



NATIONAL ASSOCIATION OF AUTOMOBILE MANUFACTURERS OF SOUTH AFRICA

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N4/2
2nd November, 2017

The Commissioner
Competition Commission
Dti Campus
Sunnyside
Pretoria

For attention: Mr Mziwodumo
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Dear Commissioner

NAAMSA SUBMISSION IN RESPONSE TO THE DRAFT CODE OF CONDUCT FOR COMPETITION IN THE SOUTH AFRICAN AUTOMOTIVE INDUSTRY – VEHICLE REPAIR AND SERVICING AND PARTS SUPPLY

1. Background and introductory comment

In terms of government notice 1011 published in government gazette number 41132 dated 22nd September, 2017 – the Competition Commission invited interested parties to provide comment on a Draft Code of Conduct for competition in the South African Automotive Industry.

The Draft Code comprises a voluntary Code of Conduct aimed at promoting competition in the South African Automotive Industry with particular focus on vehicle repairs and servicing, including motor body repairs, and the supply and distribution of aftermarket parts in South Africa.

At the outset, it is important to confirm that the National Association of Automobile Manufacturers of South Africa (NAAMSA), as an Association, has no involvement in or influence over the strategies and policies of vehicle manufacturers, importers and distributors in matters relating to the supply and distribution of aftermarket parts and the repair or servicing of motor vehicles in South Africa.

NAAMSA represents the collective, **non-competitive** interests of the new motor vehicle manufacturing and importing industry in South Africa. Membership comprises 22 companies involved in the production of cars and commercial vehicles and 21 companies involved in the importation and distribution of new motor vehicles in South Africa. The Association attends to matters which aim to promote the interests of the broader South African Automotive Industry and its members in particular. As a matter of longstanding policy, NAAMSA does not have any involvement in issues of a competitive nature and these include, amongst others, marketing, sales and pricing policies as well as automotive servicing and aftermarket policies. NAAMSA has introduced a set of competition law compliance guidelines to govern deliberations at NAAMSA meetings which specifically preclude conduct or exchange of views, information and/or the implementation of agreements and/or practices that may lessen competition.

In the circumstances, NAAMSA is only in a position to provide and coordinate a generic industry response on behalf of NAAMSA members dealing with the principle and substance of certain aspects of the Draft Code of Conduct. However, individual NAAMSA member companies will respond to the Competition Commission, in their individual capacity, providing their own reaction and views including comment on matters of a competitive nature.

2. Preliminary comment on the rationale and basis underpinning the proposed Code of Conduct

It is NAAMSA's understanding that the intent of the Competition authorities, in terms of the Code, is to 'address anti-competitive behaviour within the industry' and 'to promote industry transformation to foster inclusive growth. NAAMSA believes this should be considered against the backdrop of challenging market conditions and, in the case of transformation, recent developments relating to the empowerment initiatives in the industry.

Furthermore, we are concerned that the imposition of any such outcomes as set out in the Draft Code will –

- be counterproductive to the development of the economy;
- result in inefficiencies;
- fail to provide consumers with “competitive prices” without entirely compromising the product safety standards to which consumers are entitled;
- be destructive of the promotion of employment and is likely to result in the extensive loss of jobs within the automotive sector;
- instead of advancing the “social and economic welfare” of South Africans, in all likelihood result in the discontinuation of operations and/or opportunities which have the potential to achieve this very outcome;
- curtail the current expansion opportunities which are realised by OEMs within world markets as opposed to securing the expansion of such opportunities;
- impact directly upon the opportunities currently enjoyed by small and medium-sized enterprises within the context of the contributions which they make to the downstream value chain; and
- curtail the existing ownership opportunities which OEMs currently pursue in relation to historically disadvantaged persons.

On the first point, and stated intent, we request that the Competition authorities take into account the intensely competitive nature of the industry as well as the safety of consumers and the rights of consumers to safety and quality of service.

The following statistics – as at the beginning of 2017 – serve to illustrate the highly competitive nature of the South African Automotive Industry and outlines the number of brands and model derivatives, in respect of new motor vehicles, available to consumers –

<u>Segment</u>	<u>Brands</u>	<u>Model derivatives</u>
New cars	55	3 458
Light commercials	26	739
Medium commercials	17	185
Heavy commercials	12	132
Extra heavy commercials	11	540
Buses	9	55

During the course of 2017, five brands withdrew from the South African market including – Chery, Citroën, Chrysler, General Motors/Chevrolet and Dodge. Consequently, the number of brands in the

new car segment has reduced to 50, an indication of the current difficult trading conditions already faced by industry participants.

In general terms, total domestic new vehicle sales in South Africa over the past five years have ranged from **550 000 to 650 000** per annum with most of these vehicles sold and serviced through franchise dealers. There were an estimated **2 078** dealerships in South Africa at the beginning of 2017 – currently down to about **2 000** dealerships.

These numbers should also be seen in the context of South Africa’s vehicle population which according to Natis – as at mid-2017 – were as follows –

Motor cars	7 641 784
Minibuses	295 272
Buses	67 897
Medium trucks	2 573 143
Heavy trucks	392 038
Other vehicles	<u>241 365</u>
Total vehicles	11 211 499

The point is that all these vehicles will periodically have to be serviced and/or repaired and such activities will be undertaken by franchisees as well as independent workshops. A significant proportion of the vehicles in South Africa’s vehicle parc, about 75%, comprises vehicles which are not subject to the OEM/Importer’s warranty, service or maintenance plan. Given the size of South Africa’s vehicle parc, there is therefore an adequate number of vehicles to be serviced/repaired at any one time. There is no shortage of opportunity for any automotive business to participate in the aftermarket vehicle servicing and repairs, subject to the realities of the marketplace and the prevailing operating environment.

The figures therefore confirm the intensely competitive nature of the industry and the size of the market for vehicle repairs, servicing, replacement parts as well as motor body repairs where vehicles have been involved in accidents. The reduction in the number of new car brands from 55 down to 50 has also resulted in a reduction of the number of dealerships by approximately 50. In addition, established manufacturers/importers have implemented dealer rationalisation programmes and ownership consolidation projects which have contributed to a further reduction in the number of dealerships by about 20.

Most new motor vehicles sold in South Africa come with a warranty ranging from 3 to 7 years. Many vehicles sold also enjoy the benefit of maintenance or servicing plans. The entire franchise dealer infrastructure – comprising an estimated 2 000 dealers – has evolved over decades based principally on international norms and standards and the competitive strategies of automotive companies. **Importantly**, the relationship between vehicle manufacturers and their dealers, service providers and motor body repair services is governed by formal, legally binding agreements. The aftersales servicing and vehicle repair operations differ markedly between the various manufacturers and importers. As a consequence of the vastly different strategic models and policies of automotive companies – there is no ‘one size fits all’ model applicable in the industry in respect of vehicle servicing, repairs and parts supply.

On the second point, there may be perceptions that the Automotive Industry in South Africa is a closed system that deliberately excludes ‘competitors’ particularly small medium enterprises – in the automotive aftermarket, repair, servicing and parts supply activities.

Any such perceptions have no basis in reality.

The only restrictions to participation in franchise dealer operations (including vehicle repair and servicing) comprise access to capital, appropriate skills, technology and economic viability limitations in the form of number of dealerships/servicing outlets per area. These represent market and commercial realities and should not be construed as anti-competitive. Anyone can participate in the industry on the same terms and conditions.

Applications for dealerships that meet capital investment requirements, retail and servicing experience including compliance with technology and skills standards and that do not exceed a realistic number of competitors in a particular area – will be considered by automotive principals on their respective merits. In the nature of a competitive trading environment, vehicle manufacturers/importers periodically appoint new dealers and/or terminate non-performing dealers. Currently, the trend in the industry is towards a reduction in the number of dealers.

Participation in the industry is therefore open to suitably qualified businesses subject to legitimate commercial and economic factors. The advent of new entrants into the industry over the past 20 years attests to this.

Moreover, considering the Draft Code as a package – it represents an additional transformation set of requirements over and above existing black economic empowerment legislation. It does not appear to take account of the very substantial contribution by automotive companies, individually, and the industry collectively (through the industry's Venture Capital Fund), to advance and develop black businesses in the aftermarket servicing and repair sector. **The contribution by the seven major OEMs to broad based black economic empowerment is currently being surveyed and the results will be shared with the Competition authorities as soon as this information is available from all seven major OEM's.** It is noteworthy that the planned R3.5 billion transformation fund will allocate capital to develop black ownership in the Automotive Industry supply chain and vehicle dealership network.

NAAMSA therefore questions the notion of 'the existence of anti-competitive behaviour within the Automotive Industry in South Africa' and the lack of transformation and scope to participate in industry operations. NAAMSA also questions the legal basis and approach adopted by the Competition authorities in regard to the process of proposing the introduction of a voluntary Code of Conduct. Moreover, NAAMSA remains of the view that current legislation relating to Competition, transformation and consumer protection issues is adequate to deal with the challenges identified by the Commission.

3. Comment on the Draft Code of Conduct and issues of substance

The Draft Code includes far reaching proposals, many of which are impractical, unworkable and possibly not legal. As a package, the proposals – if implemented – have the potential to undermine and dismantle the highly competitive and efficient dealer franchise system in the South African Automotive Industry. In summary, some of the key aspects and objectives covered by the Draft Code include –

- Facilitating small, independent and historically disadvantaged service providers to undertake repair, servicing and maintenance work in respect of vehicles under warranty;
- Enabling small, historically disadvantaged body repairers to undertake auto body repairs in respect of vehicles under warranty;
- Promoting ownership of dealerships by small, historically disadvantaged individuals/businesses through the removal of 'onerous requirements';
- Providing independent third-party service providers access to OEM/importers' safety and technical specifications of parts to enable them to undertake repairs;
- Providing third party service and repair businesses with access to equipment and tools through leasing and renting options coupled with the requirement to train the repair/servicing businesses to undertake the work;
- Allowing equal – matching parts, approved by the SA Bureau of Standards, to be used in repairs without loss of warranty;
- Enhancing consumer awareness of the costs involved in the purchase of a motor vehicle including an option to purchase a new vehicle without maintenance plan, service plan and extended warranty and permitting the use of any repairer during both the warranty and extended warranty period;
- Apparently expecting OEMs/importers to fund the costs associated with most of the proposals.

The proposals by the Competition Commission in their current form would undermine the viability of franchise dealers and OEMs and particularly the aftermarket vehicle servicing and repair sectors and would jeopardise the viability and sustainability of the automotive value chain – with potentially far

reaching negative consequences on employment in the dealer sales and servicing operations which currently provides about 80 000 direct jobs in the industry.

An immediate negative consequence of the proposed Code of Conduct involves investor sentiment and the reality that established businesses (as well as potential new entrants) in the sector will place on hold any expansion decisions pending the outcome of the current consultative process. The adverse impact of a 'wait and see attitude' should not be underestimated.

These developments take place in the context of an operational environment in the Automotive Industry in South Africa to date which has provided a high degree of certainty and stability. This in turn has resulted in substantial investment in the auto industry's aftermarket servicing, repair and parts supply infrastructure. It has also contributed significantly to employment creation and retention, as well as the growth and development of the sector – despite the low economic growth in South Africa.

NAAMSA is justifiably concerned that irreparable harm may be caused to an industry which has become the successful cornerstone of growth and development in South Africa. Automotive companies deem it imperative to protect the investments of existing and future participants in the automotive value chain and that it is therefore critical to end up with a Code which is realistic and practical. In this regard, on 8th June, 2017 NAAMSA made a submission to the Competition Commission on a possible voluntary Code of Conduct based on the Russian FAS Code of Conduct with added elements from the European Union and Australian Codes. In NAAMSA's submission, it was pointed out that in a complex, highly competitive industry, characterised by substantial investment by government, foreign and local businesses, supporting international export markets and tens of thousands of jobs – the NAAMSA proposed Code was aimed at safeguarding a sustainable future for the industry whilst, at the same time, addressing the objectives which the Commission envisaged.

The unrestricted and/or facilitated access of new dealers and of independent service providers to in-warranty repair maintenance work, technical specifications, data and parts, equipment, tooling and training (at the apparent costs to the OEM/Importer) takes no cognisance of factors which include the following considerations –

- The OEM/Importer have made extensive investments in existing facilities, technologies, tooling and technical information.
- The maintenance of the standards and quality of work necessary to ensure customer safety and the protection of customer investments.
- The global imposition by brand owners of dealer standards necessary to secure access to the rights of the OEM/Importer to manufacture/import vehicles.
- The stringent requirements of the manufacturers, internationally and locally, of vehicles in regard to all interactions undertaken in respect of repair and maintenance whilst warranty/maintenance plans are operative, so as to ensure that operational safety is not compromised.
- The obligations of the OEMs/Importers in relation to guarantees issued in regard to the standard of warranty repairs and their obligations to meet the costs of such repairs.
- The extensive costs associated with purchasing of tooling for "rental/lease".
- The requirements imposed by brand owners upon OEM/Importer and dealers to ensure that the reputation of the brand is protected and the safety of the consumer is not compromised.
- The access to technical specifications which remain the intellectual property of the brand owner, is dependent upon the payment of applicable fees which remain an essential requirement of the brand owner to cover the costs of compiling the technical information and data and making it available in an accessible format to OEMs/Dealerships.

- That parts specifications remain proprietary information which may not be disclosed by the intellectual property owner.
- That automotive companies have invested substantially in parts development and retain the full right regarding the control and use of specifications, which equally remains an internationally accepted form of protecting intellectual property.
- That all existing dealers are obliged to approach financial service providers to the extent that finance and leasing options are required.
- That OEMs/Importers do not and will not cover any failures attributable to the use of non-genuine parts.
- That service and maintenance plans form part of the product offering to customers based on their needs and requirements and that the ability to offer service and maintenance plans remains subject to conditions imposed by the OEMs/brand owners including but not limited to the standards, equipment, facilities, and systems applied by the dealerships none which are capable of being separated and dealt with in isolation from the sale of the vehicle.
- That automotive financing institutions would be negatively affected by the impact on vehicle trade and retail values if vehicles are not repaired, serviced and maintained according to manufacturers' specifications.

In summary –

- NAAMSA is concerned that the content of the Draft Code will seriously and fundamentally compromise current and future investments in the country as it undermines the way many global automotive players implement their strategies. The legality of the Draft Code is also questionable as it appears to ignore fundamental South African legal principles such as –
 - i) the sanctity of contract,
 - ii) the causal nexus between manufacturers/importers and their product liability,
 - iii) intellectual proprietary rights and associated investments therein,

and also appears to conflict with other legislation such as the Consumer Protection Act as well as the Broad-based Black Economic Empowerment Act.
- Allied to the above, the Draft Code appears to ignore the interests of the consumer. Vehicles are highly complex, high technology products requiring vast investment in development and engineering in order to ensure safety to the user and longevity due to the cost of the item. Safety and quality standards can never be compromised.

As it stands, the Draft Code, in its present form, cannot be supported. Manufacturers or importers would not in good faith be able to sign a document that offers no protection for the vast investments made in South Africa, that results in negative effects on jobs in the industry and introduces significant risks to safety of consumers and, importantly, which threatens the viability of existing, legitimate servicing and repair activities.

4. Conclusions and Recommendations

For the reasons outlined in this submission NAAMSA cannot support to the Draft voluntary Code of Conduct in its present form.

NAAMSA recommends –

- (i) That, for the reasons outlined, the Draft voluntary Code of Conduct by the Competition Commission be withdrawn in its entirety;
- (ii) That the authorities should revisit NAAMSA's earlier proposal for a voluntary Code of Conduct sent to the Commission under cover of a letter dated 8th June, 2017 which adequately addresses internationally accepted practices, the legitimate interests of consumers and the changes envisaged by the Commission. NAAMSA proposes this should be done in conjunction with all relevant regulatory authorities in an effort to determine not only the legality of any such voluntary Code of Conduct but also the terms of such a Code and under whose auspices such a Code should be published;
- (iii) That transformation and black economic empowerment remain a function of empowerment initiatives by automotive companies, individually, and, collectively, through the Venture Capital Fund;
- (iv) That in view of the far reaching and potentially negative consequences for the industry, the substance of any revised Code be subjected to a detailed socio-economic-employment impact study;
- (v) That in view of the auto industry developmental implications, the Ministry and Department of Trade and Industry be required to participate in the process;
- (vi) That in light of the interests of consumers and consumer safety, the Consumer Commission be consulted on all aspects of any possible future Code of Conduct; and
- (vii) That in light of the above, the Commission **extends its deadline** in which to submit responses to the Draft Code of Conduct **by, at least, a further thirty (30) days** to enable NAAMSA and its members to meaningfully engage with the Commission to debate the issues referred to in this response as well as to enable NAAMSA and its members to respond in further detail to the Draft Code of Conduct after the suggested engagements.

In respect of item (vii) above, industry and individual member/s representatives are available to meet with the Competition Commission to elaborate on the industry submission and requirements and to engage in a constructive manner.

Yours Sincerely

NMW VERMEULEN
DIRECTOR