Boosting the Auto Industry

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Sequence

• Recent policy research on the sector
• Sector Highlights
• Policy Prescriptions
Recent policy work done on Auto-Sector
Key Policy Studies Contributing to Evidence

• Regional Study on the Auto Sector, IDEAS
  – Faisal Bari, Nazish Afraz, Nadia Mukhtar, Usman Khan, Turab Hussain

• Engagement with Punjab under CPEC: Proposed framework; IGC
  – Nazish Afraz, Hassan Khawar, Ijaz Nabi

• Policy Reforms for Punjab’s Priority Business Sectors, BERP
  – Usman Khan, Nazish Afraz & Hina Sheikh

• Assessment of the Lahore Auto & Auto-parts Cluster
  – Cluster Development Initiatives, GoPunjab and UNIDO
Sector Highlights
Contribution by the sector to the National Economy

- 16% of the national manufacturing sector
  - US$ 6Bn per annum in Value
- Direct employment of over 200,000
- Over two million annual production
  - 88% are two wheelers
- Auto parts enjoy a derived demand
  - Over 2,000 manufacturers specializing in range of production technologies
  - Exports of over US$15 million, potential
SWOT of the Auto & Auto-parts Sector (Lahore cluster)

**Strengths:**
- Strong 2-wheeler industry
- Lower labour cost than in China
- Strategic geographical position on the new silk road between east Asia and the Arabian Sea (CPEC)
- Strong government focus on automotive cluster development

**Opportunities:**
- Growing population and growing market
- Despite image problems, Pakistan/ Lahore are on the right way to attract direct investment:
  - Planning-phase: Hyundai, BAIC
  - Potentially: Renault, VW, Audi
  - Using competence in low to medium volumes as USP for export
  - Create visibility for local competence
  - Example: “Small green goods mover designed and manufactured in Lahore”

**Weaknesses:**
- Auto parts suppliers focus on manufacturing assigned parts
- No active role in increasing local content
- Competence gap in reverse engineering limiting local content growth
- Challenging process for importing raw-materials
- Low competency manufacturing: Low value added and cost pressure
- Protective industry policy model is not conducive for the growth of automotive sector

**Threats:**
- Volatile market conditions
- Local supplier’s potential at risk due to international competitors and international standards
- Not creating a balance between Mexican Vs Brazilian model

[Diagram showing SWOT analysis]
Factors that make Auto Sector a Promising Opportunity

• Production in automotive is organized in Global Value Chains
  – Lighter and more expensive parts sourced from competitive locations
  – Heavier parts sourced from locations closer to assembly lines

• Geographic proximity with China – large automotive manufacturer
  – Significant investment in technology and R&D, domestic demand on rise
  – FTA-2; in 313 product lines – over $20 billion in imports of auto-parts

• CPEC infrastructure offers connectivity to large Chinese market

• Auto parts from Pakistan already being exported to developed markets

• Large technology and employment (E.g. motorbikes) spillover impacts
4-Dimensional Analysis

1. Economic Benefit

- Domestic demand of vehicles increasing (long-term trend)
- Investors coming in post incentives offered in New Auto Policy 2016-21
- Exports of auto parts can increase
- Pakistan can potentially manufacture for Chinese GVCs
- New entrants likely to increase competition
- Potential JVs to enhance integration opportunities
2. Social Inclusiveness
   - Over 0.5 million direct and indirect employment
   - Globally, auto sector has the second highest employment multipliers
   - Current Human Capital suited for Tier 2/3 Firms

3. Innovation
   - Pakistan is still at basic level, globally one of the most innovative
   - China GVC offers significant opportunities

4. Environmental Sustainability
   - Generally considered a clean manufacturing process
   - Environmental impact in use varies, Pakistan has no national standards
   - Manufacturers usually follow international standards
Business Environment Issues

Source: Field data collected for BERF Report (Auto-part manufacturers based in Lahore)
Focusing on D/M Capacity is the Key

Today’s Dies / Molds competence mainly in level I and II
Further localization of Auto parts will require Dies / Molds competence level III
Product innovation in Auto parts will require Dies / Molds competence level IV

<table>
<thead>
<tr>
<th>Automotive Supplier Industry</th>
<th>Competence levels</th>
<th>Local Dies / Molds Industry</th>
</tr>
</thead>
<tbody>
<tr>
<td>Creating new products</td>
<td>IV</td>
<td>Entire Dies / Molds process in-house</td>
</tr>
<tr>
<td>Replacing imports with local content</td>
<td>III</td>
<td>Entire Dies / Molds process in-house</td>
</tr>
<tr>
<td>Auto parts manufacturing international standards</td>
<td>II</td>
<td>Partly manufacturing of Dies / Molds</td>
</tr>
<tr>
<td>Auto parts manufacturing local standards</td>
<td>I</td>
<td>Partly manufacturing of Dies / Molds</td>
</tr>
</tbody>
</table>

- Rubber
- Casting
- Plastic
- Functional
- Sheet metal
- E/E
- Sub-Assembly
- Functional
Policy Prescriptions
Policy Outcomes

- Facilitate manufacturing to gain from Pak-China FTA
- Whole VC of D/M must be supported at the cluster level
- Explore JVs and market access under CPEC to integrate with China’s GVC
- Increase emphasis on human capital development
  - Upgrade higher education and TVET
  - Provide incentives and institutions that support R&D
- Incentivize technology acquisition for innovation, especially with China
- Consistent and long-term taxation policy – Monitoring of policy incentives
- Current Auto Policy offers no incentives for R&D and Technology Acq.
  - Advocate for revision – incentivize innovation
Policy Outcomes

• Need for phased national auto standards and a regulatory body
  – To upgrade quality and ensure access to competitive markets
• Regulatory framework required for periodic assessment of competition
  – To avoid monopolistic behaviors
• Public-private dialogue needs to be strengthened, more inclusive
• Government should support access to information
  – Markets, technology and partnerships
• Explore possibilities of outward investments in Motorbikes & Tractors
• Enhancing credit to SMEs
Thank you