electrical components, electronics, and lighting products. The thermal systems unit offers climate-control and engine-cooling components. The transmissions segment makes clutch systems, torque converters, and friction products. Valeo's distribution unit conducts aftermarket activities. Générale d'Industrie et de Participations (CGIP), the company's largest shareholder, owns about 20% of Valeo.
- Visteon. Visteon is the futuristic-sounding name Ford Motor gave its automotive components unit when it was spun off in 2000. Visteon is the world's #2 auto parts maker -- behind GM spin-off Delphi Automotive -- and has operations worldwide. North America accounts for more than 70% of its sales. The company's automotive products include climate control systems, instrument panels, suspension systems, plastic components, automotive glass, and powertrain control systems. Sales to former parent Ford account for 84% of sales. The Company operates in three business segments: COMFORT, COMMUNICATION AND SAFETY: supplies automotive climate control, interior/exterior and telematics/multimedia systems, modules and components. DYNAMICS AND ENERGY CONVERSION: supplies automotive energy transformation and chassis systems, modules and components. GLASS: is divided into two product groups: vehicle glazing product group, which produces glass products for Ford and aftermarket customers, and the commercial glass product group, which produces float glass for commercial architecture. The South African operation presently only makes some engine control components.

- Yazaki. Yazaki Corporation is a global leader in the development and manufacturing of vehicle power and data solutions, and is continually researching and developing advanced electronic technologies for vehicles. Yazaki produces electrical distribution systems, fibre optics, advanced networking, instrumentation, junction blocks, connector systems, switches, electronics and advanced technology. Worldwide, the company employs over 100,000 people in 31 countries.

H. THE EASTERN CAPE AUTO SECTOR CLUSTER PROCESS

In 1999, the DTI initiated a cluster process for the Auto Sector in the Eastern Cape which was referred to as the Fish River Auto Cluster. The intention was to pilot the cluster, learn from the experience and thereafter introduce the cluster concept in Gauteng and Kwa-Zulu Natal. A process of engagement between the key stakeholders representing the OEMs, the component suppliers, NUMSA and Government resulted in the parties reaching agreement on:

- a shared vision for the Fish River Auto Industry
- the key focus areas which would build a foundation for the sectors to become internationally competitive and stimulate the creation of sustainable employment
- cluster structures which would ensure effective leadership and management of the process

The Fish River Auto Cluster Vision

The Fish River Auto Cluster stakeholders had gone through a particularly turbulent period during the late '80s and early '90s and there were increasing questions being asked about the future of the Auto Industry as the advent of the removal of protective tariffs become more of a reality. The industrial relations instability within the industry and particularly in the Eastern Cape, had become a serious concern which was also compounded by a move from enterprise level bargaining to centralised bargaining for the Auto Sector. The vision for the Fish River Auto Cluster was forged in a difficult environment. The vision which was agreed to after a lengthy process of consultation and negotiation was:

To establish a viable, local and internationally competitive industry, capable of achieving both continuous growth and sustainable job creation.

The leadership of the strategic partners made unequivocal commitments to support the achievement of the cluster vision.

Minister Alec Irwin – National Cabinet Minister : Department of Trade and Industry

The policy framework governing the development of the motor industry in South Africa has enabled the regional leadership within the Eastern Cape (Fish River) in Government, business and unions to form a strategic partnership which is committed to realising the full potential of the local motor industry. The competitive platform which is being developed, has resulted in focussed projects in respect of strategic investments, human resource development, logistics and supplier development, which will ensure that a sound basis is established for investments and stimulus for job creation.

MEC Enoch Godongwana : Member of the Eastern Cape Government for Economic Affairs, Environment and Tourism

The primary responsibility of the Eastern Cape Provincial Government is to support the motor industry in becoming globally competitive, by ensuring the provision of internationally competitive services and support at Provincial and Local Government levels.

Willie van Wyk – Cluster Chairperson – Managing Director Delta Corporation (General Motors)

The external factors demanding structural change within the South African motor industry are real and potentially threatening. Role players in the industry can make one of two choices, either go it alone or work together to make the auto industry in South Africa the springboard for not only the African renaissance but also for manufacturing and assembly for export. The Fish River Motor Cluster has opted for the latter alternative.

NUMSA

NUMSA was unable to define its level of commitment primarily due inability to assess the impact of global competitiveness on its members. The employees were firmly of the view that employment levels would go down within the industry in the light of the new manufacturing requirements and technology required to become globally competitive. The discussions centred around the potential for the industry to stimulate employment in other sectors if it became globally competitive and the necessary infrastructure was put in place. At a conceptual level, NUMSA fully supported the need to become globally competitive but had severe reservations about the prospect of reducing employment in the sector. The reality is that the strategic partners were about to charter new territory where the real impact of entering globally competitive markets were not known.

STRATEGIC FOCUS AREAS IN THE FISH RIVER AUTO CLUSTER

The parties following a process of detailed analysis and discussion, decided to establish four projects which they felt would provide the necessary building blocks for the industry to become internationally competitive.

1. Strategic Investments

The scope of this project covered:

- An analysis of the national policy framework (MIDP) and in particular the competitiveness of the incentives
- The strategic investments required to build a strong component supply base

2. Logistics and Infrastructure

The scope of this project covered:

- Identification of areas of opportunity for cooperation between the OEMs and suppliers to reduce costs, i.e. shipping, road transportation, air freight, etc.
- Identification of infrastructure requirements, i.e. ports, roads, rail, etc.

3. Human Resource Development

The scope of this project covered:

- Identification of skills required
- Identification of service providers and in particular the capacity and competence of the local Technikons and tertiary institutions

4. **Supplier Development**

The scope of this project covered:

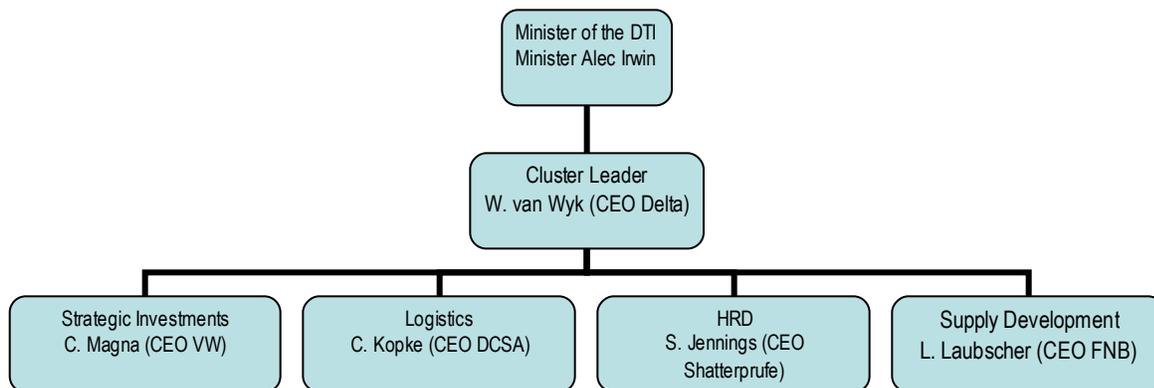
- Identification of the competence required by local suppliers to become internationally competitive
- The process to facilitate strategic partnerships between local and international suppliers

I. THE EASTERN CAPE FISH RIVER CLUSTER STRUCTURES

The key principles identified by the cluster leadership in designing what was considered the ideal structures were:

- The structures should promote a high level of cooperation and a spirit of partnership
- An effective process whereby Government could respond efficiently in facilitating sustainable solutions to issues impacting on the auto sector’s ability to become internationally competitive
- Clear accountability for projects
- Effective reporting and monitoring of progress

The structures and the level of seniority of the leadership is reflected below:



The cluster steering committee met on a quarterly basis to review progress of the projects and give strategic direction. NUMSA participated at the level of the steering committee and to a limited extent, in the projects. The limited participation did not relate to a lack of commitment but rather to serious constraints in respect of capacity and also an acknowledged lack of skills to participate effectively in the process. **All the parties seriously underestimated the time it would take to institutionalise effective cluster structures and processes and the resourcing required to ensure its sustainability.** The Fish River Cluster process which was funded by the Sector Partnership Fund was only for the duration of 1999. It became increasingly clear that the cluster process would need to be institutionalised at a Provincial Government level. The cluster partners were working under enormous operational pressures and needed solutions to problems to be designed in consultation with the key stakeholders and then put forward to the structures for endorsement or refinement. The parties were simply too busy in many cases to design the solutions themselves and had high expectations of the level of support they would receive from Government. A summary of the key challenges in 1999 and brief commentary of progress is set out below:

FISH RIVER AUTO SECTOR CHALLENGES - 1999	
KEY CHALLENGES	COMMENTS
<p><u>Strategic Partnerships</u></p> <ul style="list-style-type: none"> • Adversarial relationships between NUMSA / employers • Unstructured relationship between industry and Government particularly at a Provincial / Local level • No shared vision • No common understanding or support for a National / Provincial Auto Sector strategy • Fragmented initiatives • No integrated knowledge resource 	<p>The parties gained a better understanding of the threats imposed by globalisation and the phased removal of protection. The development of a shared vision was a good start but a sustainable Auto Sector plan for the Province was not developed or institutionalised as the cluster process only lasted for one year (1999). The most significant weakness in the process was that the role of Provincial Government as a key catalyst for facilitating the resolution of challenges facing the Fish River Cluster Sector was not defined and institutionalised.</p>
<p><u>Strategic Investments</u></p> <ul style="list-style-type: none"> • Uncertainty about the National Auto Sector Policy and regulatory framework • Uncompetitive incentives • No supply strategy for the sector • High levels of competition between OEMs with limited cooperation • Difficulty in attracting key suppliers • Low volumes 	<p>Strategic investments in this instance related to the key suppliers required to ensure a platform for international competitiveness. The OEMs had historically worked primarily with their own dedicated suppliers with no significant cooperation between them. There was limited progress in this area with the formation of a structure consisting of the Purchasing Managers from all the OEMs to identify strategic investments required to support OEM export and production of world class vehicles. In addition, the position of the OEMs and suppliers in relation to incentives to attract and retain investments was developed and submitted to the DTI.</p>
<p><u>Logistics</u></p> <ul style="list-style-type: none"> • Poor cooperation between OEMs and suppliers • No logistic strategy at a National, Provincial or Local level • Cost savings through cooperation between the stakeholders to reduce the cost of logistics in the short term was not being realised • No structured approach between the parties in dealing with the logistics challenges • The role of Provincial Government in facilitating solutions was not clear • National Government painted a picture of a world class logistics concept being developed and implemented, but there was no accountability for the implementation plan 	<p>This was possibly the most successful project in that the parties realised the benefits of cooperation in order to gain short term cost savings through negotiating common shipping, transport arrangements etc. The parties relied on National Government to give effect to the high level logistics strategy which had been outlined. Even during of 1999 there was increasing frustration about the manner in which the Government was managing this aspect. The role of Provincial Government was not clear and a Provincial strategy was not developed. An example of the tensions created at leadership level was when East London received approval from National Government for the establishment of the car terminal facility. The view of the employees in the Port Elizabeth area was that this was in direct conflict with the concept proposed by the DTI and that it was not consistent with the spirit of partnership to take decisions of that nature</p>

	<p>without proper consultation. The logistics project was translated into a structure known as the MIC (Motor Industry Cluster) which subsequently became part of the AIDC which has continued to play an important role in supporting the auto sector at a National level.</p>
<p><u>Human Resource Development</u></p> <ul style="list-style-type: none"> • Inadequate skills • Skills required by the Auto Sector had not been identified • No Provincial skills plan • Service providers, particularly within the Universities and Technikons, did not have the capacity or competence to meet the needs of the industry • Differences in approach towards developed a skills development strategy between the OEMs and a fragmented approach from the suppliers 	<p>This was a particularly difficult area as the National Skills Strategy was still in the process of being formalised and there appeared to be a vacuum at a Provincial / Local level. The employers had historically focused on their own needs and there had been very little cooperation. Attempts to analyse the skills needs and identify the necessary service providers were made without a great deal of success primarily due to limited resources and the magnitude of the exercise. At an operational level, the parties were still endeavouring to understand the implications of sector agreements which were increasingly focused on the skill / wage model which requires a high level of standardisation for basic skills across the industry.</p>
<p><u>Supplier Development</u></p> <ul style="list-style-type: none"> • Too many suppliers • Many suppliers without the capacity or competence to become internationally competitive due to lack of international partners, limited finance and technology, etc. • Uncertainty about the supplier rationalisation process • Difficult relationships between suppliers and OEMs particularly due to cost pressures • Poor cooperation between suppliers • Limited understanding of the impact of globalisation • No common supplier strategy within the industry 	<p>The threats to the suppliers was enormous. The OEMs had begun to work more closely together in looking at common supplier strategies led by the German companies VW, DCSA and BMW. Delta was later incorporated into this group. The primary focus was to improve quality and reduce the cost of supply over a relatively short period of time which put massive pressure on the suppliers. The OEMs began a significant process of rationalisation of suppliers and introduced new concepts of passing back greater responsibility to 1st tier suppliers in respect of R&D and managing relationships with 2nd and 3rd tier suppliers. This required that 1st tier suppliers develop a new level of capacity and competence and in many cases, without any long term security in the relationship with the respective OEMs.</p>

J. LESSONS LEARNT

The most important lesson learnt from the Fish River Motor Industry Cluster process was that it must be institutionalised through the necessary structures, processes and systems to ensure its sustainability. The slide on the next page shows 3 phases, namely:

- Design
- Implementation
- Institutionalise

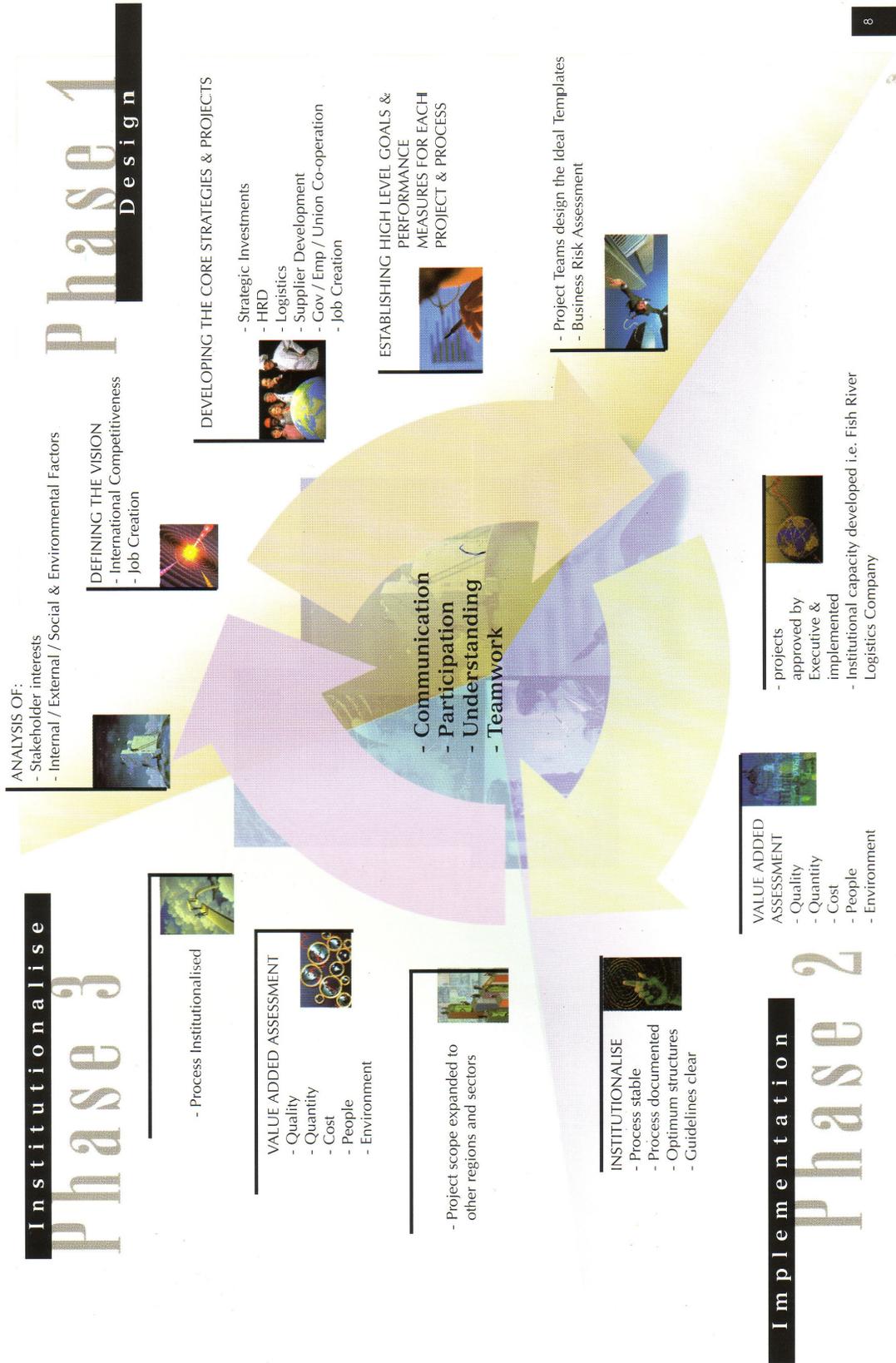
The process reflected was far too ambitious to be achieved in one year. The progress during 1999 was really only in the phase referred to as the Design Phase which covered:

- An analysis of the stakeholder interests
- Defining the vision
- Developing the core strategies and projects
- Establishing high level goals and performance measures for each project and process
- Designing the ideal templates and conducting business risk assessments

By the end of 1999, even Phase 1 was incomplete as the magnitude of the task has been completely underestimated. It was very evident that without a central catalyst within Government accountable for facilitating the development of a Eastern Cape Auto Strategy, it would not be possible to institutionalise a process. It was also clear that the Eastern Cape Provincial Government should have been the catalyst. Reference is made to an earlier quote: *“Primary responsibility of the Eastern Cape Provincial Government is to support the motor industry in becoming globally competitive by ensuring the provision of internationally competitive services and support at Provincial and Local Government levels.”* In hindsight, the role of Provincial Government could broadly be described as:

- To ensure strategic alignment at a National, Provincial and Local Government level in order to create an enabling environment for the Auto Industry in the Eastern Cape
- To facilitate effective participation on National policy issues
- To facilitate effective resolution of cross-cutting issues impacting on the auto sector which will prevent the sector become internationally competitive
- To develop a Best Practice knowledge resource for all partners to draw from, thus enabling them to develop and implement internationally competitive strategies

THE FISH RIVER MOTOR INDUSTRY CLUSTER PROCESS



K. THE EASTERN CAPE MOTOR INDUSTRY 2006

The Eastern Cape motor industry has made substantial progress since 1999 in responding to the challenges of globalisation. It has in many senses taken limited advantage of the strengths which have been identified by the auto sector such as:

- Emerging market cost advantages, e.g. labour and property costs
- Flexible production ability as a result of a low volume production which is usually lower than the long production runs of international competitors
- Low tooling costs
- Raw material availability with a greater emphasis on greater beneficiation
- Competitive electricity / land / service costs
- Southern hemisphere distribution to South America in the west and Australasia in the east and the African market
- First world production with a number of first world production facilities which are demonstrating the ability to produce world class vehicles and components
- Some elements of first world infrastructure, e.g. financial services and in some of the logistics areas relating to road, rail, sea and air systems
- Supply side measures which are constantly being challenged by the employers which Government is endeavouring to respond to within the context of the World Trade Organisations regulations

The Eastern Cape Government has decided to develop an Industrial Strategy for the Eastern Cape which will underpin and contribute to the achievement of the Provincial Growth and Development targets. The Auto Sector is considered to be a key sector with its proven capacity to attract new investments and create new jobs. A particularly important aspect is the extent to which the Auto Industry can become a catalyst for the stimulation of investment and the creation of jobs in other sectors.

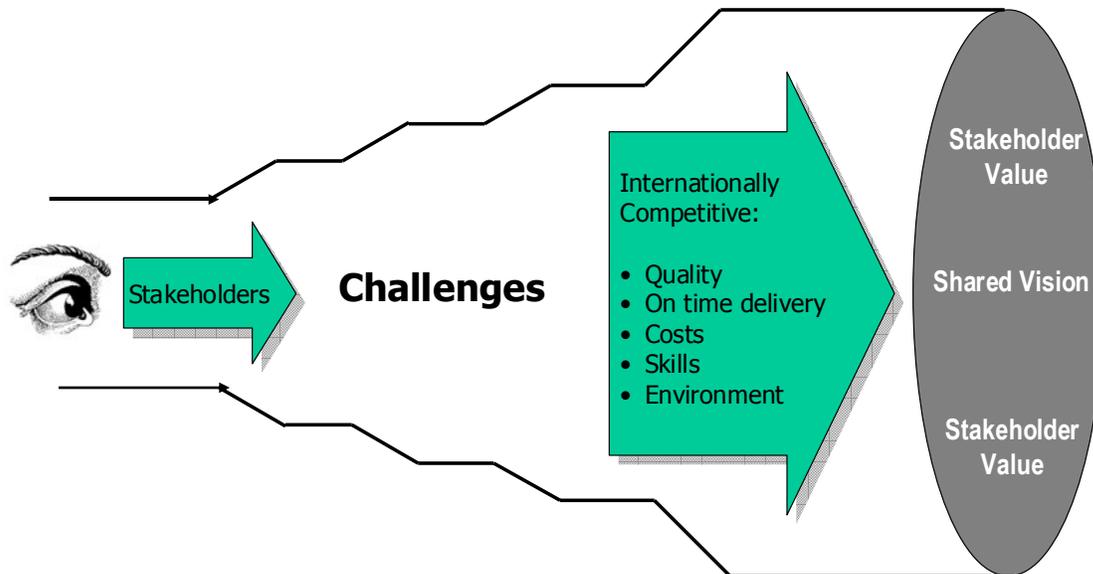
A series of interviews with the key roleplayers in the Auto Sector within the Eastern Cape was undertaken in March 2006 as the first phase in developing a strategy for the Eastern Cape Motor Industry which will be institutionalised within the Eastern Cape Industrial Strategy. The purpose of the interviews was to:

- Identify the key challenges facing the industry in the Eastern Cape
- Identify the role of Provincial Government in assisting to facilitate solutions to these constraints

The interviews took place with senior representatives of DCSA, VW, General Motors, East London IDZ, Coega and the Uitenhage Logistics / Supply Park. These interviews were supplemented with information received from various tiers of Government and employer organisations such as NAAMSA, NACAM, as well as Government funded agencies dealing with cluster processes such as the AIDC and an organisation known as the Benchmarking and Manufacturing Analysts. The latter two organisations, although primarily funded by Government, both had strategies in place to become self-funding. The challenges which were identified and elaborated more upon below are still fundamental and in the view of the Auto Industry companies in the Eastern Cape of the magnitude that if they remain unresolved

they could seriously impact on the future growth and viability of the industry. It is important to note that many of the challenges identified in 1999 during the Auto Cluster process still remain and in many cases, have become more critical. The challenge for the Auto Sector in the Eastern Cape is whether the strategic partners can design solutions which will overcome the challenges.

Development of an Eastern Cape Auto Sector Strategy



Lessons Learnt

- The strategy to initiate a cluster process for the Fish River Auto Industry Cluster process in 1999 was correct.
- The cluster process could have achieved a great deal more if:
 - Provincial Government had played a stronger lead role in facilitating effective implementation of the strategic projects
 - The necessary funds had been made available after 1999
- Gauteng and KwaZulu Natal recognised the value of initiating the cluster concept. In Gauteng, the AIDC was established through the CSIR which is now funded by the Gauteng Government Blue IQ Project. It has established an office in PE which is funded by the ECDC. The AIDC has developed a high level of competence and has been involved in a number of important initiatives such as the establishment of the Rosslyn Supplier Park and, more recently, the Uitenhage Supplier Park.
- KwaZulu Natal have established a cluster process which is facilitated by the Benchmark Club which, like the AIDC, is offering its service to the national industry.

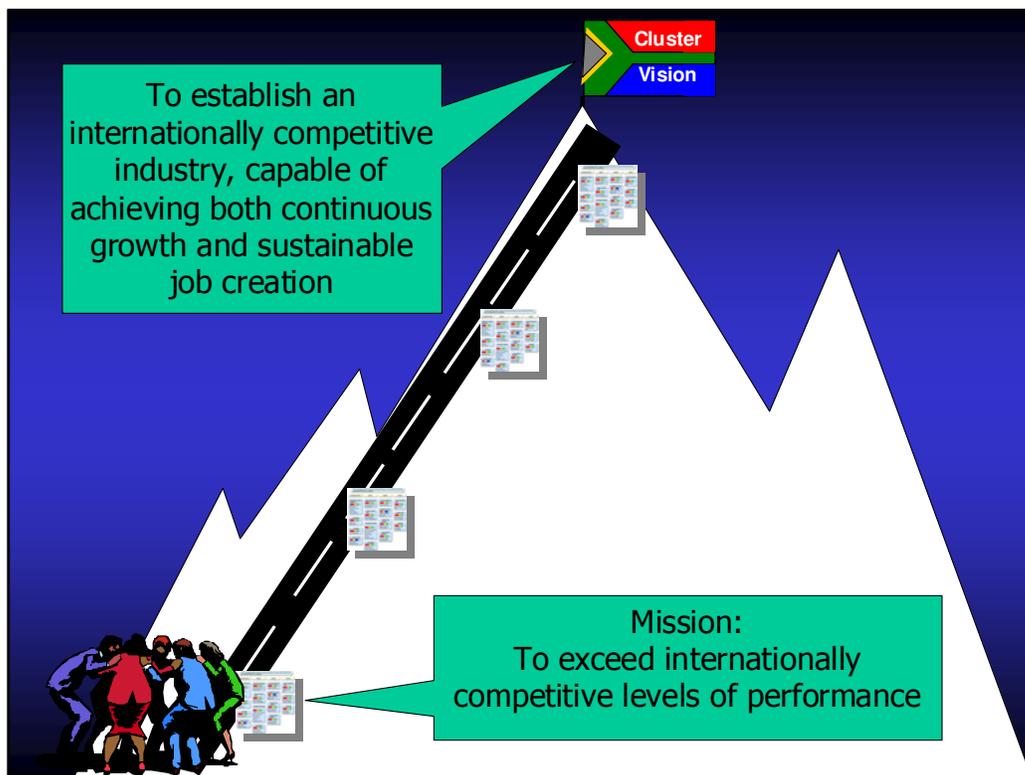
L. CHALLENGES FACING THE EASTERN CAPE MOTOR INDUSTRY

The representatives from VW, DCSA and General Motors confirmed that their organisations had met and in some cases, exceeded the performance targets set by their parent companies. Their level of performance in this respect has been quite remarkable as evidenced by the earlier statistics relating to exports. The constraints which they identified can broadly be described as:

- The challenges of globalisation. These issues which are dealt with earlier in this document are challenges which the local companies have very little control over. The challenges relate to distance from the primary markets and small volumes in the local market
- Challenges which can be influenced by the parties in South Africa which are fundamental to the future of the industry

A quote from a senior executive of one of the auto companies highlights a perception that Government does not understand how fragile the future of the Auto Industry is.

“Government seems to think we are going to be around under any circumstances. We will not get future models unless we exceed the levels of performance of our other plants around the world. Unless the key challenges are overcome, we have no future in South Africa as we will not be able to achieve internationally competitive quality, on time delivery and cost targets. The environment is becoming increasingly competitive on the international stage and all the stakeholders need to understand the level of commitment required to ensure our future in South Africa. The odds are against us and we must have a coherent strategy to climb the highest mountain in the world together.”



The challenges identified below focus on those which can be influenced or resolved by the parties in the Fish River Motor Cluster process with the understanding and support of the National roleplayers.

1. Optimising Stakeholder Relationships

The challenges in the relationships and the potential for greater synergy are briefly described below. It is important to note that all the stakeholders interviewed were absolutely unanimous that unless there is a high level of synergy and cooperation in resolving these challenges, it could severely impact on the future growth and viability of the Motor Industry in the Eastern Cape. Key relationships and challenges are briefly analysed at the different levels:

- Between OEMs (VW, General Motors and DCSA)
- Between OEMs and suppliers
- Between employers and Unions
- Between DCSA and the East London IDZ
- Between VW / General Motors and Coega
- Between VW and the Uitenhage Supply / Logistics Park
- Between the Eastern Cape Motor Industry and Government

Relationships between OEMs

The relationships between the OEMs in the Eastern Cape have improved dramatically in recent years as the parties recognised that there are many beneficial areas for cooperation. The OEMs face similar challenges at a global and domestic level and are increasingly able to identify issues which are in the National / Provincial interests which require a high level of cooperation, and those issues which are internal issues which will be dealt with in a way that will optimise their competitiveness. The primary concerns raised by the OEMs which will be dealt with in more detail below are:

- Lack of any formalised Auto Sector strategy for the Eastern Cape. There is an understanding that there is a National Strategy which has been formalised into a Policy. The primary concern however, is that the Policy has not been developed into a National plan which has been translated into a Provincial plan.
- There are pockets of excellence which have been developed at a Local Government level and within the IDZs which are not coordinated at all at a Provincial level which results in unnecessary competition in certain respects between the Buffalo City Municipality and the Nelson Mandela Metropole.
- Fundamental issues raised by the OEMs at different tiers of Government, with different Departments and with parastatals are not resolved.

Relationships between OEMs and Suppliers

This relationships must be considered in the light of a significant restructuring in the relationship which has led to a major rationalisation of suppliers. The OEMs have increasingly placed greater responsibility on the 1st tier suppliers in respect of R&D as well as the management of 2nd and 3rd tier suppliers. The cost drive by the international parent companies has been felt most strongly by the suppliers, many of whom are struggling to meet continuous demand from the OEMs for higher levels of performance, particularly in the area of costs.

Relationships between Employers and Unions

The relationships between employers and NUMSA at a National, Sector and Enterprise level, have improved significantly from the late '80s into a major part of the '90s where there was a great deal of industrial instability. There are now relatively harmonious relationships with a far greater focus on performance. The German companies are generally of the view that the cooperation between their companies and NUMSA is far greater than the level of cooperation in Germany. The German companies based in the Eastern Cape however, face massive pressure from their parent companies to move the current export production back to the European plants because of the excess capacity there and threat to jobs. The IG Metal which is the biggest trade union in the world, is putting a great deal of pressure on the German Government and German companies based in South Africa to relocate the current export production from South Africa. In general, Management and NUMSA have shown great maturity in cooperating to create an environment which has allowed the local manufacturers to become more internationally competitive.

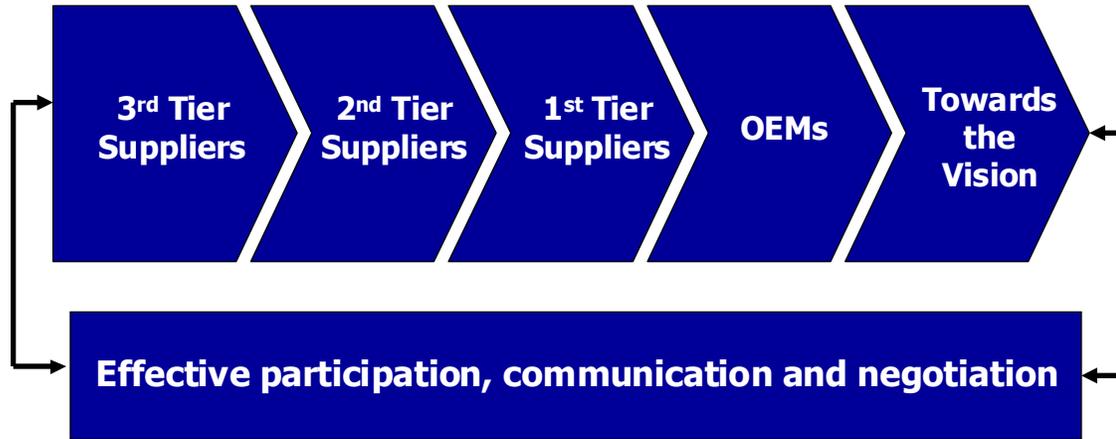
Relationship between DCSA and the East London IDZ

It has been difficult to institutionalise a strategic relationship between the EL IDZ and DCSA until fairly recently. It was only in the latter stages of 2005 that a final decision was taken by DCSA to invest in the new W204 in the East London manufacturing plant. Significant progress is however being made by the parties in building a relationship which is intended to ensure that key suppliers are located in the IDZ. The parties are in the process of working together to overcome key challenges facing the Auto Sector in East London which will be dealt with below.

Relationships between VW, General Motors, Coega and the Uitenhage Supply Park

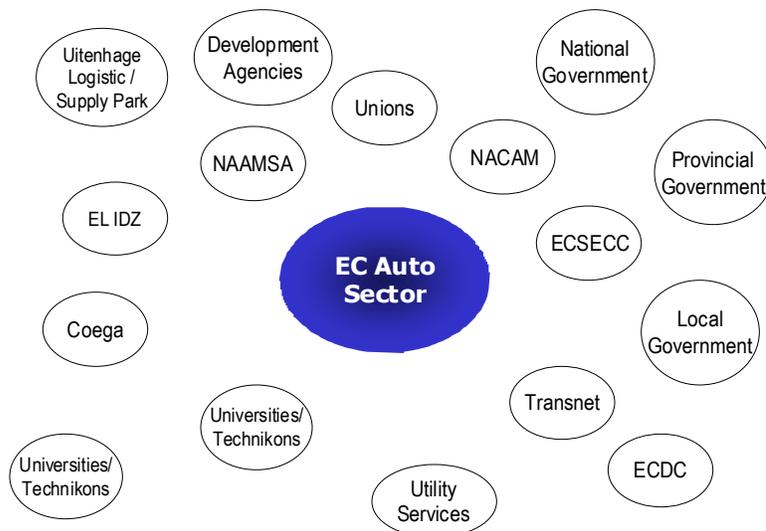
The relationship between VW and Coega has not been as close as that of General Motors and Coega. VW's perception is that it was not effectively consulted during the initial phases of developing the Coega strategy, and the benefits of closer cooperation need to be optimised. In respect of General Motors, there has been close cooperation but, once again, there seems to be considerable opportunity through close cooperation. A particular area for cooperation is the alignment of investments across the value chain with a particular focus on 1st, 2nd and 3rd tier suppliers. VW has been instrumental in facilitating the establishment of the Uitenhage Supply / Logistics Park which is situated within 5 km's of the VW manufacturing plant. VW is encouraging key 1st tier suppliers to move into the Supply Park. What is not clear is what strategy needs to be put in place to ensure that the necessary 1st, 2nd and 3rd tier suppliers are attracted to invest in the Eastern Cape.

Aligning the Supplier Strategy



Relationship between the Eastern Cape Motor Industry and Government

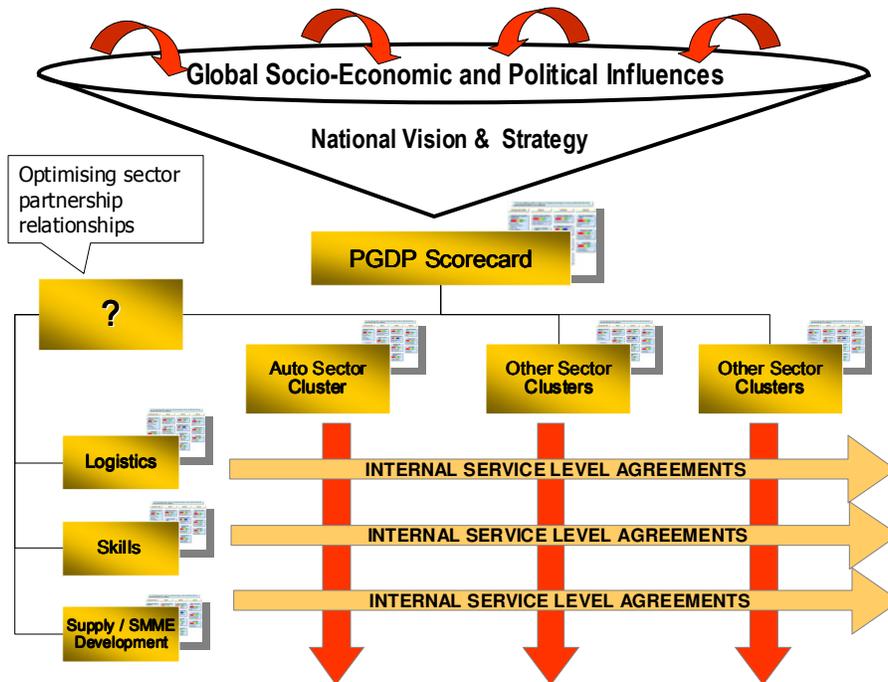
Concerns were raised about the fragmented approach Government was taking in dealing with issues raised by the industry and the many interfaces which have to be dealt with within Government and parastatals at a National, Provincial, District and Local level. The absence of an Eastern Cape Motor Industry Strategy and inability of the Provincial Government to facilitate solutions to a range of issues such as logistics, infrastructure, skills problems, etc. is a matter of serious concern. The Auto Sector companies are not sure who they should be dealing with in Government and, as a consequence, interface at a variety of different levels both within National, Local and with parastatals and other agencies in an attempt to resolve problems. The nett result is that issues remain unresolved and the limited Best Practice which is being developed at a Local Government level and within the IDZs is happening in isolation.



In 1999, the Eastern Cape Government committed itself to supporting the Motor Industry in becoming globally competitive, by ensuring the provision of internationally competitive services and support at Provincial and Local Government levels. In hindsight, it is clear that the level of support required and the nature of support was not understood by the parties at that stage. The perception of the employers is that they have focused on becoming internationally competitive but their energies are diluted due to the amount of time they are required to spend in endeavouring to resolve issues which they believe Government should be facilitating. It is the considered view of all the parties interviewed that a further Provincial Cluster initiative for the Province will fail unless:

- A well defined strategy is developed with the understanding and support of the key role players at a Provincial level.
- The strategy is understood and supported by Local, Provincial and National Government
- Provincial Government institutionalises structures, processes and systems which effectively facilitate the resolution of challenges facing the sector

Progress has been made, once again in a relatively unstructured manner, in Gauteng and KwaZulu Natal where cluster processes have been initiated. The Rosslyn Auto Supply Park was an outcome of the Gauteng based cluster process whilst KwaZulu Natal have also established an auto cluster process. **There is no precedent where the Provincial Government has taken the lead role in developing and institutionalising a comprehensive Auto Sector Strategy at a Provincial level with the understanding and support of Local and National Government.** It is critically important that this template is developed, particularly in the light of the Provincial initiative to develop an integrated industrial strategy for the Province. The full benefits of effectively implementing the Fish River Auto Cluster process in 1999 were not achieved. The key challenges which are reflected further in this document, if effectively resolved, could have a significant spin-off for the other sectors. The challenges referred to are broadly, optimising stakeholder relationships, logistics and infrastructure, skills and supplier development



2. Policy and Regulatory Framework

The review of the MIDP is creating a level of uncertainty within the industry. The general view is that the outcome of the review process will not prove to be more onerous than the current MIDP. It is acknowledged by the OEMs that the MIDP has achieved its objectives to date but that there needs to be certainty for the future. The suppliers are particularly concerned about the level of incentives and the ability of the supplier industry to compete and invest in new technology if the investments are not significantly enhanced. At this stage, the discussions are merely speculative and NAMSAs and NAACAM have both given their input into the MIDP review process. There was a view expressed that the Provincial Government should have involved itself in the process in order to motivate and support the positions put forward by the industry which is a key sector in the Eastern Cape economy. The need to protect and grow the Auto Sector in the Eastern Cape is considered to be more critical than in Gauteng and KwaZulu Natal which has a stronger sectoral platform.

3. Logistics and Infrastructure

Buffalo City

The issue of logistics and infrastructure is a major concern for the East London and Port Elizabeth based auto companies. DCSA, for a number of years, has been engaging the different Transnet companies in an endeavour to have its specific needs taken into account. In summary, these needs are:

- A deeper port which is able to accommodate larger vessels
- The infrastructure required to ensure efficiency in the port, i.e. gantry cranes, etc.
- The upgrading of the East London / Gauteng rail link

The issues referred to above were identified as serious challenges during the Auto cluster process in 1999. At that stage the DTI indicated that it was in the process of finalising a National logistics strategy which would result in world class infrastructure governing a number of logistic port hubs with all the inter-connecting infrastructural facilities covering roads, rail, air, etc. DCSA is seriously concerned about the lack of progress which has been made and is currently engaging with Transnet and other key stakeholders to develop a business case to be put forward to the relevant role players. The challenge for DCSA and the role players who are developing the proposal is who will facilitate the process thereafter in order that decisions can be taken and a solution implemented. It is clear from the discussions with DCSA and the East London IDZ that their requirements have to be met to ensure the future growth and viability of DCSA and the EL IDZ.

Nelson Mandela Metropole

The two main issues for the OEMs based in the Nelson Mandela Metropole are:

- A need to upgrade the current facilities in the Port Elizabeth port. There is consensus between VW and GM that the Port Elizabeth port will be used for the export of motor vehicles which will not be possible at Coega because of the nature of the industry and beneficiation processes which will take place and the concerns about contamination of the export vehicles. The Port Elizabeth port berthing facilities are not adequate as well as the current infrastructure. The port is operating at an efficiency level of 65% on average which means that it cannot accommodate the Auto Sector needs in peak periods. Coega

indicated that it was undertaking an environmental impact study (Zone 14) which will support its strategy to attract OEMs and 1st tier suppliers and facilitate the export of vehicles.

- The upgrading of the rail link between Port Elizabeth and Johannesburg. Like East London, this is a major area of concern. General Motors indicated that only 40% of their vehicles to Johannesburg were going by rail. All parties highlighted the inefficiencies in the current rail system

The case to upgrade the logistics infrastructure for both East London and the Nelson Mandela Metropole will need to take into account the needs of all the key sectors in the Eastern Cape. In many instances, the needs of the key sectors will be based on future projections and the finalisation of the Provincial Industrial strategy.

4. Skills

Technical, supervisory and operational skills remain a major challenge for the Eastern Cape Auto Industry. All the OEMs confirm that significant progress has been made within their companies, but that initiatives around skills development are happening in isolation of a Provincial Skills Plan for the Auto Sector. A number of very innovative developments have taken place in recent years such as:

- Significant investment by the Auto Industry players in upgrading the skills of employees including programs which have sent numerous employees to the parent companies
- Coega has undertaken a very ambitious project which has resulted in a detailed skills plan and delivery system to meet the needs of prospective investors in all sectors. The interesting aspect of the Coega Human Resource strategy is that they have gone to extraordinary lengths to gain the understanding and support of key role players. A labour zone agreement was recently signed between employer organisations and seven trade unions which will be interacting in the Coega Development Zone. It is a unique agreement which will need to be very carefully implemented and its effectiveness monitored on a regular basis to ensure that it meets the needs of the parties.
- The East London IDZ and DCSA are in formative stages of developing a skills strategy for the IDZ which will meet the needs of the Auto Sector suppliers in the IDZ.
- Volkswagen has been a major catalyst in the establishment of the Uitenhage Logistics / Supply Park. A program was initiated in 2005, funded by the Department of Labour, and resulted in the training of 1000 operators of whom 700 have been placed in permanent employment.
- The Nelson Mandela Metropole University, and particularly its Technikon, have been very proactive in identifying skills requirements in the industry and responding to such needs.

The parties interviewed were unaware that there is a Provincial Skills Plan. The Nelson Mandela Metropole is in the process of developing a skills plan which appears to be happening in isolation of the Provincial Skills Plan. It was the considered view of all parties that the limited capacity of the service providers in the Eastern Cape would need to be optimised through developing an integrated strategy to ensure cost effective service delivery. A high level of cooperation would be needed between the Universities and Technikons to create a framework where all parties could build on their strengths in meeting the needs of the industry.

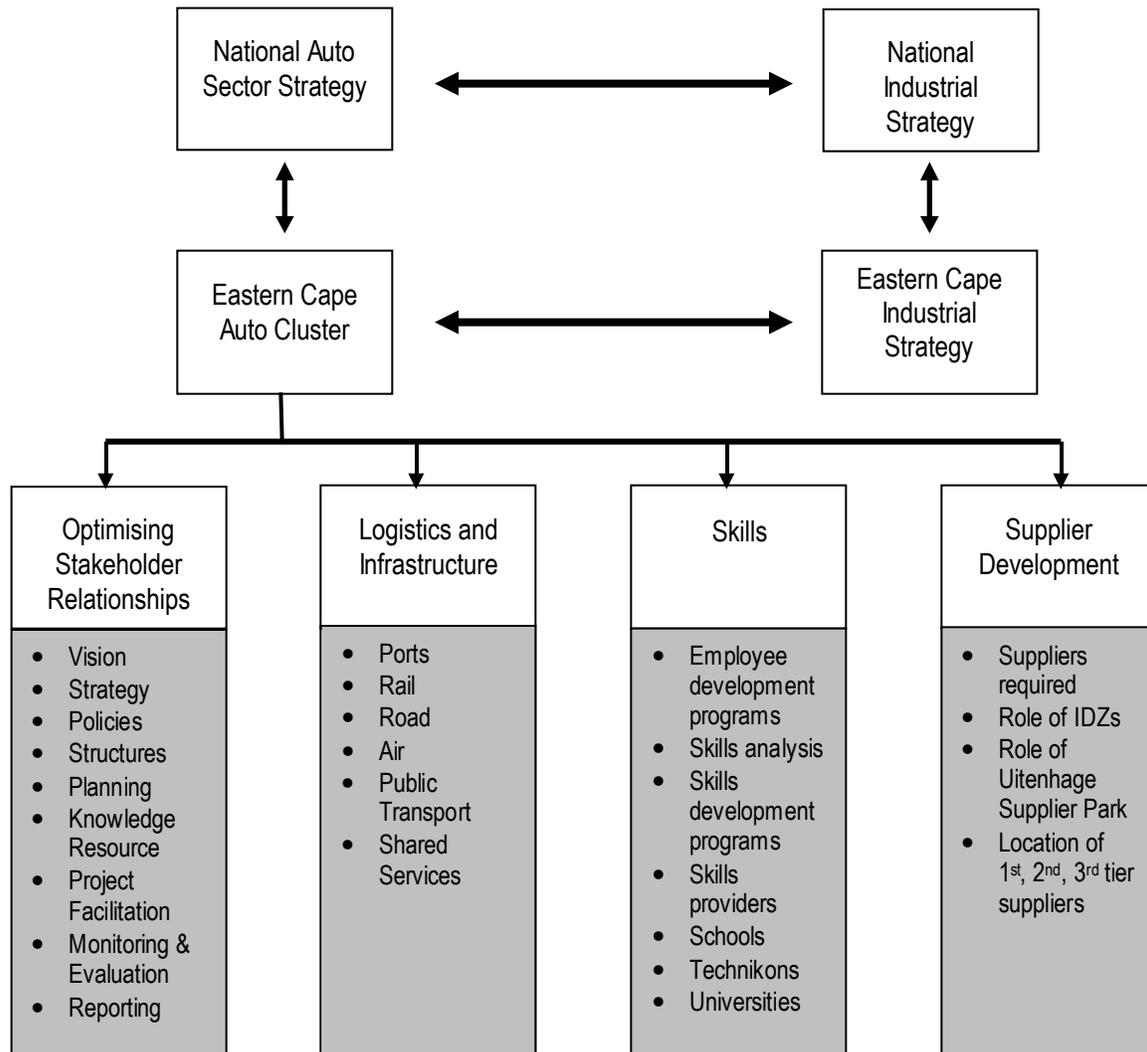
5. Supplier and SMME Development

The IDZs and supplier parks have been identified as the main vehicles for supplier development. At a concept level this strategy has been accepted by the parties. There is however, a considerable amount of work to be done in formalising the supplier development strategy so that there is not unnecessary competition between the IDZs and logistics / supplier parks in the Eastern Cape. This strategy will recognise the economic reality that 1st tier suppliers will be influenced by the volumes required by OEMs and the opportunities presented for the export of components. In this respect, Port Elizabeth / Uitenhage has a distinct advantage with a combined vehicle output of close to 200 000 units per year as opposed to DaimlerChrysler's 50 000 units per year. In respect of the development of 2nd and 3rd tier suppliers, it would seem logical that Coega in most instances would be the preferred location as the OEMs and 1st tier suppliers may not be able to co-exist with the types of industries which will be attracted to Coega.

M. RECOMMENDATIONS

The first recommendation is that Provincial Government should facilitate the establishment of a cluster process for the Eastern Cape Auto Industry which ensures that the key challenges are resolved on a sustainable basis. ECSECC should be made responsible to facilitate the process and provided with the necessary resources and budget. The strategy and project structures must be designed to ensure the optimum efficiency and flexibility in resolving the challenges facing the Auto Sector in a very dynamic environment. It must be recognised that the key challenges reflected in the project concept structure below will change based on the needs of the industry in future.

CLUSTER CONCEPT



KEY PRINCIPLES IN DESIGNING AND DEVELOPING THE STRATEGY, STRUCTURES AND PROJECTS

- There must be strategic alignment between National, Provincial and Local Government in support of the Eastern Cape Auto Industry
- The Provincial Government’s primary role is to play a strategic facilitation and coordinating role relating to all initiatives to support the industry
- The technical expertise for the projects identified in consultation with the industry must be drawn primarily from industry resources on a project by project basis
- Funding and resources for the projects should be sourced from the various departments within National, Provincial and Local Government and the industry based on sound business cases which demonstrate the benefits to all stakeholders
- The focus of the projects must be on the key strategic issues which will build or strengthen a sustainable platform for the growth of the industry
- Cross-cutting issues between the Auto Sector and other key sectors which can enhance growth of the industries must be leveraged
- The structures must be able to monitor and evaluate progress and, in particular, what contribution the sector is making towards the achievement of the PGDP targets (scorecard)

KEY PROJECTS

<p>Optimising Stakeholder Relationships</p>	<p>The scope of this project will need to cover the issues reflected in the adjacent diagram. The activities which will need to be incorporated into a detailed project implementation plan will require significant facilitation between the key roleplayers in order to ensure that their full buy-in is gained. If ECSECC is made responsible by Provincial Government to facilitate the establishment of the Auto Sector Cluster, it will need to develop the institutional capacity within ECSECC to ensure that this process is sustainable. It is important to recognise that the cluster process is a long term process which Government will need to lead with the understanding and support of the key roleplayers. The specific steps required in establishing this project are:</p> <ul style="list-style-type: none"> • To develop the project scope • To develop detailed project plans and budgets • To present the project plans and budgets to the Auto Cluster leadership (Sector Summit) • To refine the project scope, implementation plans and budgets • Implement the project • Monitor and evaluate
<ul style="list-style-type: none"> • Vision • Strategy • Policies • Structures • Planning • Knowledge Resource • Project Facilitation • Monitoring & Evaluation • Reporting 	

Logistics and Infrastructure
<ul style="list-style-type: none"> • Ports • Rail • Road • Air • Public Transport • Shared Services

The IDZs and the Uitenhage Logistics and Supplier Park all refer to the development of world class logistics and infrastructure. The reality is that the Auto Sector in the Nelson Mandela and Amatole districts are still facing the same challenges that were identified in the Fish River Cluster process of 1999 and soon thereafter. Work in the three organisations has reached an advanced stage from a design point of view. There is considerable risk that National Government departments will be once again confronted with proposals which are not integrated into a Provincial logistics and infrastructure strategy and either not take decisions or take decisions which create conflict between the regions. It is important that the cluster project leadership are able to develop an integrated strategy which prioritises the needs of the Auto Sector across the Eastern Cape and clearly identifies its role in expediting decisions in the appropriate structures. A sound business case to support the decisions required will need to be developed within the context of the broader Provincial Industrial Strategy as well as key socio-economic issues. The specific steps required in establishing this project are:

- To develop the project scope
- To develop detailed project plans and budgets
- To present the project plans and budgets to the Auto Cluster leadership (Sector Summit)
- To refine the project scope, implementation plans and budgets
- Implement the project
- Monitor and evaluate

Skills
<ul style="list-style-type: none"> • Employee development programs • Skills analysis • Skills development programs • Skills providers • Schools • Technikons • Universities

The Auto Sector in the Eastern Cape has used all the resources at its disposal to fast-track skills development within their respective organisations. The IDZs and Uitenhage Supplier Park have designed some very innovative templates to facilitate skills development within their organisations to support the potential investors in the Auto Sector. These initiatives are happening within the framework of the National Skills legislation. The challenge, however, is that there is no integrated skills strategy for the Province which will capitalise on the combined intellectual capacity and resources of the different organisations involved in skills development. There is no doubt that the different best practices can be integrated into a generic template for the Province which can be very beneficial to all the stakeholders. The IDZs and the Uitenhage Supplier Park would be key catalysts in designing, developing and implementing the skills strategy in consultation with key Auto Sector roleplayers. The specific steps required in establishing this project are:

- To develop the project scope
- To develop detailed project plans and budgets
- To present the project plans and budgets to the Auto Cluster leadership (Sector Summit)
- To refine the project scope, implementation plans and budgets
- Implement the project
- Monitor and evaluate

Supplier Development
<ul style="list-style-type: none"> • Suppliers required • Role of IDZs • Role of Uitenhage Supplier Park • Location of 1st, 2nd, 3rd tier suppliers

At a strategic level, there is absolute consensus between the OEMs in the Eastern Cape that it is critical to attract 1st, 2nd and 3rd tier suppliers into the IDZs and Uitenhage Supplier Park. The critical challenge is to identify which suppliers are needed and where they should be located. One option is to allow the current status quo to continue where the OEMs are implementing their own supplier investment and development strategies and the IDZs and Uitenhage Supplier Park are also competing against each other for investments from suppliers. An alternative option is for the parties to engage in order to develop a strategy which will endeavour to meet the needs of the respective organisations and the Provincial Government. The reality is that the OEMs and IDZs within the Province are competing against other IDZs within South Africa and globally and a fragmented approach in approaching potential investors could be problematic and result in potential conflict. Key questions must be considered by the parties and the necessary solutions developed even if this results in only the building blocks being put in place to facilitate an effective long term supplier strategy, e.g.:

- Where should new OEMs (i.e. from India or China which will concentrate on the lower end of the market) be encouraged to locate?
- Where will the necessary 1st tier suppliers be encouraged to locate?
- Where will 2nd and 3rd tier suppliers be encouraged to locate?

The specific steps required in establishing this project are:

- To develop the project scope
- To develop detailed project plans and budgets
- To present the project plans and budgets to the Auto Cluster leadership (Sector Summit)
- To refine the project scope, implementation plans and budgets
- Implement the project
- Monitor and evaluate

THE ROLE AND RESPONSIBILITY OF THE CLUSTER LEADERSHIP

The key representatives from Industry, Government and Labour will be required to lead and manage the cluster process in a way which ensures that the project goals, measures and targets are achieved within the time frames set out in the project plans. The level of seniority of the representatives must be consistent with the competence to take decisions or expedite decisions which carry the understanding and support of their respective constituencies. The preparatory work for any cluster review process by leadership on a structured basis will need to be exceptionally well done in order that the process is able to gain credibility from inception. It is evident that all the parties in the Auto Sector are reluctant to invest time and energy in any process which they do not perceive to be able to add measurable benefits to improving their performance in respect of internationally competitive quality and cost targets. Whilst the majority of the work will be done within the projects, there will be a considerable amount of work in coordinating and integrating the various outcomes to be considered by the cluster executive leadership when taking decisions or giving strategic direction to the process.

N. CONCLUSION

- The general consensus from the industry stakeholders was that a cluster process for the Auto Sector will fail unless it is institutionalised through Provincial Government playing a leading role. The current scenario where the industry roleplayers deal with multiple interfaces to try and overcome challenges is likely to get worse.
- The industry in the Eastern Cape has done remarkably well in responding to the global challenge and there are numerous examples of best practices developing in isolation, e.g.
 - Initiatives in the IDZs and Supplier Park
 - Initiatives within the local authorities
 - Initiatives with the Technikons and tertiary institutions
 - Skills initiatives within the OEMs, suppliers, IDZs and Supplier Park
- The National Government has taken a decision that the Auto Sector is an important catalyst for the stimulation of investment and sustainable job creation
- The Auto Sector in the Eastern Cape has clearly demonstrated that it is possible to become internationally competitive within the current environment. This is an important benchmark for other potential investors
- Whilst the Auto Sector will not create a massive number of new jobs it is, and should continue to be, recognised and supported as an important catalyst in stimulating job creation in other sectors within the Eastern Cape.