CHAPTER FIVE

RETROSPECT

It has been a decade since the National Car hit the market and over this time span the automotive industry has experienced quite a drastic transformation. From the early days when cars that plied the streets were either assembled from imported CKD kits or imported in CBU form, we now have cars which have a strong Malaysian flavour. The Government seems to have reaped quite a satisfactory harvest from the National Car Project as it has succeeded in achieving applausible mileage in its intended objectives. To recapitulate :

* it has succeeded in increasing Bumiputera equity and participation in the automotive industry

* the National Car Project has indeed spearheaded the development and growth of the auto-parts and components sector and enhance greater utilisation of local components, at least for PROTON cars.

and * there has been much more technology transfer and development of skills than before.

Nevertheless there is a price for its success in these areas and the price can be quite hefty. An attempt is made to disuss some

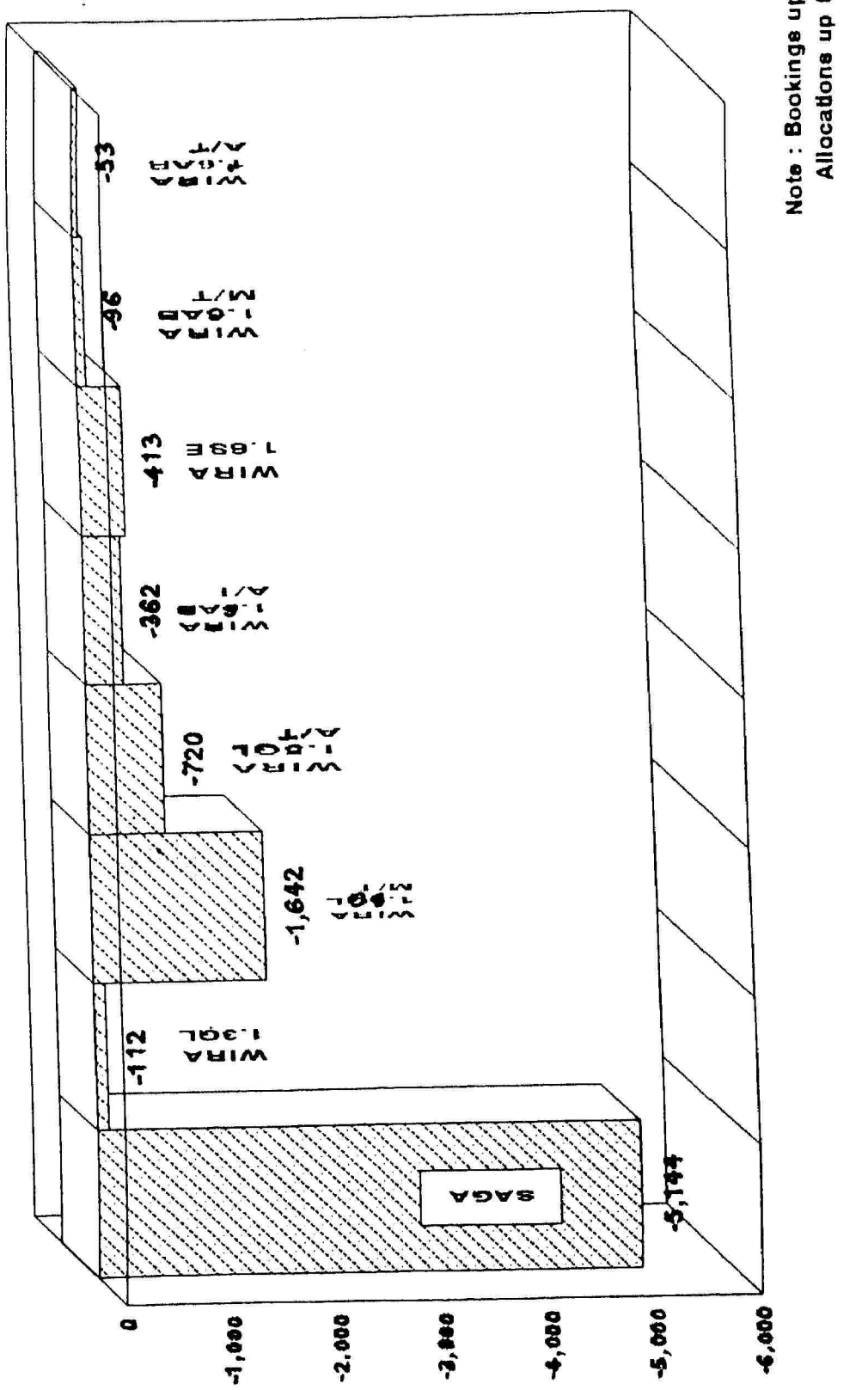
)f the more pressing issues.

5.1 : Market imperfection

Economists will definitely cry foul over the increasing degree of imperfection caused by the launch of PROTON. As it is, even before PROTON was launched, the automobile industry was already very highly regulated by the Government. Almost every aspects of the industry need the approval of the Ministry. This applies to the approved selling prices of cars to model modification and model change and even to prices of deleted components. Now, with the presence of PROTON as a player, the industry has become even more supervised. PROTON, being partly Government-owned, via shares held by the Minister of Finance Incorporated and Government Agencies, is an instrument to the attainment of the Government many national objectives. It is a means to manifest the move in the direction of industrialisation and to seek world recognition since all industrialised nations do have their own automobile industry. It also paves the way for the development and growth of SMIs and auto-parts and components industry and it is also instrumental in increasing Bumiputera's participation in the economy. With so many objectives, especially those which may not be economic-based, the question of allocative efficiency will of course surface. The over protection bestowed upon PROTON has resulted in market segmentation. Thus, the passenger car market now composes of the PROTON cars market, which is monopoly in structure, and the non-PROTON cars market which can be described

as oligopolistic in nature. The lack of competition for the PROTON market segment may harness inefficiency and market distortions. An example of this is perhaps the excess of demand for PROTON cars in relation to the ability of PROTON to supply sufficient cars. The vast price differential between PROTON cars and non-PROTON cars has resulted in product substitution and consequently the many complaints on late delivery of orders of PROTON cars. In fact the seriousness of the problem of late delivery of PROTONs does not apply equally across all PROTON cars. Figure 5.1, in showing the bookings and allocations of PROTONS for 1994, clearly illuminates the problem of market distortion that emancipates from the absence of the market price mechanism in synchronising the demand and supply of different PROTON models. The prices of the SAGAs are still comparatively much lower than the prices of the WIRAs. This is especially applicable to the ISWARA "down-specification" model which is still being sold at slightly above RM30 000. The main intention of the Government in producing this model is to cater to those who are from the lower income group. Instead, demand for this model also comes from beyond this group. Thus, this has resulted in a waiting time of as long as six months or more before a buyer can take delivery of his car. EON Bhd. expects the problem to ease in 1995 when PROTON increases its capacity to 150 000 units per annum. Nevertheless, the matter is unlikely to be resolved unless the Government can come close to the right market price for all its models. Otherwise, there will still be models which are short in supply.

Figure 5.1 : BOOKINGS VS ALLOCATIONS



5.2 : Displacement of resources

The question of possible displacement of resources arises because of the rapid take over of the dominance of the passenger vehicle market by a single manufacturer, PROTON, from a number of assemblers and the implementation of the LCMP. The assembly of motor-vehicle and the need to perhaps produce some parts in-house to meet the local material content target of the Government involves huge capital investment. This will require scale production to enable the outlay to be written-off within its expected life span. None of the assemblers, either than PROTON and PERODUA, manage to sell more than 10 000 units of vehicles per annum. Table 5.1 provides some insight into the share of the market in the last two years.

As for PROTON, it has recently invested quite a handsome sum in upgrading its production capacity and in the in-house production of some of the more complex parts and components like the engine blocks. Such investment outlay will be viable if the output of PROTON cars can be increased in the long run. This in turn depends on the future demand for passenger cars. Thus, the question on the possible displacement of resources in PROTON depends on whether the sales of PROTON cars can be increased to the required level.

Micro-economics Theories will explain that the demand for PROTON cars will depend on the prices of PROTON cars, prices of its

substitutes ie. the other makes of cars, the income per capita of household, the population size of Malaysia, existing stock of passenger cars, existing public transport system, the availability and cost of credit and the volume of replacement demand. Some of the above factors, like the prices of PROTON cars, may be favourably manipulated via Government policies. However, there will also be mounting pressure on Malaysia to open up in view of its success in the international market. Then, there are also certain forces at play that are beyond Government manipulation. For instance, the per capita income of Malaysians can only increase if the country continues to experience high economic growth. Malaysia, being an open economy, is subjected to the business cycle that impact all nations although it may not be in equal magnitude nor at the same time. Thus, it is doubtful as to whether Malaysia can always continue to enjoy an economic growth of above 8 percent .

Moreover, threats of inflation that tend to accompany economic growth may force the Government to opt for a lower rate of growth. As it is, recently, a number of leading local banks have revised their Base Lending Rates upwards although a surplus of funds can be expected in future following the Government decision to allow house buyers to withdraw as much as 30 % of their EPF savings to reduce the mortgage on their houses. Failure to sustain the current economic growth may not augur well for the passenger car market as the demand for cars tend to be income elastic. The impact of a change in income on the demand for cars may be illustrated by the effects of the stock market crash in

1987 and the recent plunge in the composite index of the KLSE. Thus, although the sales of PROTON was higher for the first six months of 1994 compared to that of 1993, the sales figure for 1994 was lower due to slack performance in the second half of the year.

TABLE 5.1 : MOTOR-VEHICLE SALES BY MAKE IN MALAYSIA

Make	1993		1994	
	Pass. Veh.	Comm. Veh.	Pass. Veh.	Comm. Veh.
PROTON	95448	-	110505	-
TOYOTA	5344	6873	6425	7948
NISSAN	6389	5833	5661	6084
HONDA	9026	-	10523	-
DAIHATSU	2124	5349	1394	6942
FORD	2729	2689	2016	2619
MITSUBISHI	70	1773	35	1935
MADZA	1538	1797	1074	1550
ISUZU	-	3504	-	3594
OTHERS	5932	3465	18132	3302
TOTAL	128600	31283	155765	33974

Source: MMTA

It is also difficult to predict with any certainty the effect of the introduction of the nation first Light Rail Transit (LRT) on the future demand for cars. Although this System is presently confined to the Klang Valley, the impact of it on the demand for cars cannot be ignored as the sales of vehicles is likely to be highly concentrated in this region as well. Thus, the success of the LRT and the single-occupancy vehicle (SOV) campaign to control the traffic woes of the urban city may backfire and hold back the rate of increase in demand for cars. If this happens, then, there is a possibility that PROTON may end up with excess capacity unless it can expand overseas. There may be difficulty in this aspect if Malaysia were to graduate out of the GSP System.

Then, there is the question on the potential market size of the passenger vehicle market. Car ownership in Malaysia has increased remarkably in the last few years. The Motor Business Review reported that there was one vehicle to every eleven people in 1990. In 1994, according to the Automotive Industry Handbook, the number of motor-vehicles to every 1000 people was 158 (refer to Table 5.2). This works out to one vehicle to every six people. As illustrated, the car ownership in Malaysia is high by ASEAN standard although it is still low when compared to the developed nations. The Managing Director of PROTON himself is of the opinion that the market may be approaching its saturation point. Yet, it is believed that the automotive industry should be producing 250 000 to 300 000 units of cars per annum to be competitive and PROTON actually has a long term plan of raising

its production capacity to around 200 000 cars per annum to take advantage of the possible economies of scale.

TABLE 5.2 : A COMPARISON OF CAR OWNERSHIP IN SOME COUNTRIES

Country	Vehicles per 1000 population
United States	755
Germany	517
Japan	483
United Kingdom	463
Taiwan	115
Rep. of Korea	98
Thailand	45
Malaysia	158
Indonesia	16

Source : "Automotive Industry Handbook"
Daily Automotive Journal 1994

Table 5.3 gives the current production capacity and the planned production of the various national cars. The market forecast for the total industry volume in 1995 is 220 000 units out of which 65 % or 143 000 is for passenger cars. Therefore, even if the various national cars are the only ones purchased, there is still

excess capacity in all the plants. In order for the domestic demand of cars to rise substantially, the Government may have to increase the replacement demand for cars.

TABLE 5.3 : PRODUCTION CAPACITY AND PLANNED PRODUCTION OF THE VARIOUS NATIONAL CARS

Make	Production capacity	Planned Production
PROTON	150 000	140 000
PERODUA	45 000	40 000
SATRIA	54 000	30 000

Source: Various Press Reports

The replacement demand for motor-vehicle depends on the average life span of the vehicles, income, trade-off prices of buyers' existing cars and Government legislation. It is definitely unspeakable to think of the Government intentionally shortening the life span of motor-vehicles in an attempt to increase the replacement demand for vehicles. However, the government has ample room to provide the need to replace vehicles via its legislation. For instance, it can in the name of environment protection gradually phase out the sale of leaded petrol in the market. In doing so, cars of above ten years or so will have no

choice but be forced off the road unless modification can be done to the engines of the cars. Alternatively, the Government can levy an environmental conservation tax on old cars on the road. This will again result in an early retirement of cars. On a more subtle note, the Government may make it compulsory for more frequent periodic mechanical checks by RMIV (Jabatan Pengangkutan Jalan) on old vehicles. The desire to avoid such inconveniences may encourage a higher replacement rate. Similarly, a penalty can be imposed on the use of old cars. This can be in the form of higher road tax and higher insurance premium for such cars. However, for these measures to be effective, the penalty must be sufficiently high. Monetary policy can also be utilised to increase the demand for new or newer cars. A more stringent procedure in vetting loan application to finance the purchase of old cars, couple with a higher interest rate on such loans and a shorter repayment period will have some impact on replacement demand.

Nevertheless, the Government has so far been lenient in introducing such legislations. This is probably due to the need to consider the plight of such car owners. They are likely to be in the low-income group and thus do not possess the means to buy newer cars. They will have to bear the full brunt if such legislations were made. As such, the Government has to come out with an institutional system for the replacement of motor-vehicles. Measures may have to be taken to keep prices of new cars low and trade-in values of old used cars sufficiently high to encourage replacement demand. Much propaganda has been given

TABLE 5.4 : AGE PROFILE OF PASSENGER VEHICLES ON MALAYSIA

Total registration at end of 1993	2299464 vehicles
New registration between 1989-93 (up to 5 years old)	558933 vehicles (24.3 %)
New registration between 1984-88 (5 - 10 years old)	293415 vehicles (12.8 %)
Total registration at the end of 1983 (more than 10 years old)	1447116 vehicles (62.9 %)

* from 1982 - 1992, there were 27945 cancellations of motor-vehicle registrations

Source: Transport Statistics, Ministry of Transport, M'sia 1994

to the concept of recycling. So, it is possible that the Government or private sector be encouraged to look into the technicality and viability of recycling motor-vehicle parts. This will contribute to both higher prices for trade-ins as well as lower prices of new cars. The fact is that by creating more demand than possible by normal market expansion, plants can be worked at production capacity and the required scale capacity and this will ultimately lead to higher productivity and competivity of the local motor-vehicle industry. Through this, it may be possible to avoid the displacement of resources that comes with under-production. Table 5.5 provides an estimation of the replacement market in Malaysia. It has been found that the

average life span of a vehicle in Malaysia is 15.5 years and that 62.9 % of the cars on the road is more than 10 years old. In comparison, there is not any vehicle on the road that is older than 10 years in Japan while the average life-span of their vehicles is 4.5 years.

5.3 : Uncertainty arising from the National Car Project

Eversince the launch of the National Car Project, the existing assemblers and franchise holders have been thrown into a state of confusion. From the initial 1.3 cc car, PROTON has slowly but surely moved into the 1.5 cc and 1.6 cc class range leaving the assemblers the upmarket. The very recent launch of the PERDANA, the 2 litre model, adds to the uncertainty as to the future roles to be played by the existing assemblers and franchise holders. The very recent announcement that Malaysia will make its own van, one tonne truck and other heavy vehicles by the Prime Minister, Datuk Seri Dr. Mahathir Mohammad at the press conference after the signing of a Memorandum of Understanding for the development and manufacture of a made-in-Malaysia motorcycles, raises further uncertainty over the future of the franchise holders and assemblers. PROTON's joint-venture with Vietnam Transport and Communication Import and Export Corporation, Mitsubishi Motors Corporation (MMC) and Mitsubishi Corporation to undertake the manufacturing of motor-vehicles in Vietnam may be a mark to the

initial step in this direction. The initial product to be manufactured is a mini-bus similar to the Mitsubishi Delica Model with provisions to assemble cars, trucks and buses in the future. Moreover, the intention of the Government, as stated in the IMP, to reduce the number of assemblers and manufacturers to three further prevents existing non-PROTON players in the market from making any long-term investment commitments. In an economy, there are many observors at the side lines and the Government's manouver in the automobile industry may also cause some concern to potential foreign investors interested in entering the other industries.

5.4 : Loss of Government revenue

The greater the extent PROTON cars have succeeded in displacing the other makes of cars, the greater the forgone tax revenue to the Government of Malaysia. The excise duty on cars and the import duties on imported CKD kits contribute substantially to Government tax revenue. PROTON's assess to CKD kits at 13 % duty compared to the 42 % to be paid by other assemblers and franchise holders and the 50 % rebate on excise duty will definitely decrease Government's revenue especially when PROTON's production and sales volume are significant.

5.5 : Conclusion

In the early days, when foreign experts were asked for their opinion on the rationality in establishing an automobile industry in Malaysia, many of them said that Malaysia's population of seventeen million was incapable of sustaining such an industry. So far, they have been proven wrong. The National Car Project has been the pride of the nation. Over the past decade, PROTON cars have achieved excellance not only at the home front but also in the international market. Although the concept of variable cost pricing of export models may not be fully understood nor appealing to all, it is an economic rational strategy. And although there are controversial arguments over the protection given to the National Car, such protection is normally accorded to all infant industry. Even developed nations have adopted such strategy. What is more important is that the Project can contribute to the overall social, economic and national aspirations of the country.