CHAPTER II

GOVERNMENT'S IMPLEMENTATION POLICY

In March 1963, the Minister of Commerce and Industry gave the first indication of Government's intention to encourage the establishment of a motor vehicle assembly industry in Malaya in order to give further impetus to the industrilisation of the country. The announcement was based on a report by a Colombo Plan industrial expert, which stated, that the circumstances were favourable, for the establishment of a viable motor vehicle assembly industry, in Malaya.

Subsequently, with the impending formation of Malaysia at that time, the Malayan Government, in consultation with the State Government of Singapore decided on a co-ordinated policy for promoting sound and speedy development of the motor vehicle industry in Malaysia, starting with assembly and progressive manufacture of parts and components. Malaysia is already one of the most highly motorised nations in Asia. The demand for motor vehicles is increasing rapidly. With these considerations, applications for setting up such assembly plants were invited. Before a final decision on the applications could be made, there was a constitutional change leading to the separation of Singapore from Malaysia.

In view of the separation of Singapore it was necessary for the Malaysian Government to review its policy relating to the motor vehicle assembly industry. In order to assist the Government to reasses the position, the expert advice of an international firm of industrial consultants, ARTHUR D. LITTLE INC, was obtained. The report of the consultants confirms that it is possible for Malaysia to establish immediately a viable motor vehicle assembly industry including the progressive manufacture of parts and components.

Having regard to the urgent need of the country to intensify its industrial development programme and to provide the maximum employment opportunity to meet the employment target for 450,000 people under the First Malaysian Plan, the Government decided to proceed immediately with the encouragement of the industry in the country. The Government also felt that this industry will provide a great impetus to the expansion of a wide range of engineering and ancillary industries.

In formulating this development policy, the Government is guided by the following basic considerations :-

a) To keep the costs and the prices of vehicles assembled in Malaysia at the lowest possible level.

b) To encourage the use of parts and components that can be made efficiently and economically in Malaysia, thus obtaining progressive manufacture of motor vehicles.

c) To continue a free and competitive market in motor vehicles in the future, and to ensure, as far as possible, that interests of the existing distributors, would not be a free choice of the types and models, at the lowest possible price.

Before going on to explain the various incentives that the Government is willing to accord, in pursuant to the policy, to promote this industry, I would like it to be noted that the Government has prepared Schedules for the definitions of completely-knocked-down (CKD), semi-knocked-down (SKD) or medium-knocked-down (MKD), and completely-built-up (CBU) vehicles to be imported into Malaysia. The interpretation of these definitions rests with the Comptroller-General, Royal Customs and Excise, Malaysia.

However, in view of the early stage of development of the industry, exemption from the requirements of the aforesaid scheduled definitions may be granted by the Minister of Finance, Malaysia, if he is satisfied that local assembly of these parts or sub-assemblies would not be economical and/or technically justified.

In exceptional cases, if specially designed vehicles could not conform to the C.K.D., S.K.D./M.K.D. definitions set forth in the First and Second schedules, either for technical or economic reasons, it would be the importer's/assembler's responsibility to prove to the Minister of Finance, Malaysia, that the sub-assemblies or complete vehicles should be admitted under the relevant definition.

With a view to promoting the progressive manufacture of vehicle parts and components in Malaysia, the definitions in the schedules will be subject to periodic review and revision.

For the above purposes, a Joint Advisory Committee consisting of officials of the proper authorities of both the Central and State Governments concerned, a representative of assemblers and later, a representative of the manufacturers of car components and parts will be appointed to advise and make recommendations to the Minister of Finance, Malaysia.

Now we can go on to the incentives that the Government is offering for the promotion of the industry :-

Tariff Protection

The prospective import duty will be 30% ad valorem (a.v.) and 15% a.v. on imported C.B.U. and S.K.D. passenger cars respectively, and 30% a.v. and 20% a.v. respectively on imported C.B.U. and S.K.D. commercial vehicles subject to examination by the Tariff Advisory Board that such levels of tariff are appropriate. All C.K.D. parts will be allowed to be imported free of duty except for those parts that are locally manufactured presently, such as tyres, tubes and batteries. The import duties will be imposed on a date, to be decided by Government which will not be later than 18 months from the date of the notice i.e. February 24th, 1966. Provision will be made for the exemption from import duty on certain types of specialised motor vehicles. The specialised vehicles are those like fire-engines, ambulances, special vehicles used by, say, the National Electricity Board and Telecommunications Department, etc. which are not dealt with along commercial lines.

Import Licensing and Quantitive Restrictions

The Government will impose with immediate effect (February 24th 1966) licensing and quantitative restrictions on the import of all C.B.U. and S.K.D. vehicles. Quotas will be allocated on the basis of the importer's average proved imports into the states of Malaya during the years 1964 and 1965 and will be reviewed periodically. The quota for C.B.U. and S.K.D. vehicles will be as follows :-

Passenger vehicles	-	110%
Commercial vehicles	-	80%

C.K.D. vehicles will be allowed to be imported without any restrictions.

For example, the 1964 import of passenger cars amounted to 19,231 units and the 1965 imports amounted to 18,837 units, the average of those two figures is 19,034 units. That means the import quota for 1966 will be 110% of 19,034, which amounts to 20,937 (refer to Table 4).

For the purpose of quota restrictions the year would be divided into two 6 month periods. At the end of each quota period the restrictions would be reviewed, and any changes that are deemed necessary will be put into effect. What the trends would be, regarding quota restrictions, is very indefinite - all depends on the circumstances i.e. policy would be implemented on a trial and error basis. But it can safely be assumed that the quota would be gradually, if not radically, decreased.

To implement this quota restrictions all importers of motor vehicles would be required to obtain import licences (which would be issued free of charge). A nominal sum of $3.00 would be charged only for a replacement of a lost licence. Licences will have to be renewed annually.

This method of imposing quota on the 1964 and 1965 imports does not make concessions for firms which were newly established then, and which since then have made rapid progress in sales. This method would only be fair to long-standing firms which have gradual progress in sales. In other words, the new firms, though they have a greater capacity to handle sales are restricted because they were in a stage of infancy during the 1964 and 1965 periods.

However, new firms wanting to establish themselves as motor-car dealers would be allowed a certain quota, though they have no past records of their capacity. This would however have to be on arbitrary basis.

These import restrictions have the following purposes :

a) To make sure that hoarding is not practised. Local assembly of vehicles could very well mean higher costs of final product, especially if assembly is carried on a small scale, which would mean that it would be uneconomic. In such a case, dealers may still be desiring to import vehicles in C.B.U. or S.K.D. form. Such a state of affairs would be no encouragement for dealers to start local assembly. Connected to this is the fact that the consumers might be prejudiced against locally assembled vehicles. In such a state of affairs what could happen is that, the dealers could still import C.B.U. vehicles from the traditional exporters in large numbers, and sell these vehicles at a much higher mark-up. This could very well work out if consumers are more willing to pay higher prices for vehicles in which they have faith. Such a situation is detrimental to both the consumer and the industry, while a small handful of people gain at others' expense.

b) To act as an inducement for manufacturers and dealers to assemble locally. The general tendency is for imports of vehicles to increase year by year, both, as a result of population increase, and the rising standard of living, of the people of the nation. This increase in imports is illustrated in Table 4, and now, with the end of confrontation, the increase in imports could increase even further. With this quota restriction, the supply of motor vehicles to the public can be expected to fall short of demand, and the only way to meet local demands would be by assembling locally. And though there is no such indication at the moment, we can fairly expect the quota to decrease as time goes on, so that the compulsion to assemble locally would be even greater.

It must be pointed out here that quota restrictions will be based, not on the make of the vehicle, but rather on the firm dealing in motor vehicles. A firm like Wearne Brothers, which sells very many models, will be given a quota based on its total imports, so that the number of different makes it imports is left to the firm's own discretion, as long as its total imports, for the 6 month 'quota-period' does not exceed the quota.

Distributors and private individuals who wish to import, used motor vehicles, may be permitted to do so, subject to a licence being obtained from the Government. The number of used vehicles imported by or through distributors will be deducted from the respective quotas allocated to the distributors for their imports.

Quantitative restrictions will not be applied to certain types of specialised motor vehicles which will be specified in Customs Notices.

<u>Assembly Tax</u>

In order to stimulate the progressive manufacture and utilisation of local component parts, an assembly tax will be introduced. The proposed tax is designed as a progressive tax, to be applied at specific intervals, to those assemblers who fail to meet the Government's minimum requirements of local content, for both passenger and commercial vehicles. The percentage of local content that must be attained, and the period within which it should be attained, and the assembly tax applicable will be as follows :-

TABLE 5 (a)

PASSENGER CARS AND COMMERCIAL VEHICLES
OF LESS THAN 1 TON CARRYING CAPACITY

Percentage of Local Content that must be attained (1)	Maximum time permitted from the date of announcement (2)	Rate of Application of Tax (3)
8%	2 years	25%
12%	4 years	50%
16%	6 years	75%
20%	8 years	100%

(The rate of application of tax is cumulative to a maximum of 12% of vehicle value for passenger cars and 5% for commercial vehicles of less than one ton carrying capacity.)

TABLE 5 (b)

COMMERCIAL VEHICLES IN EXCESS OF
1 TON CARRYING CAPACITY.

Percentage of Local content that must be attained (1)	Maximum time permitted from the date of announcement (2)	Rate of Application of Tax (3)
17%	2 years	25%
21%	4 years	50%
24%	6 years	75%
28%	8 years	100%

(The rate of application of tax is cumulative to a maximum of 5% of vehicle value.)

As an illustration, if an assembler of passenger cars has not attained at least 8% local content (as defined a litter later) within 2 years from the date of this announcement (February 24th, 1966), he would then be liable to an assembly tax equal to 25% of the maximum 12% assembly tax. This would be equivalent to a 3% assembly tax on the value of the vehicle as defined below. Should the assembler fail to attain 12% local content within 4 years from the date of this announcement, he would then be liable to an assembly tax of 50% of the maximum 12%, or 6% of the value of the vehicle.

Here the question may be asked, as to why the local content is expected to be greater for commercial vehicles in excess of one ton, than for passenger cars and commercial vehicles of less than one ton carrying capacity. This is because the local content that can be added to heavy lorries has greater potentialities. For example, for a passenger car five tyres (plus spare) would cost, at about $35 each, about $175. Whereas, for a heavy lorry seven tyres would have to be used, each of which cost much more, summing up to around a $1,000. Again, the whole wooden or aluminium bodywork can be done locally. It is these items which increase the potential of local content in a commercial vehicle of more than one ton carrying capacity.

In order to understand properly the formulae set out for assembly tax imposition, we have to define certain terms, which otherwise might obscure comprehension of the mechanics.

Definition of Terms :

Local Contents :

The local content is measured by the 'deletion allowance' in C.K.D. and S.K.D. packs provided to the assembler by the basic manufacturer. The deletion allowance in, say, a C.K.D. pack would be those essential parts of the vehicle that are left out from the pack, so that locally made parts are substituted. For example a C.K.D. pack may be imported without tyres, tubes and batteries because these items are manufactured locally, and make up the 'local content'.

Value of Vehicle :

The value of a passenger car or commercial vehicle shall consist only of the following direct manufacturing costs :

i) Costs of raw materials and of semi-finished or finished articles delivered at the assembly plant;

ii) Costs of fuel, other utilities and materials necessary for manufacture delivered at the assembly plant;

iii) Wages and other workers' benefits for labour participating directly in the production of the vehicle.

Factory overheads, depreciation and general and administrative expenses are excluded.

Percentage of Local Content :

The percentage of local content is equal to the total deletion allowance divided by the total vehicle value as defined above. The percentage of local content will be calculated thus :

$$\frac{\text{Total value of deletion allowance}}{\text{Total value of vehicle}} \times 100$$

Preferential Rate of Ad Valorem Registration Fee :

An ad valorem registration fee (AVRF) has had to be paid, for every car imported and sold in this country all along. The fees have been at the following rates :

TABLE 6

A.V.R.F. RATES

	Commonwealth Origin	Non-Commonwealth Origin
Passenger cars	10%	25%
Commercial vehicles	Nil	15%

These rates still continue to be imposed, but in order to promote fair competition among assemblers of all makes of vehicles, and to encourage the utilization of local materials, parts and components that can be made efficiently and economically in Malaysia, the Government has decided to grant the preferential rate of AVRF to all locally assembled vehicles. This means that all locally assembled vehicles would be charged the AVRF at 10% for passenger cars and nil for commercial vehicles, regardless of origin of the parts and components. In respect of vehicles of non-Commonwealth origin (i.e. less than 50% Commonwealth content) they will be subject to the full rate of AVRF if they do not attain the minimum local content requirements within the period stipulated earlier.

All C.B.U. vehicles will continue to pay AVRF which is based on the c.i.f. values. Locally assembled vehicles will initially pay AVRF based on c.i.f. price of identical C.B.U. models. This basis will, however, be subject to review. Just as the quota restrictions, this basis of AVRF payment for locally assembled vehicles will be worked upon a trial and error method.

To sum up the case of the local assembled car or vehicle, it receives first of all, tariff protection up to a maximum of 30%. Added to this protection in the form of quota restriction on C.B.U. and S.K.D. vehicles imported. It only has to pay assembly tax if it fails to reach the Government's local content requirement within the stipulated time. Lastly, while it is subject to AVRF, it is given preferential treatment.

Pioneer status is not granted by the Government to the assembly industry. There are two main reasons for this. When the assembly industry was first envisaged in co-ordination with the Government of Singapore, Ford Motors had already been in the industry for about 36 years without such Government concession. Therefore to grant such a status then, would have been unfair to Ford's. Secondly, the assembly industry is not a manufacturing industry, and as such the granting of pioneer status is not warranted.

The Government has also stipulated that assemblers should use local parts and components as, and when they are available, subject to the quality being acceptable. The Government is prepared to grant pioneer status (and in fact has done so, in principle) and to introduce the necessary tariff protection for the local manufacture of parts and components, whenever this may be done economically. The Government would like to see in particular the early manufacture of the following items : trimming materials, seat frames, leaf and coil springs, silencers and exhaust pipes, radiators and core, fan belts, shock absorbers, sealing materials, brake lining and parts, safety glass, spark plugs, canvas hoods and bumper bars.

The assemblers are at liberty to select sites of their own choice within the States of Malaya, for the setting up of their plants. In fact there is already one truck assembly plant in Petaling Jaya which assembles Mercedez Benz trucks for Cycle and Carriage Co. Ltd.. There have been indications of site development in Batu Tiga which has a direct linkage by road and rail to Port Swettenham and about ten miles away from it.

The number of assembly plants that may be established may be limited by the Government, if necessary. Assemblers, however, may group themselves into a consortium if they so desire; i.e. a few dealers of different makes could get together and open a single assembly plant, where their various models of vehicles could be assembled under the same roof.

On the other hand, vehicles may also be assembled by contract assemblers. In fact, there is already an Australian firm which is going to undertake contract assembly in Malaysia, but the name of this firm is still a Government secret!

Subject to the provisions of the existing customs legislation, assembly plants may be treated as customs bonded areas. Customs officials will be stationed at these bonded areas, and the cost of maintaining them shall be borne by the assembly plants. Bonded areas may also be considered for C.B.U. vehicles.

The Borneo States are being consulted with a view to the adaption by all States of Malaysia of a uniform policy.