The Star ONLINE

Sunday, 24 Jun 2018

Heeding the realities

By Bunn Nagara

The international marketplace can be an unforgiving arena, if the hard economic realities of global markets are replaced by sentimentality or nostalgia.

THERE is a pattern and a rhythm in global markets that, when acknowledged and heeded, can yield profits – but when denied or confronted may lead to loss and pain.

Asia's two largest economies, China and Japan, are set to face off in South-East Asia in at least one sector: automobiles.

The signs of this looming challenge are becoming observable, as the portents of the rivalry settle steadily into place. A "national car" in Vietnam or Malaysia tends to miss the wood for the trees. Larger regional realities determine the local prospects, not the other way round. All goods and services are subjected to tough market realities. A temporary reprieve may come only with costly subsidies or tariffs which then render items uncompetitive over the longer term.

Among the realities of the global auto market are, first, that the motorcar is the single most costly consumer item commonly sold across borders. Second, of all the global consumer items traded daily, the car is probably the least nationally oriented. Parts come from all over the world, plants are established abroad for cost and other reasons, and companies from abroad buy proud "national" firms producing even the most prestigious brands.

Britain's Jaguar Land Rover was bought by America's Ford, and then by India's Tata. Britain's most prestigious marques, Rolls Royce and Bentley, were bought by Germany's Volkswagen which also bought Italy's supercar Lamborghini and France's pride Bugatti, besides Spain's Seat and Czechoslovakia's Skoda.

Lamborghini was previously taken over by the Swiss (Mimrans), then the Americans (Chrysler), and then Indonesians (V'Power) and Malaysians (MyCom).

China's Geely bought Sweden's Volvo, the London Taxi Company, Germany's prestigious Daimler (Mercedes) Benz, the US "flying car" company Terrafugia – and Malaysia's Proton and Lotus.

Proton had earlier acquired Britain's iconic sports car company, Lotus. Ownership "promiscuity" in the auto industry across borders is spread all round.

Some of these acquisitions may not be 100% but they are still substantial. Geely for example owns 49.9% of Proton and 9.69% of Benz, both being the single largest stake in the companies. Among the earliest purchases across borders was General Motors' of Germany's Opel in 1929, after which Opel models were still sold in the UK as "British" Vauxhall. Last year Opel was acquired by France's Groupe PSA which incorporates Peugeot and Citroen.

The pace and number of cross-border auto acquisitions continue to grow, along with the scale. It is a game for the super cash-rich, making independent national operations unviable while squeezing the prospects of new startups. In Asean countries today, mega competition on Level Two between Japanese and Chinese auto firms is shaping up. Even Korean companies are only looking in to see if there is a possible opening.

Sales of individual cars to consumers on Level One continue for all marques, but sales of whole auto companies (Level Two) are the name of the game. Apart from direct competition between Japanese and Chinese corporations, competition is growing between their locally named subsidiaries – and between rival compatriot firms. The result may see South-East Asian auto companies functioning largely as proxies of parent Chinese and Japanese firms.

SAIC Motor, China's biggest auto firm which also assembles US and European brands, wants Thailand as the regional production hub for export to other countries. Japanese companies had set that example in this region and are still trying to keep the "flag flying." Toyota has raised its stake in the Philippines, as has Mitsubishi, with increased investments in factories for larger output. However, higher levels of local technical input are still limited at best.

The international auto acquisitions market has also involved prestigious car design firms. Vietnam's first car company Vinfast proudly announced engaging Italy's Pininfarina, which designed Ferrari and Maserati models – and which was bought earlier (76%) by India's Mahindra.

Developing countries may be smitten by the "national car" bug, while developed countries are more interested in producing sophisticated high-value systems that can be incorporated into all cars: among them, AI for self-driving cars. These high-end components are the real value-added skills in auto production today, rather than basic parts assembly so commonly found in Third World car factories.

Ultimately, the issue is the degree of local content along with the technical input rather than a hidebound obsession with a "national" car. Production and ownership promiscuity across borders means that cars no longer have distinct nationalities.

Thailand produces some two million cars a year, more than half for export, about as many produced as all the other Asean countries combined. It has no national car project since it manufactures only automotive components and assembles cars from other countries. Nonetheless its automobile sector is widely regarded as economically successful, employing more than half a million people and accounting for 10-15% of GDP. Most of the world's auto parts and automobile manufacturers operate in the country.

A lack of high-end technical inputs for greater value-added has however been limiting to growth. Lately the auto sector pledged to scale up the technical ladder, with attractive government-supported incentives for environmentally clean designs.

Indonesia has ambitious plans for boosting its auto sector, encouraged by rising local demand since 2012 but still hampered by limited exports. It therefore risks mistaking local demand for overseas demand, which has been only 20% of Thailand's.

Within Asean, Indonesia is the biggest country with the biggest population and economy, but its auto sector has not been competitive internationally. Government support through protectionism is no answer. Now the Indonesian auto sector may be facing another challenge – competition from elsewhere in Asean such as Vietnam. Its structural inefficiencies remain a persistent problem.

A study by Prof Sadayuki Takii found that the problems include weak or minimal local content and government protection contributing to a lack of competitiveness. The same conditions may be found in other Asean countries.

Another reality in the global auto market is how successful companies come from countries with a sizeable domestic market providing healthy competition nationally. Through the years, market discipline made these companies competitive internationally and fit to compete against companies in other countries. Protectionism however works in the opposite direction.

Indonesian President Joko Widodo has been toying with the idea of an "Asean car," which would bring together engineering skills across this region to produce a competitive world-class item. This desire still exceeds the capacity or the prospect, unfortunately.

Countries in Asean still need to get over the lack of substantive technology transfer if they are to acquire the real skills that make the auto sector competitive. Increasing investments by Japanese and

Chinese firms at largely parts assembly level are contributing to the problem. But who can say no to immediate investments offering more jobs?

Beyond technology transfers, local players also need to become innovative on their own. That has yet to happen. Another problem to resolve is the growing competition between Asean countries. The competing concepts of “regional car” and “national car” are in a zero-sum game.

The Philippines also wants to be the regional auto manufacturing hub within a decade. This national-centric approach, typical of the region, retards regional integration and prospects for the Asean Economic Community.

The more likely prospect is to become local outposts for larger Chinese or Japanese firms.

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