tcf services
DELIVERING THE FUTURE

The Australian Automotive Industry Advisor

Vol.2, No.1 - April 2003

Editorial Comment

• *More choice ultimately leading to higher industry costs*

With new motor vehicle sales in 2002 at a fever pitch - industry figures indicate they were up 6.7% on 2001, to an all time record of 824,309 vehicles - continued low interest rates together with solid economic fundamentals suggest 2003 should witness another firm year for new vehicle sales, with most major manufacturers forecasting something in the range of 800,000 to 815,000 units.

Whilst this is providing strong cash flow for motor vehicle manufacturers - with Holden at the top of the list again at 178,000 vehicles - progressive tariff cuts are also encouraging a boom in the number of models being offered to the Australian motoring public, particularly from European marques.

Whilst the proliferation of models can be argued as being good for boosting consumer choice and helping drive sales volume, higher costs in supporting multiple spare parts and logistics systems are also undermining the traditional economics of the industry.

Faced with the virtual smorgasbord of vehicles, consumers have also become more discerning, forcing fierce competition on the car lots, and putting pressure on gross margins and dealership profitability to the point where new vehicle sales now contribute very little in terms of net profit across total dealership sales turnover. The margins in used car sales are not that much better.

The saviour of the industry has been in the margins made via the provision of Finance and Insurance, and within the replacement parts and vehicle maintenance/service departments. This is just as well, for with further tariff cuts due to kick-in within the next few years following the Government's decision on the 2005-2015 assistance environment, the situation is unlikely to improve.

Local manufacturers are destined to face an increasing inflow of differentiated brands and vehicle types cutting into aggregate vehicle shares, thus reducing the opportunity to minimise costs on long production runs.

ACIS under a cloud in new Free Trade Agreement

The outbreak of hostilities in Iraq is having a subdued effect on prospects for the US-Australia Free Trade Agreement (FTA), including opportunities for Australia's automotive producers in the more open trading environment that is potentially, just around the corner in 2005.

In the midst of what appears to be a campaign by the US to steal Australian wheat exports to Iraq, negotiations began in earnest last month in Canberra with both sides promising they would pursue a wide-ranging and comprehensive set of objectives in FTA negotiations - which for industrial goods means, "the elimination of tariffs and other barriers to trade."

The problem for Australian automobile and related component producers is that in the Government's most recent decision on post-2005 assistance, both a Tariff and ACIS entitlements made up key on-going components of the total package. So whilst it might be of less concern to some that under a new FTA import tariffs will go somewhat quicker than first expected, there will be widespread concern at the prospect of ACIS entitlements being suspended for investments/product principally destined for the USA.

In Wellington 9 March to celebrate the 20th anniversary of the ANZCERTA free trade deal with New Zealand, Prime Minister Howard toasted the agreement for its innovation, and said it was the model to which all future trade agreements should be moulded. ANZCERTA's implementation, of course, saw the immediate death of all tariffs and subsidies in trans-Tasman trade.

Few within the Canberra bureaucracy are willing to talk about the prospect of ACIS entitlements being negotiated away as part of a broad ranging FTA with the Americans, however, foriegn authorities have not held back. At a recent Canberra briefing on approaches to the new trade deal, the US Embassy's Economic Counsellor, Michael Delany, thought the simple achievement of a full elimination of automotive tariffs between the two countries after 2005 might be a sufficient enough goal, without entertaining the need to address the future of ACIS.

This is certainly an issue where our advice is - watch this space!

Report coming on insights into vendor tooling

Vendor tooling continues to be a sore point amongst many participants, with AusIndustry audits and customer service visits revealing some 'double-dipping' by those that build the tool and sell it up the supply chain to the ultimate owners, who also claim the tool as production P&E against their returns.

In essence, the builders/suppliers of the tool (unless for own use) are building a 'stock item', with a view to eventually selling, or transferring ownership to a third party (after successful OTS or PPAP signoff), even though the tool usually remains on their premises for the production of parts.

Until the tool is paid for in full, or under progress payments, the builders/suppliers of the tool are of the opinion that it is theirs to claim as eligible P&E. Such a tool, would not appear to meet the definition of approved plant and equipment under Section 6 of the Act or S13E of the regulations as a normal production asset to be claimed by the builder or supplier of the tool. The approach would be no different to the treatment afforded to the manufacture and supply of a normal production part, given ACIS participants receive 5% (capped) of eligible sales of components, tools and services.

The Purchase Order/RFQ will indicate who the beneficial owner is/will be, and as a result, will determine who the eligible party is that will have the rightful claim under ACIS. Tools built against a customer order, capitalised in the fixed asset register and amortised through 'piece price' would appear to escape the 'vendor tooling' net Apparently, further guidance from ACIS administrators is on the way in this area. No doubt there will be UCL's arising from any corrective action in regards to entitlements, especially if claimants have been using this approach since Scheme commencement.

If you need to discuss Vendor Tooling and specific claim eligibility, please feel free to call TCF Services, as many scenarios can apply and if you get it wrong, the repercussions can be significant in financial terms. **Call David Tonkin on 02/8219-4900 or Peter Choma on 03/9379-0022 to work through your scenarios.**