



Trade and Poverty Project
Southern Africa Labour and Development Research Unit
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Trade and Poverty in South Africa: Motor Industry Case Study

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By: Frank Flatters and Nnzeni Netshitomboni¹

1 Introduction

The motor industry was one of South Africa's most heavily protected industries prior to the trade liberalization program that was launched in the 1990s. The sector has attracted enormous government attention and a wide range of public support in adjusting to the new trading environment. The centrepiece of government support has been the Motor Industry Development Program (MIDP) that was launched in 1995. The program has been modified and/or extended several times, and is currently scheduled to continue until 2012. A review is now under way to examine future policy options for the industry.

The MIDP and other support measures for the motor industry were quite novel in that they were designed not simply to reduce protection for the industry, but also to encourage a major restructuring and reorientation of firms with the long term goal of orienting them to external markets and increasing their global competitiveness.

While there have been some interesting recent discussions of the overall costs and benefits of the MIDP to the South African economy,² little of the debate has focussed on its implications for poverty. The purpose of this paper is to draw attention to the poverty dimension of the trade and trade liberalization experience of this industry by examining issues related to

- employment in the both the motor industry and related downstream vehicle sales and service industries,
- the importance of motor vehicles in transportation services for the poor, and
- the role of motor vehicles as both a consumer product and an input into income earning activities for the poor.

We begin with an overview of motor industry trade and industrial policies and of recent industry performance.

2 The MIDP: Its Rationale and How it Works³

The MIDP was initiated in 1995 to help the motor industry adjust to South Africa's reintegration into the global economy. Prior to that time the industry was protected by tariffs in excess of 100 percent and burdensome local content requirements. Unsurprisingly it produced a very wide range of products at low scales of output and at high cost. It was a very inefficient import substitution sector that could not have competed either domestically or internationally in the face of immediate trade liberalization.

The MIDP was designed to help the industry adjust and increase its competitiveness in the new post-apartheid trade policy environment. The program comprised four principal elements:

- a gradual reduction in import duties on both vehicles and components,
- an export-import complementation scheme under which vehicle and components exporters can earn tradable "Import Rebate Credit Certificates" (IRCCs) to offset duties on imported vehicles and components,

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² See papers by Barnes et al, Bell, Black, Flatters and Kaplan in References at end of this paper.

³ This section draws heavily on Flatters 2005.



- access to the standard duty drawback program for exporters, under which all import duties paid on components and intermediate inputs used in exported vehicles and components can be rebated, and
- a duty free allowance on imported components of 27 percent of the value of vehicles produced for the domestic market.

The incentives in respect of components apply only to those sold directly to OEM manufacturers. This excludes from the program after-market components, a sector in which South Africa might have some regional and maybe even global comparative advantage.⁴

The idea of the program was to provide incentives to rationalize production into a smaller range of products and achieve economies of scale through exporting them. All other products would be imported. At the same time, the amount of protection and the size of the incentives were designed to be scaled down gradually through the simple mechanism of reductions in the import duties on vehicles and components.

The MIDP was expanded in 2002 to include a direct investment subsidy in the form of a “Productive Asset Allowance” (PAA) that provides import duty credits equal to 20 percent of the value of qualifying investments.⁵

The industry benefits as well from a wide variety of other initiatives by national, provincial and local governments. These range from restrictions on imports of used cars to provision of infrastructure, factory facilities and special financial arrangements.

The MIDP creates substantial incentives to invest and to produce for export and for the domestic market.⁶

Producers for the domestic market benefit from tariff protection against imports and from the duty free allowance (DFA), which offsets the cost-raising effect of import duties on components.⁷ Consumers pay for this through prices that are higher than they would be in the absence of the import duty on vehicles, and the National Treasury pays by foregoing customs duties on components.

Firms producing vehicles or components for export qualify for duty drawbacks on all imported components and also receive IRCCs in proportion to their exports. These allow them to import motor vehicles (and components) duty-free and sell them domestically at the duty-inclusive price. The value of the IRCCs depends on the price mark-up permitted by the tariff. Without this price mark-up the principal MIDP incentive would be of no value to vehicle and components exporters.

Table 1 shows the MIDP tariff rates on vehicles and components from the beginning of the program in 1995 to its currently scheduled end date in 2012. Although it shows gradually declining tariff rates over the life of the program, the rates are and will remain high relative to South Africa’s general tariff schedule, even at the end of the phase-down period. South Africa’s average tariff rate in 2004 was only 7.9 percent, less than one quarter the rate on motor vehicles at that time and still less than one third the rate that will apply to motor vehicles in 2012.

⁴ Some South African firms claim to be exporting after-market parts competitively without MIDP support. Bosal South Africa exports mechanics trolleys to Japan and towbars to Europe (*Business Day* 5 July 2005). CAPE Manufacturing Engineers (CME) claims to be a “second tier” exporter of catalytic components parts without the benefit of MIDP support (*Business Day* 4 July 2005). However, it may be an indirect MIDP beneficiary since the catalytic converters in which its parts are used almost certainly get MIDP benefits.

⁵ These credits can then be used in five equal annual instalments.

⁶ The following is only a brief description of the main incentives provided by MIDP. For a more complete description and analysis see Flatters 2005.

⁷ They also benefit from a virtual ban on the import of used cars.



Table 1. MIDP Import Duty Rates, 1995-2012

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
MIDP Tariff Rates (%):																		
Cars	65	61	57.5	54	50.5	47	43.5	40	38	36	34	32	30	29	28	27	26	25
Parts	49	46	43	40	37.5	35	32.5	30	29	28	27	26	25	24	23	22	21	20

Source: The DTI.

Tables 2 and 3 show estimates of the resulting *effective rate of protection* given to producers of vehicles and components. This is a measure of the percentage increase (or decrease) in domestic manufacturing costs made possible by tariffs and MIDP incentives relative to what manufacturing costs would be necessary for the firm to be able to compete in the absence of any import duties on vehicles and components and in the absence of any MIDP incentives. It takes account of the price raising effect of the tariff on vehicles and components sold in the domestic market, the offsetting effect of the duty free allowance on imported components and the value of IRCCs earned through the export of vehicles and components.⁸

This is a standard indicator of protection used in international trade policy analysis. It measures the level of protection given to existing producers, assuming capital costs are already sunk. It is indicative of, but does not accurately measure the incentive to invest. It is not able to capture the incentive provided by the Productive Asset Allowance, since the duty credits received under this part of the MIDP are not a function of current levels of production, but rather on past levels of qualifying investments.

Table 2 shows effective rates of protection (ERPs) given to vehicles produced for both the domestic market and for export for each year from the beginning of MIDP to its scheduled end date of 2012. The first row shows estimates of the ERPs provided to production of vehicles for export; they are based on the assumption that export IRCCs are used to import built-up vehicles (CBUs) and that there is full pass-through of the import duty to domestic consumers.⁹ The effective rate of protection for domestic sales (final three rows) depends on the share of imported inputs in total production costs. ERPs are shown for low (30 percent), medium (50 percent) and high (70 percent) levels of import content.

Estimates of effective protection provided to OEM components exports are shown in Table 3. Catalytic converters are subject to a slightly different regime that is designed to eliminate the export subsidy for their precious metals component. Therefore separate ERPs are presented for converters and for other OEM components exports. As with vehicle exports, the effective protection provided to components exports depends on whether IRCCs are used to import CBUs or other components. ERPs are shown for both cases.

Table 2. MIDP: Effective Protection for Motor Vehicles (%)

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Export Sales	65	61	58	54	51	47	44	40	36	32	29	26	23	21	20	19	18	18
Domestic Sales																		
Import Share																		
30%	106	99	92	86	80	74	68	62	58	55	52	48	45	43	42	40	39	37
50%	125	116	109	101	94	87	80	73	69	65	61	57	53	51	49	47	45	44
70%	175	163	152	142	132	121	111	101	95	89	83	77	71	69	66	64	61	59

Source: Flatters, 2005.

⁸ Alternatively, the effective rate of protection is an estimate of the percentage increase (or decrease) in domestic value added in the presence of prevailing import duties and incentives relative to what it would be under free trade and in the absence of incentives.

⁹ Estimates for the case where IRCCs are used to import components have also been done and are available on request.

**Table 3. MIDP: Effective Protection for OEM Components Exports (%)**

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
IRCCs used for CBUs																		
Converters	62	55	49	43	34	26	18	13	9	9	8	8	7	7	7	6	6	6
Other Exports	62	55	49	43	38	33	30	26	21	19	18	16	14	13	12	11	11	11
IRCCs used for Parts																		
Converters	49	46	43	40	34	28	20	15	12	11	11	10	10	10	9	9	8	8
Other Exports	49	46	43	40	38	35	33	30	27	25	23	21	20	18	16	15	15	14

Source: Flatters 2005.

The results show several clear patterns of protection provided by the MIDP.

- High levels of protection are given to all activities—domestic sales, exports, vehicles and OEM components.
- The anti-export bias of pre-MIDP motor industry policies has been eliminated. In the early years of the program the effective protection for vehicle and components exports exceeded 60 percent, a far cry from the negative protection due to tariffs on industrial raw materials and components and the further burdens of compulsory local content requirements under the earlier regime.
- The highest levels of protection are still given to production of vehicles for the domestic market. In its early years, MIDP gave effective protection for domestic sales well in excess of 100 percent and it remains as high as 83 percent even after ten year of operation of the program.¹⁰
- Declining import duties together with the gradual discounting of IRCCs relative to the value of exports supported mean that effective protection is declining over time. Nevertheless, after 10 years of operation, effective protection remains high—29 percent in the case of vehicle exports, 52 to 83 percent for domestic vehicle sales and 23 percent for exports of components other than catalytic converters (for which the ERP is currently 11 percent). At the end date of the program vehicle exports will still receive protection at a rate of 18 percent and domestic sales will be getting 37 to 59 percent.

Estimates of the *net subsidy to investments* in the sector as a result of the program provide broadly similar results and are not reported here.¹¹

3 Post-1995 Motor Industry Performance

The general patterns of recent motor industry performance are quite well known. The highlights are summarized in Figure 1.

Vehicle exports grew from negligible amounts in 1995/96 to well over 100,000 units per year now. Imports grew from about 20,000 units per year in 1995 to 120,000 in 2004. Investment in the vehicles sector has been substantial and has grown steadily, from less than R1 billion in 1995 to over R3.5 billion in 2004, and has exceeded R2.5 billion in every year since 2001.

Components exports have grown in a similar fashion and are now in excess of R22 billion per year. While a wide variety of products are exported, over 50 percent of the total is accounted for by just two, catalytic converters (38 percent of the total) and stitched leather seat covers (14 percent).

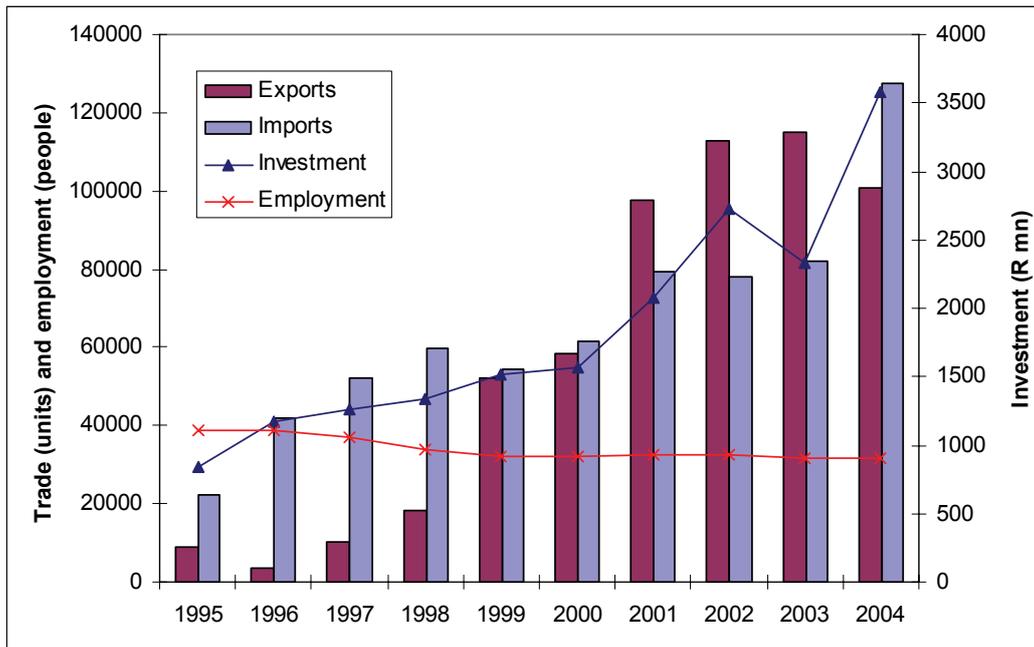
Employment growth has been much less rapid, but that topic is left to a later section.

¹⁰ This does not take account of the substantial protection to domestic market sales provided by the virtual ban on the import of used cars.

¹¹ They can be found in Flatters 2005.



Figure 1. Vehicle Assembly in South Africa



Source: Compiled from NAAMSA data.

4 Trade and Poverty

We discuss three main links between trade and poverty in the motor industry:

- the direct impacts of trade on the poor through the prices of vehicles,
- impacts of trade on employment, and
- impacts of trade on the public sector budget.

4.1 Trade and Prices

International trade has affected vehicle prices in a number of important ways. The decision to liberalize this sector has enabled South African consumers to benefit from wider choice of automobiles, not constrained to buy from high cost domestic producers that, prior to the start of liberalization, operated at very high cost due to low scale production runs and other regulatory requirements, especially local content regulations. Gradual reductions in import duties on CBUs have allowed prices to fall in a similar fashion.

However, the continuation of import duties has kept vehicle prices higher than they otherwise would be. Despite the export of vehicles at competitive international prices from South Africa, domestic consumers still pay a duty-inclusive (or import parity) price.

Furthermore, the virtual ban on the import of used cars has denied South African consumers access to an alternative source of high quality vehicles at very competitive prices.

There has been considerable discussion of the magnitude of the price raising effect of South Africa's vehicle import duties. A number of studies have attempted to compare South African prices with those in other markets. An early one (Barnes et al 2004) claimed to show that prices in South Africa are similar to those in the UK, while a later one by the same authors (Barnes et al 2005) reached the same conclusion for high-end vehicles but found that South African prices were higher at the low end



of the market. The Competition Commission has recently reported a finding from its own research that South African vehicle prices are 14 percent higher, on average, than in the EU.¹²

These studies all suffer from the difficulty that they compare retail rather than manufacturers' prices, and thus assuming that distribution and sales costs are identical between South Africa and comparator countries. This is a dubious assumption and almost certainly biases the results in favour of showing "good" prices in South Africa. They also suffer from using comparator countries that are well known as being high price markets, once again biasing the results in favour of demonstrating price competitiveness in South Africa. Finally, by using "representative" cars from the South African market, they ignore one of the most important impacts of protection of the local industry—to saddle low-end South African consumers with out of date and technological obsolete vehicles that have been out of production in the rest of the world for decades.

We are not aware of any formal studies of used car prices. However, casual observation suggests that the price differentials on used vehicles are much larger than on new cars, frequently in the order of 100 percent or more.¹³ Recent pressure by vehicle dealers in Namibia to force the government there to enact a similar ban to South Africa's on used car imports suggests that price differences are large. Strong measures by the South African government to prevent smuggling of used cars that have been legally imported into BLNS neighbours suggest the same thing.

Whatever might be the findings of inter-country retail price comparisons, there can be little doubt that the South African import duties on vehicles and components make their domestic prices higher than they otherwise would be. The following evidence from the South African motor vehicle market confirms that consumers are paying at least a duty-inclusive price.

- Vehicle sellers often pay 80 to 90 percent of the face value of import rebate credit certificates and have been complaining recently about shortages of IRCCs in the market.¹⁴ Almost all of the IRCCs purchased are used to offset the duty on imported cars, not components. The market value placed on IRCCs reflects the mark up over the border price that must be recovered from the consumer. The fact that IRCC's have a market price greater than zero is indisputable evidence that prices of vehicles are greater than the border price.
- Vehicle producers have been quite vocal about the need to continue MIDP if they are to continue producing in South Africa after 2012. This would appear to contradict claims that the MIDP incentives are of no value to them, as would be the case if duty savings were being passed on to consumers.
- Discussions of market pricing with some South African vehicle sellers suggest that current prices are higher, not lower, than the duty-inclusive price. According to them domestic prices can be thought of roughly as the sum of the c.i.f. cost of importing, all import duties and taxes, all domestic distribution and sales costs, including a normal return to all capital invested, plus another 10 percent, making South Africa one of the most profitable vehicle markets in the world at the moment.

In summary, the MIDP works by subsidizing production of vehicles and OEM components for both the domestic market and for export. The subsidies are paid for by domestic consumers of vehicles in the form of restricted choice and higher prices. The system of duty credits on exports means that consumers subsidize not only vehicles produced for the domestic market, but also those produced for export. The import duties that the Treasury foregoes in honouring export IRCCs do not lower the prices paid by domestic consumers. Rather, they subsidize vehicle and components exporters while domestic buyers still pay (at least) a duty-inclusive price.¹⁵

¹² See press reports and commentary, for instance, in *Business Day* September 12 2005. The Commission has apparently discussed its study with the MIDP Review Team, but has not made it more generally available.

¹³ Our own comparison of internet quotes on four Japanese used vehicle models offered for delivery in SADC with similar models (with equal or lower specs) advertised in South Africa found price differentials equal to or in excess of 100 percent in three cases and more than 40 percent in the fourth.

¹⁴ Based on authors' discussions with vehicle importers.

¹⁵ Some MIDP supporters observe that IRCCs are only pieces of paper that can be used in lieu of import duties, but cannot be used to buy anything else. Since they are not a cash outlay from the government budget, they argue, they are not really a subsidy. By this test, neither a prohibitive import duty nor a ban on vehicle imports would be considered a subsidy to domestic producers. Defining subsidies solely as cash outlays is very different from common usage in economics. Regardless of what label one might wish to apply, the IRCCs provided by the MIDP are of real value to exporters and have

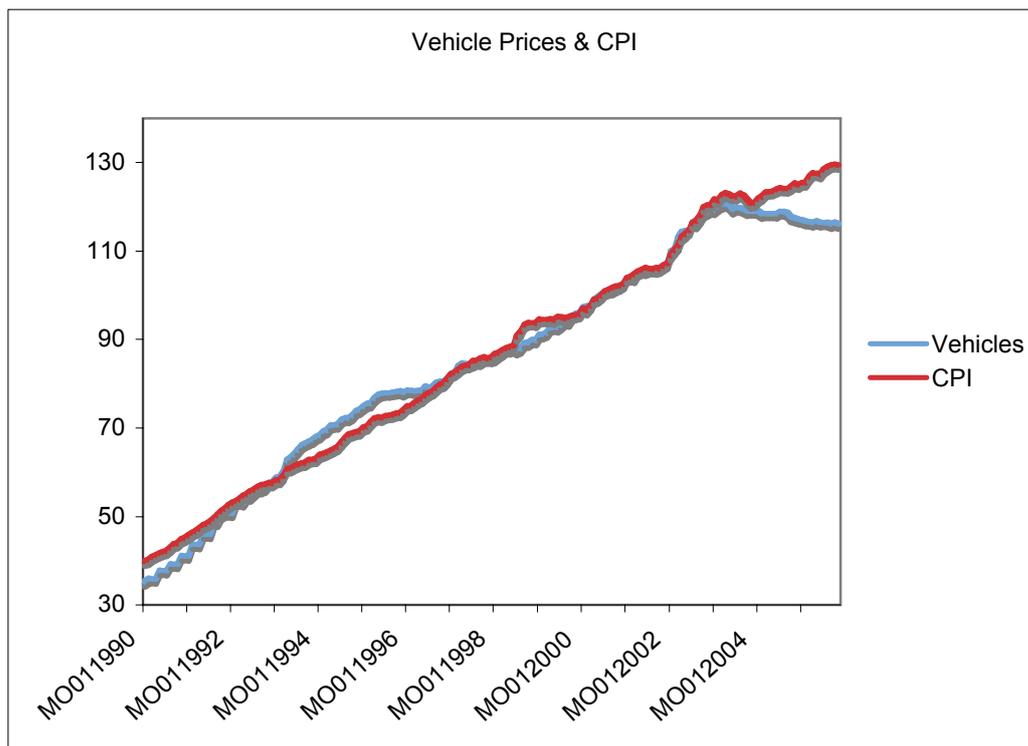


We can conclude therefore that

- the factory price of new vehicles in South Africa is no less than the duty-inclusive import parity price, and
- the mark up on used cars is at least as much and might be considerably greater.

One implication is that, at least under moderately competitive market conditions in the domestic market, vehicle prices should have fallen over the past decade, at least relative to prices elsewhere, and maybe relative to overall consumer prices. A crude test of this hypothesis is simply to compare average new vehicle prices and the overall consumer price index (CPI) for South Africa.¹⁶ Figure 2 shows a plot of both the CPI and the StatsSA index of vehicle prices since 1990.

Figure 2. Vehicle Prices and the Overall CPI



Source: Statistics South Africa consumer price indices from StatsSA web site.

The data suggest that until about 1995/96, when the MIDP began, vehicle prices increased more rapidly than overall consumer prices. For a year or two thereafter vehicle prices grew more slowly than the CPI and then grew at more or less the same rate until sometime in 2002. From then until the end of 2005 vehicle prices and the CPI have diverged considerably, with vehicle prices actually falling slightly while the CPI has continued to grow.

While these crude data patterns prove nothing conclusively, they are consistent with a number of possible hypotheses. Among the more interesting are the following.

- In both 1995 and 2002, the beneficial effects of substantial tariff reductions on motor vehicles were passed on, at least in part, to consumers. The mystery then is why there was no divergence

real effects on their cash flows. The price-raising effect of the associated import duties on vehicles has a real impact on vehicle buyers.

¹⁶ The CPI might be argued to be an inappropriate comparator since it includes services and non-tradeables that would be expected to be less responsive than tradeables to tariff and exchange rate shocks, especially during the recent period of Rand appreciation. However, domestic vehicle prices include quite a large retail service component and it is for that reason that we use the CPI rather than some other index such as the manufacturing producer price index that excludes retail services and other non-tradeables.



between vehicle prices and the CPI between 1997 and 2002. One possibility is that there was simply a lag in the response of the market, due in part to its relatively underdeveloped state. The massive growth in car imports in recent years might be a reflection of both growth in the market and a lagged response of the industry to the possibilities opened up by trade liberalization. The lag might also reflect the fact that, despite rate reductions there was still some “water” in the tariff. Whatever the explanation, there can be little doubt that in recent years the market has begun to respond to tariff reductions, partly through lower prices and partly through introduction of a much greater variety of imported vehicles.¹⁷

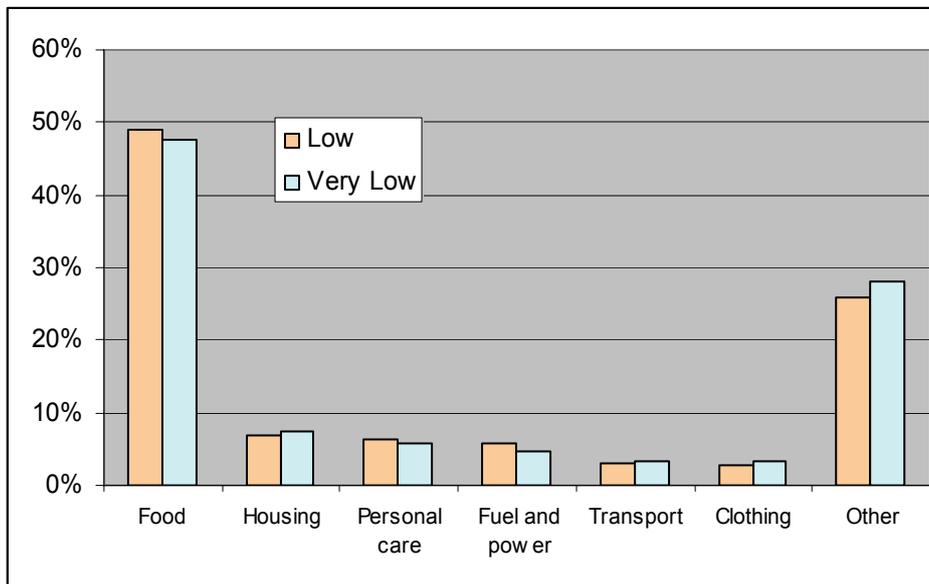
- Another possible explanation of the recent divergence between vehicle prices and the CPI is the real appreciation of the Rand that began at about the same time as the observed price divergence. This would also help to explain the recent boom in vehicle imports.

More serious econometric investigations into the links between the tariff, the exchange rate and domestic prices would be a welcome addition to knowledge about price transmission mechanisms in this and other key sectors of the South African economy. Pending such research, to the extent that either or both of these hypotheses are correct, they provide an indication that trade has helped to bring down relative prices of new motor vehicles. Nevertheless, the initial level of the import duty rates, the slow pace at which they have been and continue to be phased down, and the current levels that are significantly above the general structure of South Africa’s import tariffs mean that South African consumers pay significantly higher prices than necessary for motor vehicles.

What do high vehicle prices mean for the poor?

Measured as a proportion of income spent, new vehicles are not nearly as important in consumption spending, on average, for the poor as for middle and higher income consumers (see Figures 3 and 4 below). The unnecessarily high prices of vehicles, especially used ones, make this even more true than necessary in South Africa. Consumption of the two lowest income quintiles groups is dominated by food as illustrated in Figure 3.¹⁸

Figure 3. Consumption Shares for Low and Very Low Expenditure Groups

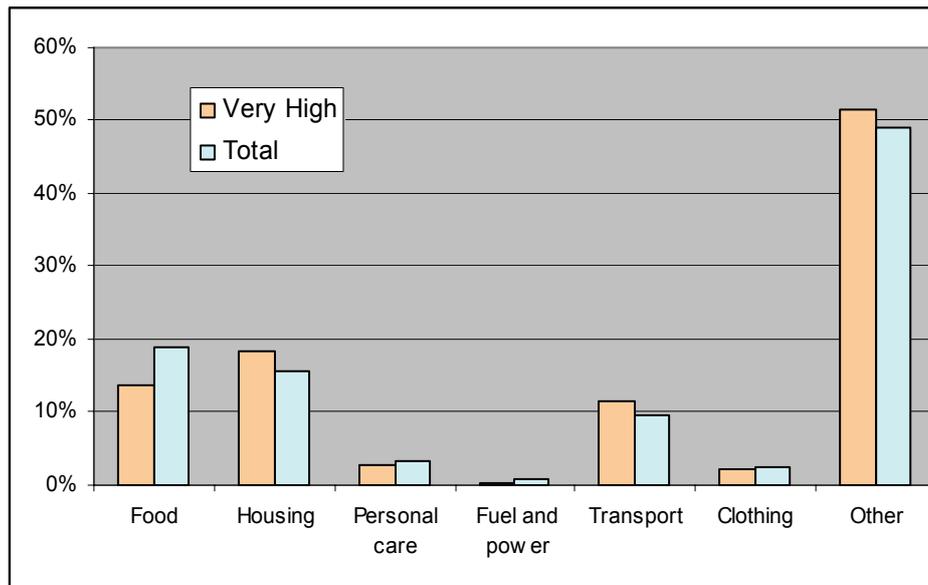


Source: Stats SA Consumer Expenditure Survey, available on line at Stats SA.

Figure 4. Consumption Shares for Very High and All Expenditure Groups

¹⁷ The recent demise of the Mazda 323 and Toyota Tazz are indicators of the same phenomenon on the production side.

¹⁸ The last two quintiles of South African households by expenditure constitute very low and low expenditure groups. Very low expenditure households spend up to R 8 070 and low expenditure households spend between R8 071 and R12 263. Very high income groups spend R 41 485 while the total expenditure is R26 264.



Source: Stats SA Consumer Expenditure Survey, available on line at Stats SA.

Does this mean that transportation and motor vehicles are unimportant for the poor? No. The Statistics South Africa expenditure survey from which the previous tables are derived also shows that the bulk of expenditure on transport services by the poor goes to minibus taxis and hired transport (see Figure 5). Another data source, the National Household Travel Survey shows that almost half of the households with a monthly income of R500 or less spend more than a fifth of their income on transport. Taxis transport about 65 per cent of commuters in South Africa. The importance of taxis as a means of transport is more pronounced in poor communities.

The negative impact of vehicle prices on the poor is aggravated by urban configuration legacies from the previous regime that have led to wide geographical separation between work and accommodation, especially for the poor. Public transportation systems have not developed sufficiently to deal with this problem. As a result time and transport costs are a great barrier to obtaining work and a very large drain on net incomes and on the quality of life for those who do find jobs.

High prices of new vehicles and the ban on used car imports combine to keep used car prices high and to ensure that vehicles tend to be kept on the road regardless of roadworthiness and passenger safety.¹⁹ This is especially important for the taxi services that are so important for the poor.

The effect of high vehicle and transport costs on the poor is multi-dimensional.

- Since poor communities are concentrated in informal settlements, rural villages and townships away from passenger train and bus routes, hired transport plays an important part in transporting people to church gatherings, funerals, stokvels, and family gatherings. This entails hiring of buses, taxis and privately owned vehicles.²⁰
- A growing perception of significant quality differentials between township and city schools have led to increased demand for associated school transport. High costs of this service are a major barrier to access to better quality education for poor families.²¹
- High commuting costs are a serious barrier to job-search activities for the poor who live in townships and other remote communities and lack the means to cover the significant out of pocket costs of seeking work.

¹⁹ Without a relaxation of import duties on vehicles and components and of import restrictions on used cars plans to “recapitalize” taxi fleets will be more of a subsidy to the auto industry than to poor users of transport services.

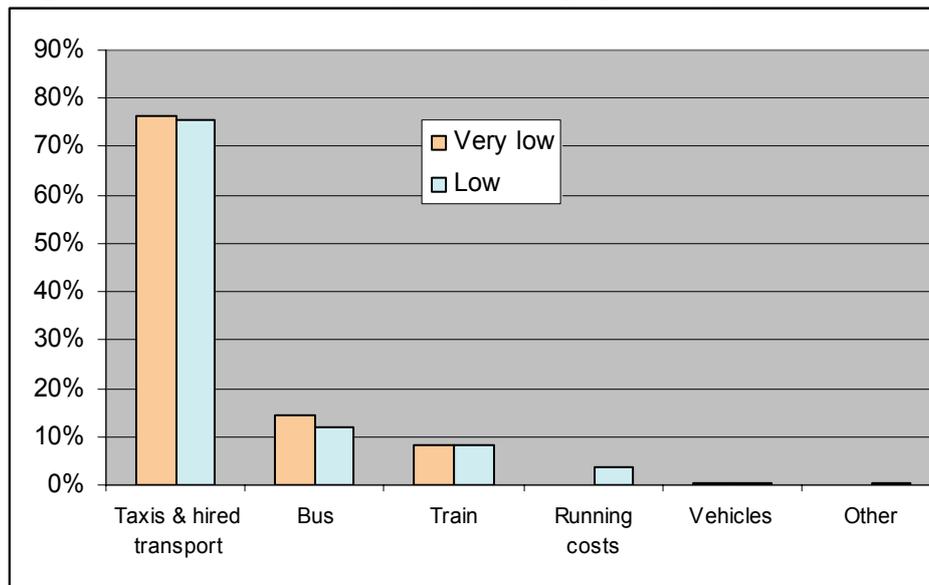
²⁰ Current law does not permit vehicles owners to charge a fee from passengers. They are required to have a public drivers’ permit necessary to transport passengers. This law is obviously being flouted.

²¹ High costs are only one of the barriers. Other problems include serious overcrowding of vehicles and the use of vehicles that are of questionable roadworthiness and suitability for transport of people. These problems can also be traced, at least in part to the cost of new and second-hand vehicles.



- For those in poor communities that are fortunate to get employment outside, the time and financial costs of daily commuting are a major drain on net income from employment. The National Transportation Survey referred to earlier suggests that the commuting tax is often as high as 20 percent of income. An additional time tax of 50 percent of the normal working day significantly reduces time available for household activities, including child-care.
- Budget and used cars can be a major cost item for small businesses and entrepreneurs, and their high prices can be a significant deterrent to entry into a wide range of income earning businesses for the poor. Informal traders also rely on hired transport to move wares from suppliers and to the selling points, particularly at sports and cultural events, music festivals, etc.

Figure 5. Breakdown of Transport Spending by Low Expenditure Groups



Source: Stats SA Consumer Expenditure Survey, available on line at Stats SA.

4.2 Trade and Employment

What has been the net effect of trade in the motor industry on wages and employment? The original goal of the MIDP was to assist and provide incentives for the motor industry to adjust to trade liberalization and become internationally competitive. The success of the program in stimulating investment and exports has led it to be viewed as a possible model for development in other sectors of the economy.

Has there been a payoff from MIDP in terms of employment? Table 4 shows that for the first five years of the program, employment in the manufacture of both vehicles and components declined by 17 percent. Since 2000, employment in vehicle production has more or less stabilized, but has not grown significantly. Investments in excess of R12 billion since 2000 have resulted in virtually no job growth in vehicle assembly. Employment in components production (including tires) has grown by a modest 6 percent, or barely over 1 percent per year, over the same five-year period.



Table 4. Employment in the Motor Industry

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Assembly	38600	38600	37100	33700	32000	32300	32389	32370	31700	31500
Components	47000	45000	44000	40000	39000	38500	39000			
Components					67200	69500	72100	74100	75000	74500
Tyres	11000	10000	9500	9100	9000	8600	8700			
Tyres					6670	6575	6300	6000	6000	6000
Motor Trade	178000	180000	180000	170000	175000	180000	182000	185000	191000	194000

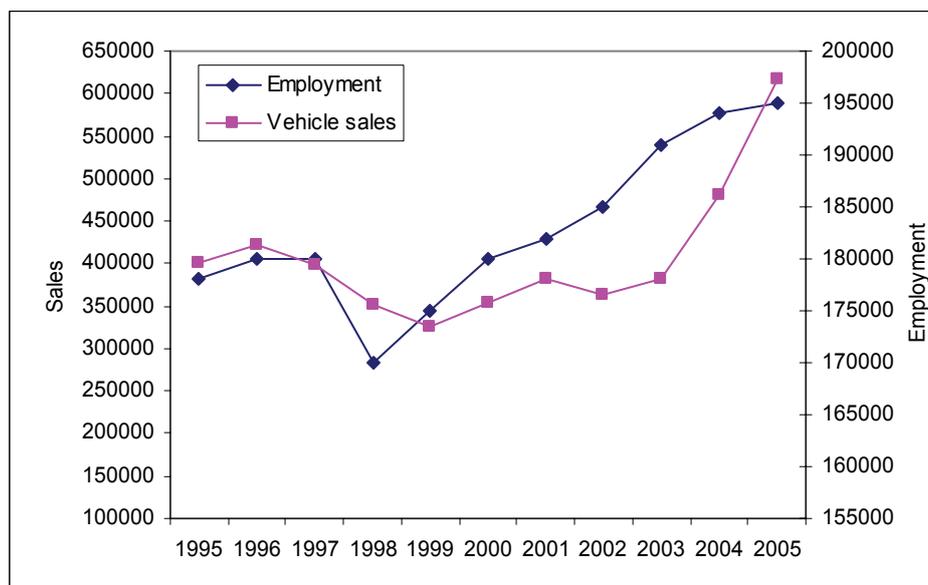
Source: NAAMSA. Note that the breaks in the series for the components and tyre industries are a result of statistical reclassifications undertaken by NAACAM, the association of components manufacturers. Note as well that employment in assembly is exaggerated by the inclusion of components units operated by OEM assemblers.

An unanswered question is whether the MIDP has resulted in the development of an internationally competitive domestic motor industry. If not, it will become permanently dependent of sizable subsidies, or it will fail. Failure would result in significant job losses. Many of these jobs are not jobs that were temporarily saved as a result of the MIDP, but new jobs that never would have existed without the MIDP. There can be little doubt that there have been significant labour market adjustments in this sector over the past decade, with many jobs lost and some new ones created. If the end result of the MIDP was to have shed a number of unsustainable jobs while creating a number of new but ultimately unviable ones, one might ask whether there might be more efficient ways to assist workers who were displaced by trade liberalization and to create more sustainable and hence more permanent jobs that are not dependent on long term subsidies.

Regardless of the answers to these questions, the more interesting and much less explored employment story in this sector is in the motor trade, the service industry involved in sales, distribution, maintenance and operation of motor vehicles. Table 4 shows that this sector accounts for twice as many jobs as in vehicle and components production together. This does not include the downstream transportation service sector, another employment intensive activity.

Figure 6 shows that since 1998 motor vehicle sales have been growing quite rapidly, as has employment in the motor trade.

Figure 6. New Vehicle Sales and Employment in the Motor Trade



Source: NAAMSA

The motor trade comprises several distinct elements—selling of vehicles, maintenance and repair of vehicles, sales of spare parts, and sales of fuel. Table 5 shows the relative magnitudes of these different components in terms of several indicators in 2002.

**Table 5. Summary Data for the Motor Trade Industry, 2002**

	Sales of Motor Vehicles	Maint. And Repair of Vehicles	Sales of Motor Vehicle Parts and Accessories	Sales and Repair of Motor Cycles and Related	Retail Outlets for Automotive Fuel	Total
Total Income (Rm)	85 454	11 284	18 979	1 152	33 216	150 625
Net Profit (Rm)	1 998	175	510	54	242	2 979
Capital Exp. (Rm)	720	150	120	3	215	1 209
Gross Salaries (Rm)	4 270	2 011	1 803	73	1 368	9 525
Number of Employees	52 535	46 709	32 967	1 549	51 362	185 122

Source: Stats SA²²

Motor vehicle sales and service have been rapidly growing and apparently quite profitable industries in South Africa recently. There are approximately 1,150 franchised motor vehicle dealerships in South Africa. Most of these dealerships distribute and sell new motor vehicles on the basis of franchise agreements with car manufacturers. About eight companies own most of these dealerships, McCarthy Limited being the leader with a turnover of around R12 billion. Imperial Holdings with a turnover of about R12 billion and over 100,000 of new vehicle sales in 2004/05 was ranked second. There are four other key players in the industry namely Barloworld Motor, Unitrans Limited, CMH Group and Super Group and two smaller ones (Forza Group and Vaal Auto). There are also about 400 quality independent dealerships as well. Several of the major vehicle producers have also been investing heavily in the retail and service sectors recently.

Service, whether in large integrated sales and service outlets or in small neighbourhood garages and panel-beating shops, is clearly labour intensive and probably much more so than vehicle or component manufacturing. Petrol sales are even more so, and provide an important entry point into the formal labour market for unskilled black males (HSRC 2002). In 2002 minimum wages (excluding tips) for petrol attendants were lower than that of domestic workers. Workers in this industry generally have no prior or on the job training and are often recruited from the streets (HSRC 2002). A poll conducted on the industry found that over two-thirds of petrol attendants had no prior work experience in the industry (ibid).

Employment in the motor trade depends primarily on the level of sales and the stock of motor vehicles on the road in South Africa, regardless of where they are manufactured. Figure 6 above shows the strong relationship between vehicle sales and employment in the motor trade.

There can be little doubt that high prices are a constraint on vehicle demand, and that these are due in turn to the import duties and the ban on used vehicle imports through which the MIDP supports the assembly industry. The recent boom in domestic sales is due to a number of factors including, at least in some part, the significant reduction in import duties that has occurred since the start of MIDP. The potential for future growth has not gone unnoticed by the OEM manufacturers and other major players in local sales. These firms have begun to invest heavily in "lifestyle" sales and service centres, each of which supports a significant number of jobs relative the amounts invested.

Further liberalization of the vehicle market through tariff reductions and elimination of restrictions on used car imports would lead to continued growth in associated downstream motor trade and transportation service industries. Resulting employment growth in these sectors would offset considerably and might well outstrip any reductions in employment in vehicle and component assembly.

Finally, as noted in the previous section, high vehicle prices have an important effect on transportation for the poor in relation to job search and commuting. And they are barriers to the development of new small businesses that might be of particular importance in generating income earning opportunities for the poor.

²² Note that the numbers in this Table 4 and Table 5 differ slightly due to rounding.



4.3 Trade and the Government Budget

In its support of the motor industry through the MIDP the government has foregone substantial amounts of customs revenues since 1996. Between 1996 and 2005 IRCCs in excess of R90 billion were granted and utilized. In 2004 and 2005 alone, this resulted in a reduction in import duty collections of over R11 billion. In addition, over 2004 and 2005 another R475 million of duty credits were granted under the PAA program, of which about 410 million have already been utilized.

The government has, however, collected import duty revenues on vehicles and components that have not benefited from MIDP rebates or credits. As result of the recent boom in vehicle imports that share of vehicles in total customs duty collections has risen from 5 to 32 percent. In 2005 alone, duty collections on vehicle imports were R4.8 billion, almost as much as was given away in duty rebates through the use of export IRCCs.

There are no estimates of which we are aware of the costs of other support through other national programs and incentives, local and provincial government programs such as Blue IQ, and investments in IDZs and other facilities.

Revenues foregone through the export IRCCs and PAA credits are currently running at about R6 billion per year, and consumers are paying another R5 billion per year in duties on imported new vehicles. These alone amount to well over R100,000 per worker per year in the vehicle assembly and components industries.

These are amounts that are serving to subsidize production of motor vehicles and components for export and for the domestic market. They result in some combination of rent transfers to (mostly foreign) vehicle assemblers and subsidization of excess costs (or inefficiencies) of producing these products in South Africa.²³ As was seen in the previous two subsections, they harm consumers, with real and serious consequences for the poor, and make at best a very marginal contribution to employment. For the much greater number of jobs of most relevance to the poor, in the downstream auto sales and service industries, the employment impact is certainly negative.

Scaling down the government's support of the motor industry would release considerable resources for other uses, some of which could be used to much greater benefit in attacking poverty and at the same time achieving the longer term (and completely consistent) goal of promoting sustainable economic growth. Modest additions to budgets for health and education would be highly effective in this regard.

If there is truth in the motor industry's claim that much of the industry could not survive without continued support at current levels —i.e. that the goal of creating a competitive motor industry in South Africa was not achievable—then reduction of support would necessitate some difficult labour market adjustments in the vehicle assembly and/or components sectors. This would be offset by corresponding and maybe even greater employment gains in the motor trade and other industries of special interest to the poor. Nevertheless, the adjustment costs to workers in the declining sectors would be real and would require government attention. A fraction of the more than R100,000 per worker per year currently being paid by South African consumers to protect jobs in the motor industry would suffice to cover all conceivable adjustment costs. A temporary excise tax on all vehicle sales in South Africa at considerably less than current tariff rates would yield enough revenue to provide very generous adjustment assistance, training and even long term income support when necessary. This would be far cheaper and much more beneficial to the poor than the kind of support currently provided to shareholders of a few foreign car producers.

5 Conclusion

There has been substantial trade liberalization in the motor industry over the past decade. Nevertheless, protection has remained high, especially compared with most other sectors of the

²³ See Flatters 2005 for estimates of the magnitude of these subsidies for particular types of investments.



economy, and substantial new support has been provided to production of vehicles and components for export. The direct beneficiaries of this support have been the shareholders of a handful of foreign owned OEM producers. Representatives of these firms have declared that their manufacturing activities and related employment are not sustainable without permanent support at current levels. The slow pace of liberalization has hurt the poor through its effects on vehicle prices, employment and the government budget. High tariffs keep vehicle prices and the cost of transport higher than necessary, with adverse effects on the poor who are highly dependent on taxi services for commuting and job search, and on inexpensive vehicles as necessary inputs for many small businesses. While protection has saved some jobs and created some new ones in the vehicle and components assembly industries, very large subsidies have created few if any net new manufacturing jobs and have been a hindrance to the development of new jobs in vehicle sales, service and maintenance, many of which would be much more relevant to the poor.

Budgetary resources used to support this sector could have been much more effectively used to help the poor, even after taking account of necessary adjustment assistance needed to help any workers displaced as a result of speedier liberalization.

6 Annex: Future Research

This project has encountered a number of issues in which further research would be helpful in understanding the effects of trade policy and its effects on the poor.

- South Africa has undergone considerable tariff reform and experienced substantial real exchange rate changes over the past decade. Nevertheless there is still little systematic understanding of the relative and absolute importance of their impact on domestic prices and how this varies across sectors according to economic characteristics of the industries and the competitive nature of their markets. This is an area in which careful econometric analysis could prove a useful complement to case study materials such as those in this and other studies for the Trade and Poverty Project.
- It is apparent that the poor are highly dependent on various forms of informal and formal transport networks. A greater understanding of the structure and costs of these networks, their direct and indirect economic impacts on the poor, and the implications for costs of trade policy alternatives would be a very useful input to future trade and industrial policy decisions.
- While we have aggregate data on the numbers of jobs in various sectors of the motor industry and the motor trade, we are aware of very little information on annual flows into and out of each sector, and what kinds of workers (age, skill levels, gender, etc.) are involved in each. Such data are necessary to understand labour and income mobility patterns, and to design sensible and necessary adjustment assistance in the event of normal and policy-induced labour market disruptions.

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