

5.2 Details

(iv) AUTO COMPONENT MANUFACTURERS ASSOCIATION

- Organisation** : Auto Component Manufacturers Association
- Objective** : CEO's Mission to assess the auto parts markets in the major countries of Latin America
- Date** : 2-19 May 1999
- Countries** : Argentina, Brazil, and Mexico

Summary Report

Argentine auto industry is the main beneficiary of the liberalisation process. Investment policies went through sudden liberalization and all the MNC component manufacturers have set up their bases in Argentina. Most locally owned companies have been taken over by MNCs. There is a National Automotive Policy for the vehicle manufacturers, based on local content and foreign exchange content is calculated by Government. Customs duties on vehicles is from 25 per cent to 30 per cent and on components the customs duty varies from 12 per cent to 18 per cent for outside Mercosur trade. The Tier System of companies is as below:

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|--------------------------------------|-----|--------------------------------|
| 1. "International" Tier 1 Companies | 30% | |
| 2. "Local" Companies with Licences | 19% | Tier 1+2 |
| 3. "Joint Venture" Companies | 21% | Tier 1+2 |
| 4. "National" Family Owned Companies | 30% | Tier 2+3+Spare Parts Suppliers |

There are 14 vehicle manufacturers in Argentina. Over the past three years, vehicle production has reduced from a level of 446,000 vehicles in 1997 to 370,000 vehicles in 1999. Exports, local sales, imports and investments have all shown a downswing during the same period. Capacity utilisation is only about 35 per cent, still more capacity is being set up as all MNCs want to have their presence in

Argentina. The situation is not very good and similar to that of India. Most OEMs are 100% owned, or with only 15-20 per cent local equity. Even these companies are expected to become 100% owned soon and no joint ventures will be left.

Brazil has a well-established and mature automotive industry. All the vehicle manufacturers are 100% foreign owned. Most Brazilian companies of its components industry went for tie-ups with MNCs. About 30 large multinational companies produce 70 per cent of all components produced in Brazil for the OEMs. Total sales of auto parts in Brazil is about US\$3 billion. There is tremendous potential for spare parts business in Brazil for Indian companies. Preliminary estimates point out that it will be a market of at least US\$ 100 million.

Cost production in Brazil is very high and there is need for cost cutting for survival. The theme of Brazil companies is to increase production and reduce costs. Many companies are thus looking to diversify their sourcing from countries like India to reduce their cost.

Mexico is different as it is a part of the NAFTA with USA and Canada. Mexico has gained access to a potentially large market of USA and Canada through this agreement. Automotive production in Mexico is on the rise since 1980s. Total vehicle production is around 1.2 million. Almost 50 per cent is exported to USA and Canada.

Mexico has a very clear Local Content Policy for the automotive industry. The key factors of the Mexican Auto Policy are “local content” and “exports” to earn foreign exchange which will allow imports of CKDs. Besides, the Mexican Government also calculates the local content of vehicles. Hence, even if an imported raw material is used for manufacture of the components by a Tier 3 supplier in Mexico, the value of raw material is considered as “import content” while calculating local content of the vehicle. After 2003, this National Automotive Policy will be substituted by the NAFTA Rules of Origin. A majority of the Mexican component manufacturers have now been taken over by MNCs. Local family owned units, which have survived the competition and emerged as successful global suppliers to the vehicle manufacturers.

Some of the key findings of the mission to these three countries are that they implement the “local content policies”. Calculations of local content go down to the Tier 4 level. In India, it is difficult to even monitor local content at Tier 1 level. Level family owned business to survive anywhere in the world, it is important to establish independence in the area of technology and R&D, thus must have its own R&D in order to remain in business. Mission’s Report suggests that becoming an OEM supplier, it is also necessary to have the right relationship and to be a part of a global supply system. This can be done only through strategic relationship with the MNCs.

Component manufacturers should pay more attention to their basket of customers. Total dependence on only 2-3 OEMs is not a good idea. Each component manufacturer should make to competition. An ideal strategy is to develop a strong export business.

The Mission also strengthens the ACMA’s view that smaller companies will have to exist mainly Tier 2 or 3 companies in the global supply chain. Therefore, a 3-point agenda for survival of the Indian SMEs could be:

1. Invest in skilled people
2. Invest in R&D. Profit should be used for investing in R&D.
3. Never give up or sell-off your brand.

Commercial practices being followed by the global OEMs and component suppliers, Mission suggests the following aspects:

1. Warranty Claims and Cost of Recalls
2. Annual Price Reductions
3. Supply of Components in the after market.

Apropos Warranty Claims & Cost of Recall suppliers have full responsibility in case of warranty claims. OEMs usually debit the component manufacturers with the full consequential liability in case of a warranty claim under a prescribed procedure for returning of the defective part. The overall conclusion that is drawn from ACMA’s discussions with more than 15 Latin American component and vehicle manufacturers are that warranty costs were a real cost for the component manufacturers. So far in India, this has been limited to “replacement cost” only. This would soon extend to cover “total recall cost”. Furthermore, insurance cover may be possible only for recall costs and not for daily warranty claims.

On the sales of components in the after-market issue, Mission gathered as much inputs from the MNCs as well as local suppliers there on the after-market practices being followed in these countries by the global vehicle players. It is found that a small degree of variance in practice by the OEMs is discovered depending on the product in question. This variance is based on whether the tooling and design of the components is the property of the OEM or the component supplier. Wherever, the component development had been done jointly by the supplier and OEM, this subject is discussed and negotiated between the two parties. After-market restrictions are normally in force for 6-7 years which is the average lifespan of the vehicle. Once the model goes out of production, usually the suppliers are allowed to directly sell the components in the after-market or continued spare parts availability.

The current trend is that the OEMs do not want to bear the high cost of tooling. Hence in the emerging situation, the component manufacturers must retain the right to sell spare parts directly in the after-market under their own brand name.

It has been learnt from this experience that it is extremely important for Indian suppliers to maintain their brand equity in the market.

Many OEMs in India have started asking for a price reduction every year. In some case these price reductions are being sought from retrospective effect. Global OEMs in Latin America follow a wide variation in the manner OEMs treat different companies in this respect. Larger, stronger MNC component manufacturers seem to be in a better negotiating posture than the smaller, local companies. Most contracts are negotiated mutually. Price reductions are expected to be achieved through suggestion schemes or through value analysis activities in companies, leading to higher productivity.

It is also observed, that in case there is an increase in the cost of raw materials, the OEM always discusses and negotiates the new price with the suppliers. Raw material price increases are always considered. The price reductions have no relation to volumes. Lower volumes due to sluggish or depressed market situation does not mean that price reductions will not be implemented.

Price reductions will be a norm in the near future, whether it is for a long-term contract or not. Indian industry will have to be prepared for it. Negotiating power of the supplier will be the most important criteria. For critical hi-tech and strategic components, the supplier may be able to negotiate better terms due to the technology and criticality of the product. Most smaller and local Tier 1 companies will have to face a major challenge. Mission report suggests that it is therefore imperative for the Indian companies to start gearing up for continuous productivity price as a factor of costs, volume and margins, etc. , will have to be re-written, particularly for the Indian SMEs.

Members of Delegation

Mr. Dinesh Munot, President and Mr. V.K. Mehta, Vice President, Auto Component Manufacturers Association (ACMA), New Delhi.

Conclusion

Indian suppliers will have to improve their own negotiating power by building a technology edge or some other strategic factor that strengthens its power to negotiate with the original equipment manufacturers (OEMs). For strategic components develop the right linkages and tie-ups with the global suppliers and develop internal strengths. For non-strategic components build own internal strengths to sustain OEM business.

Organisation : Auto Component Manufacturers Association

Objective : CEO's Mission to understand the implications of China's accession to WTO in relation to auto industry and its impact on their competitive position in the world

Date : 7-14 June 2000

Country : China: Beijing, Tianjin and Shanghai

Summary Report

This report is based on the ACMA CEO's Mission attending the Conference on "Globalisation: China's Auto Industry and the WTO", organised on 7 & 8 June 2000 in Beijing. It was also followed a 3-day programme of factory visits in the three key automotive centres of China, i.e. Beijing, Tianjin and Shanghai.

This report presents some of the key conclusions from the Conference and findings of the Mission. The report says due to massive direct investment in China, there has been an increasing focus on quality in China. This leads to a perception that China is emerging as a source that offers “European Quality at Chinese Prices”.

China’s auto industry has been growing since 1986. Broadly, the vehicle production in China is categorised into two types: Civil Automobiles and Economy Vehicles. Civil Vehicles include all commercial vehicles and other heavy vehicles including luxury passenger cars. Economy vehicles include small passenger cars, mini-vans, and mini trucks.

In 1999, China produced a total of 1.83 million motor vehicles, of which 565,366 were passenger cars. There are over 5,000 parts manufacturers in China excluding parts manufacturers that supply China’s annual output of 3 million farm vehicles, the total number could jump at least three times.

The above numbers are a clear indication that China’s auto parts industry is still fragmented, small scale, and product development capability. Leading auto-makers in China still depend heavily on parts and components supplied by their directly affiliated parts factories built in the same geographical locations.

China’s leading automakers, such as FAW, Dongfeng, SMC Tianjin, Yuejin, and Beijing were required by the state to supply itself with over 80 per cent of needed parts and components. As a result, each of the OEM now owns scores of parts manufacturers.

The Chinese auto parts industry is fragmented, with low efficiency and little economies of scale. Despite this Government’s efforts trying to reduce the total number of OE assemblers, China still has 115 OE assemblers, 525 re-fitters or re-manufacturers and another 207 farm vehicle manufacturers. By the end of 1998, China had 1,684 parts manufacturers with a workforce of 850,000 including engine manufacturers but not including manufacturers of bearings, tyres, glass and other related products. Many of the leading manufacturers of parts assemblies, except in the case of lighting and tyres, are well below the one million units mark in annual output.

China's \$7-\$8 billion after-market is largely unregulated and chaotic. Illegal operations are hurting legitimate parts manufacturers, including joint ventures set up by MNCs. There were an estimated total of 550 foreign invested parts & components companies. The Government is trying to standardize the after market parts distribution and sales.

Legitimate parts warehouse distributors and dealers are trying to build their own sales networks and chain stores. As well foreign invested parts companies are also capable of new product development by utilising their worldwide engineering resources. However, the biggest problem that faces most of these ventures is economy of scale. The sharp competition among the many OE assemblers have also driven down the prices of parts and components, cutting into the already meager profit margin of JV-suppliers.

China's high tariff rates on imported automobiles have helped increase domestic vehicle prices, making automobile assembly a lucrative business even without any economies of scale. Also over-perfectionist policies have made it much less imperative for parts and components suppliers to think globally and to become internationally competitive in terms of cost, quality, technology, R&D, delivery and services.

China's tariffs on auto parts will be reduced in equal installments from an average of 23.4 per cent at the time of accession to an average of 10 per cent by 2006 with front-loaded cuts for those parts with higher rates. Tariffs on imported automobiles will be reduced from current 80-100 per cent to 25 per cent by 1 July 2006. Import quotas on automobiles will be phased out by 2005. The gradual reduction of tariffs on automotive parts, and more importantly, China's agreement in eliminating local content requirements immediately after the country accedes to the WTO, will soon put domestic parts manufacturers in direct competition with their multinational counterparts.

On the question of China's accession to the WTO, the State Administration of Machinery Industry (SAMI) feels that China would be competitive in motorcycles, medium trucks, and mini vehicles. But China's passenger car industry would be in a weaker position. However consensus seems to be that China's accession to the

WTO will eventually improve the overall performance of China's auto industry despite the short-term pressure and challenges. With regard to Trade Related Investment Measures (TRIMs), China has agreed the terms of TRIMs, viz.

- (a) Eliminate & cease enforcing trade and foreign exchange balancing requirements;
- (b) Eliminate & cease enforcing local content requirements and refuse to enforce contract imposing these requirements on private companies; and
- (c) Impose or enforce or other provision relating to transfer of technology or other know-how only if they are in accordance with the WTO agreements on protection of IPRs and TRIMs.

China has also agreed that after accession to the WTO, it would not link investment approvals, import licences, or any other import approval process to achievement of performance requirements of any kind, including local content, offsets, transfer of technology or requirements to conduct R&D in China.

China is also open to other possible non-tariff protective measures within the scope of the WTO agreements. These may include taxes on foreign dealerships, restrictive regulations in scales, distribution and auto financing and anti-dumping procedures.

Conclusion

China has become member of WTO announced at the Doha Ministerial Meet, held in November 2001, Qatar. Tariff reduction and the phase-out of import quotas and licences seem to be the biggest challenges to many automakers as well as to the Chinese Government. China needs a period of six to seven years in order to protect this so-called infant industry from the international competition.

India should take advantage of China's auto parts industry, which is small scale and fragmented. It should concentrate on auto parts and components.

Organisation : Auto Component Manufacturers Association
Objective : CEO's Mission to study the Iran auto components market
Date : 19-24 May 2001
Country : Iran

Summary Report

Iran is one of the largest automotive after markets in the world. Iran's imports of automotive parts were US\$700 million in 1999-2000. India's share was merely US\$2.3 million, accounting for 0.33 per cent of Iran total automotive imports.

Iranian auto industry is the fastest growing industry, contributing 2.8 per cent of its GDP. There are 13 vehicle manufacturers. Iran Khodro and SAIPA are the two major giants, sharing 61.4 per cent and 32 per cent respectively. The total vehicles manufactured were 300,000 numbers in 2000. Cars account for 84 per cent followed by picks-ups 11.5 per cent, rest trucks (1.5%), 4-wheelers (1.3%) and buses (1.8%). The vehicle production target set up for 2003 is 8.74 lakh vehicles compared to 3 lakh at present.

There are 1,200 components manufacturers in Iran, having direct and indirect employment of 400,000. Iranian industry is now focusing its energies in getting into viable technology transfer arrangements from global players, including Indian companies who are willing to share technology. Therefore Iran is looking for technology tie-ups with other component manufacturers in the world who would be willing to share technology.

The automotive industry in Iran falls under the ambit of the Iran Development & Reconstruction Organisation (IDRO). These are two main automotive groups under IDRO, namely Iran Khodro and SAIPA. Both are specialised companies engaged in procurement of components from the suppliers. These OEMs do not interact directly with the suppliers, but through their procurement companies--Sazeh Gostar and SAPCO. These companies take care of the entire supply chain managements, logistics and the quality aspects.

Most of the component and the vehicle plants, visited by the ACMA Mission, have the best of machinery and the latest machine tools with a lot of investment and also excess capacity. The level of utilization of these machines are very low and also the quality aspect is missing. None of the companies seem to have much exposure to international best practices, SPC, SQC, TQC, 5.S etc. Their operations seemed to be highly inefficient with rejection levels of up to 10 per cent “on-the-line” even in the case of metal parts. Now there seemed to be a single-minded approach in all the companies to improve and to become a globally competitive player in the automotive industry.

Iran Khodro Diesel Company is keen to have technical collaborations with Indian companies in the areas of power steering, axles, differentials, pneumatics and gearboxes.

There are other auto giants on Iran, like Sazeh Gostar belongs to SIAPA Group of companies. It has been set up as a Tier 1 company that develops components and complete components systems together with more than 500 small and medium suppliers in Iran. Mego Motor Co. is a key manufacturer of engines and axles. Company makes two main types of engines--1300cc engine for the Pride and a 2400cc engines for the Nisan. SAPCO (Supplying Automotive Parts Co.) was established by Iran Khodro in March 1994 as a leading supplier and manufacturer of automotive parts and engineering services to the Iranian automotive industry as well as worldwide OEMs and OES (after market) motor vehicle industries. Zamyad Company makes minibuses and light commercial vehicles. Zamyad is keen to have JVs with Indian companies for localising the parts. SAIPA Azin manufactures door pannels and seats for Pride, Mercury Buses and trucks manufactured by SAIPA. Anghora is a part of Emdad Engineering Group. It manufactures hand tools and connecting rods. Sephan Kara manufactures starter motors of Mitsubishi type.

Iran Khodro has more than 100 subsidiaries including 70 subsidiaries for parts and components JVs in the private sector. Their future strategy is to attract foreign investment and technology. Indian can cooperate with Iranian companies with JVs and technologies transfer. There is not much scope of exporting components to Iran due to the Government regulations for local content. Therefore, JVs are the best

option. India is ideally suited to setting up JVs in Iran due to their strengths in small volume manufacture and strong technologies availability.

Indian companies have acquired a lot of component technology from the global players. This technology could be available to Iran at very economic terms through JVs with Indian companies. The priorities for Iran seem to be on passenger cars, modern and fuel efficient vehicles, local content, hard currency, and long-term relationships. That is the clear indication for the Indian mission to Iran.

There are four sets of Iranian Government policies separately covering cars, CVs, 2-wheelers, and tractor/earthmoving vehicles. The new policies are expected to give a boost to the 2-wheeler and the small 4-wheeler segments. Two-stroke engines have been banned for 2-wheelers. Emission norms in Iran are as below.

Cars	Euro I and II
Cars with Carburetor	Euro I
Cars with FI and Cataliticaical Convertor	Euro II

Customs duty on Vehicles

- 2 nd hand vehicles (less than 3 years old) with licence	15 per cent
- New cars with licence	150 per cent
- New cars without licence	190 per cent

Members of Delegation

1. Mr. L. Ganesh, President, ACMA and other Past Presidents.

Conclusion

It is due to political and other imperatives, not many European component manufacturers are interested in setting up joint ventures in Iran. This is the right time for Indian companies to partner with Iranian companies. If this opportunity is missed by the Indian companies, it would be difficult later when Iranian economy opens to the entire world. The right way to tap the Iranian market is to set up joint ventures or technology transfer arrangements with the Iranian companies with buyback arrangements or production sharing.