Policy Brief on Automobile Sector

Overview of Policy Framework

The automobile sector today operates within the rubric of several policies, frameworks and regulations: the Industrial Policy 2011; the Trade Policy Framework 2012-15; the Finance Acts which modify the fiscal and tariff regime backed by the Statutory Regulatory Orders (SROs) and the Customs General Orders (CGOs); the Auto Industry Development Programme (AIDP) 2008-12; the Tariff Based Scheme (TBS); Pakistan Standards; and the National Environmental Quality Standards (NEQS).

Since 1987, policies were devised to place the industry in Pakistan on the path of 'indigenisation'. It was believed that once complete indigenisation is achieved, prices will come down automatically. To achieve indigenisation, the import of vehicles remained banned till 2000 under the trade regime. However, import of used and reconditioned vehicles was liberalised under gift, personal baggage schemes and transfer of residence (TR). TR scheme allowed the import of cars without any age limit on them till 2006 when the import of cars under the scheme was first restricted to three and subsequently to five years, making the policy more restrictive.

Industrial Policy 2011 shows a tendency towards liberalisation in automobile sector and requires government to relax country-specific licensee for manufacturers, however it also provides 5 year window for maximum indigenisation of motor vehicles and ensure implementation of tariff-based system.

The first Auto Industry Development Programme (AIDP) 2008-12 outlined several conditions for new entrants including a minimum production levels achieved by the firms in cars, trucks, buses and agriculture tractors, a clear intent to produce parts locally, and proof of land ownership.

On 1st July 2006, **to comply with WTO rule, the Deletion Programme for the automotive industry was replaced by the Tariff Based Scheme**. During 2007-12, tariff on 800cc and 800cc-1000cc has increased from 55 per cent to 57 per cent and 65 per cent to 68 per cent respectively. However, 1,000cc-1,500cc is the only category in which Effective Rate of Protection fell from 73 per cent to 68 per cent over the same time period.

These policy developments suggest that the overall thrust of the framework is still on indigenisation while offering protection to existing local manufacturers. Additionally, the restrictions on new entrants coupled with an increasing level of tariffs reduce the level of competition in the industry with the cost being borne by the consumers.

Consequences of Protective Policies

Export of cars by Pakistani assemblers is almost non-existent. There are two main reasons. First, franchise agreements with Japanese principals are the main stumbling blocks. Presumably, according to the agreements, the prerogative to allocate the markets where Pakistani assemblers can export their products rests with the Japanese. Apparently, there are also price floors imposed on local manufacturers by their principals.

Second, **protection has created anti export bias**. The assemblers are making profit by selling in the local market, therefore they do not need to export which may be quite competitive and for that they might have to invest and adopt or develop new technology.

Moreover, **there is evidence of lack of innovation in terms of changes in models, quick availability, fuel efficiency, below par safety standards, increase in user friendliness and cost cutting.** Quality of locally produced vehicle is much below par and is not comparable at all with those produced in international market.

A key indicator of the lack of competition is that the **consumers pay high prices as compared to world prices of comparable vehicles,** and also bear the cost in terms of long delays between full payment of the price of vehicle and its actual delivery. The position has relatively improved owing to competition from imports of used cars after relaxation of import restrictions.

Protectionism has resulted in significant entry barriers and allows the existing local firms to dominate the market.

Principles of New Auto Mobile Policy

Automobile industry with present manifestation is not viable. The vulnerability is essentially the lack of domestic and foreign competition in the industry. Thus, to liberalise the automobile sector and to provide level playing field to existing and new entrants, following principles are proposed as building blocks of a new automobile policy.

Parameter	Previous Policies	New Policy
Tariff Structure	Previously, Deletion Programme and now the Tariff Based System were essentially designed to promote and protect local industry.	**New policy should bring down the tariff structure and effective rate of protection** on all segments of automobile without discriminating on the basis of engine capacity.
Impact on Jobs	Previous policies on automobile have used employment creation in auto car industry as a major rationale for protective measures.	**New policy should focus on job creation in sub-sectors such as auto-parts** and motorcycles which in any case constitutes 96 per cent of total job market. These sub-sectors, particularly the auto-parts are likely to benefit from liberalised imports.
Competitiveness	Previous policies have relied on import substitution measures for enhancement of competitiveness in the industry.	**New policy should focus on decreasing import restrictions to encourage competitiveness in the local market.**
Non -Tariff Barriers	Age limit and depreciation allowance have been used by policy makers to create non-tariff barriers.	**New policy should leave the decision to the importers and consumers in terms of valuation** of an imported car while removing age limits and depreciation allowance.
Franchise Agreements	Previous policies have an in-built anti-export bias as key assemblers are operating under license/franchise from respective Japanese manufacturers that restricts their exports only to limited geographical location and also impose price floors on products made in Pakistan.	**New policy should encourage investment from firms from other countries** without any restrictions on exports and price floors on local counterpart firms/franchisee.