Strategic Foreign Direct Investment in the Automotive Leather Industry of South Africa

The Impact of the MIDP on Branaa South Africa (Pty) Ltd-

By

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CONFIDENTIALITY CLAUSE

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TO WHOM IT MAY CONCERN

RE: CONFIDENTIALITY CLAUSE

Due to the Strategic and Financial importance of this research it would be appreciated if the contents remain confidential and not be circulated for a period of 5 years.

Sincerely

Francois Nortje

DECLARATION

This research has not been previously accepted for any degree and is not being currently submitted in candidature for any degree.

Signed..

Date...2006-10-10.......................................

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ABSTRACT

The objective of strategic management is to enable an organisation to assess its strategic position.

This study is concerned with identifying the strategic position of Branaa South Africa, and to determine the most suitable expansion strategy in order for the company to increase the current level of monetary benefits offered to Original Equipment Manufacturers under the Motor Industry Development Program. An in-depth literature review is conducted and the relevant business management tools are identified. These tools are used to analyse the position of the company and to evaluate how the current benefits offered, compare to those of competitors.

An analysis is carried out regarding the influence and value of the Motor Industry Development Program benefits. A costing model is then applied to determine how competitive Branaa South Africa is in the automotive leather seat market. The study determines how the benefits offered under the current Motor Industry Development Program structure could be increased in the South African Automotive market, and concludes with proposals on how to achieve new targets.

This study aims to prove that the strategic direction that Branaa South Africa is envisaging is correct. The company should continue to gain a competitive advantage under the current strategic goals which are reviewed annually.

Through the effective use of strategic management principles, and applying these to Branaa South Africa, the company would retain its competitive advantage in the South African Automotive market.

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LIST OF ACRONYMS

BZA	Branaa South Africa (Pty) Ltd (consisting of BZA-C & BZA-F)
BZA-C	Branaa South Africa Cutting Facility (current production facility in South Africa)
BZA-F	Branaa South Africa Finishing Facility (proposed expansion facility)
CBSA	Curtiembre Branaa Sociedad Anoniem (Company Headquarters situated in Montevideo, South America)
CBU	Complete Built Up
CKD	Complete Knock Down
ITAC	International Trade Administration Commission of South Africa
MIDP	Motor Industry Development Program
NAACAM	National Association of Automotive Component & Allied Manufacturers
NAAMSA	National Association of Automobile Manufacturers of South Africa
WTO	World Trade Organisation

Abbreviations used in the motor business in South Africa

AIDC	Automotive Industry Development Centre
AIEC	Automotive Industry Export Council
FDI	Foreign Direct Investment
MIDC	Motor Industry Development Council
MNC	Multi National Company
OEM	Original Equipment Manufacturer (Vehicle Assembler)
PAA	Productive Asset Allowance
RMI	Retail Motor Industry Organisation
SABS	South African Bureau of Standards
The DTI	The Department of Trade and Industry
TISA	Trade and Investment South Africa

CHAPTER ONE: INTRODUCTION

1.1 INTRODUCTION

> "Leadership is not a magnetic personality—that can just as well be a glib tongue. It is not making friends and influencing people—that is flattery. Leadership is lifting a person's vision to higher sights, the raising of a person's performance to a higher standard, the building of a personality beyond its normal limitations"
>
> Peter F. Drucker (2006)

This study attempts to provide a comprehensive understanding of strategic management, planning and associated principles. This understanding is necessary to enable a thorough evaulation of Branaa South Africa (Pty) Ltd (BZA) using the most appropriate strategic management tools.

BZA is a supplier of bovine leather seat covers to the automotive industry in South Africa (SA). BZA entered the SA market in 1997, and since then has experienced growth in terms of sales and product output. In the past two years, BZA has however reached a plateau in terms of securing new contracts. As a supplier to major Original Equipment Manufacturers (OEMs), or also referred to as vehicle assemblers, such as BMW, AUDI, Ford, Mazda and Nissan SA, the company realized the need to undertake a serious evaluation of its current position in the SA automotive leather industry. BZA needs to do a full strategic assessment in order to analyse its strengths, weaknesses, opportunities and threats in order to effectively position the company. Once this has been completed, BZA will be in an informed position to consider the various strategic options available and assess the most suitable options for implementation.

The South African automotive market is fuelled by the Motor Industry Development Program (MIDP) and as second tier raw material supplier; BZA is obliged to determine the real level of benefits that the company is currently offering to the OEMs through duty rebate certificates.

1.2 BACKGROUND

In a media release by the Department of Trade and Industry (DTI) (7 September 2004), it was suggested that the Motor Industry Development Program (MIDP) would undergo a review in 2005. The review is currently underway, and inputs from various stakeholders in the automotive leather seat industry are being welcomed by the DTI. In addition to this, the South African and Australian Governments have over the last few months held several rounds of consultations regarding developments in their respective automotive industries.

Proposed changes to the structure of the MIDP program would significantly impact on various parties and stakeholders in the automotive industry. Many companies have strategically aligned themselves in order to maximize benefits offered by government, and to make use of these incentives to boost competitiveness and to meet industry's objective to enhance global competitiveness. BZA is cost effective and runs a well-managed, professional operation with the main focus on continuously increasing production capacities and capabilities, and through good management principles, increase productivity (output) and decrease costs (input). These operational targets suggest that BZA is very competitive and their products well priced. BZA is in a position to increase output when an increase in demand occurs and additional production capacities are available. BZA is also in a position to diversify upstream by adding new production processes onto the current operational structure.

The concern faced by the company in regards to the MIDP, is that the MIDP benefits local content suppliers only, and not foreign or imported content i.e. raw materials or components. The strategic decision that BZA is faced with is influenced very strongly by the proposed changes in the current MIDP parameters. Although this accelerated review program is currently underway, and many industry role players are involved, no final decisions have yet been made. The question which BZA is faced with is as follows:

Would a substantial foreign direct investment by Curtiembre Branaa Sociedad Anoniem(CBSA) into BZA, to increase production processes, and to increase the companies' local content, be the correct and most suitable way forward, and how would the proposed changes to the current MIDP affect the operations of BZA? Would an investment of US$ 6 000 000 (Strategic Management meeting held at BZA, *January 2006) be justified in order to secure additional business in South Africa? Would this investment increase the net benefit to the OEM, in such a positive manner, that they would allocate new projects to BZA and in addition feel more content with current projects allocated to BZA?*

1.3 MOTIVATION

The motivation for this project is to add value to the strategic fit of BZA, and to determine and re-assure management that some strategic decisions already made, are still in line with the corporate strategy.

The researcher is the Financial Manager of BZA, thus it is imperative for him to have a good understanding of the workings of the MIDP. This study should enhance the researcher's understanding of the MIDP and help to improve his knowledge of the MIDP, and also for him to gain more insight into the SA automotive industry.

Strategic decisions have to be made, and in order for BZA management and the shareholders of the company to be well informed and to make the correct directional changes, or to develop a new corporate strategy, they need to understand what drives the industry, what the customers motivations are for allocating new business, and how they could possibly reach the set goals and targets. This research project will assist the BZA managers and directors of the company to do exactly this. BZA supplies automotive leather seat covers to OEMs, and these OEMs are driven by duty rebates and the amount of rebate certificates that can be generated in the industry. The OEMs have made it very clear to industry role players and to BZA in specific details that the MIDP benefits offered by BZA should be increased. The workings of the MIDP are broadly discussed in Chapter 4. This report will aim to determine whether the strategic change suggested by the Directors is the correct decision, and that the motivation behind the decision should not be limited to the requirements of the OEMs to increase local content. The researcher will try to prove that additional benefits need to compliment the large foreign direct investment strategy, and these benefits should be more internal, or company orientated. The final recommendations and conclusions of the researcher will be given in Chapter 5.

1.4 VALUE OF THE STUDY

The data collected and evaluations undertaken in this research will enable the Directors of BZA to make a well-informed strategic decision regarding the future orientation of the business. This information will assist them in deciding whether to invest in an upstream operation at an estimated cost of R 36 million, and if this planned investment will be sustainable over the short and long term. The purpose of this proposed investment for BZA is to secure long-term sustainable business in the automotive leather seat industry. This is an option already being considered within BZA.

1.5 PROBLEM STATEMENT

When the Directors of the Multinational Branaa Group of Companies visited South Africa during 2004, they realized that some strategic changes were required in order for BZA to remain competitive as a company competing in the automotive industry against fierce competitors. These competitors were winning tenders and new business projects, and BZA was lagging behind in securing larger more reliable long-term contracts with the major OEMs in the country.

The dilemma facing the directors was to determine how BZA can become more competitive in the local automotive leather market. A large proportion of export business is not allocated to BZA. The main reasons given by the OEMs to BZA are that the local content contribution that BZA is offering on raw materials is lower than required, and is lower than what competitors are offering in the industry. The MIDP is driven by the local content portion of the product, and the lower the local content, the less net benefit there is for the OEM.

A new corporate strategy and operational direction of BZA needed to be investigated, researched, identified and successfully implemented. The researcher was tasked with compiling and preparing an in depth report for submission to the directors of BZA in order for them to make a strategic management decision.

The higher the local content of export products, the higher the returns or net benefit to the OEMs will be, as a result of the increased Eligible Export Credit Certificates (EECCs) values, which they earn. These certificates are used to offset import duties that are raised by customs on imported components or completely knock down (CKD) – units, and completely built up (CBU) - units vehicles for use in the local market

As a leather supplier to BMW South Africa, BZA was considered for new projects, but was unsuccessful in securing substantial new business deals. Projects have life spans, and as these projects run out, BZA was unsuccessful in securing new projects. The directors' intentions were to expand operations in South Africa and increase output volumes. BZA has a competitive advantage in the quality and supply of the automotive leather seat products, against other major suppliers in the leather seat cover value chain (as discussed in details in Chapter 3 of this study). Strategic management sessions held at BZA, identified that the company was not only competing against other suppliers to the OEMs, but that BZA was competing against an unfair subsidy offered by the South African government on local content products. (As a 100% importer of raw materials, BZA has to compete against local raw material, and in terms of the local content application in the MIDP, this is a disadvantage to BZA). This subsidy is fuelled through the MIDP program and offers larger benefits to local product suppliers. The subsidy (through import duty rebate substitution) negatively impacts on foreign companies investing in the local market. This proves to be an unfair advantage that the local hide suppliers received. On the other hand, the shortage of raw leather hides in the South African, and Southern African region requires an imported product to assist in the continuous supply of an export product. Without foreign products entering into the South African market, the constant supply of export products would be jeopardized, which would negatively impact on the automotive leather industry. BZA had to make a strategic decision in deciding which direction the company must take, and had two options, namely:

1. How could BZA increase the local content portion of their product to derive more MIDP benefits for the OEMs? Would this make BZA more competitive, so that the OEMs should re-consider purchasing from BZA? Would the increased local content portion mean an increase in the benefit offered through the MIDP to the OEMs?
2. BZA should determine exactly what the real net benefit in monetary value is that the OEMs receives through the current MIDP program, and determine if this benefit could be offered to the OEMs in terms of a price reduction. Could BZA lower their product selling price

sufficiently enough to offer the same benefit to the OEMs, and still remain a profitable manufacturing concern in the South African automotive market?

1.6 OBJECTIVES OF THE STUDY

This research project will aim to offer valuable insights (Chapter 5) into developing a new corporate strategy through a substantial foreign direct investment in an upstream operation in terms of a new leather finishing plant.

The overall objective of this paper is to solve a specific business problem, namely, the Directors of BZA have to make, and successfully implement, a strategic decision about the future of BZA, and the effects that the MIDP has on the company currently, in the short term (the next 12 to 24 months), and in the long term (until the end of the current structure of the MIDP which runs out in 2012). In order to achieve this, the following objectives will be examined:

- To understand the environment in which BZA operates, through the utilization of various strategic analysis techniques.
- To determine the value of the MIDP benefits offered under the current investment structure (BZA cutting facility only)
- To determine the value of the MIDP benefits offered under the proposed new investment structure (BZA cutting facility and finishing plant).
- To evaluate the increased benefits derived from increased investment, and thereby satisfying the requirements of the OEMs.
- Establish how the company must position itself in order to become more competitive and how to develop a sustainable competitive advantage.
- Determine which strategy should be implemented at BZA, especially in relation to these two options: an *expansion strategy* in the South African automotive leather seat industry, or a *price reducing strategy* to increase BZA in terms of price-competitiveness in the South African automotive leather industry.
- To evaluate whether the strategy suggested by the directors of BZA is correct in terms of the increased financial benefits offered to the OEMs

- Provide recommendations that will provide BZA with valuable information and strategic evaluations in order to re-position and align itself with the possibilities of increasing the actual net requirements of the OEMs in terms of the MIDP program, through increased local content contributions.

The abovementioned objectives of the study will be clearly identified, evaluated and addressed, and the desired end results will be made available to the Directors of BZA in order to assist them with their strategic planning and vision for the future of the company in South Africa.

1.7 METHODOLOGY

The methodology, or research method, of this project is based on an actual case study of a South African company supplying the automotive industry. This company is Branaa South Africa (Pty) Ltd.

Methodology "refers to the theory of how research should be undertaken" (Saunders, 2003:2).
Robson (2002:178) defines a case study as "a strategy for doing research which involves an empirical investigation of a particular contemporary phenomenon within its real life context using multiple sources of evidence"
As this is a case study approach, the researcher will not gather data through data collection methods, but rather use readily available data.

1.8 LIMITATIONS

Although there are some limitations to the project, all efforts are made to objectively evaluate the relevant facts and to interpret the data into reliable information. Whilst evaluating the information, certain financial information will be made available, but will carry some financial limitations, and will be considered confidential. In these cases, financial data will be disguised, but the essential relationships of the data will be preserved

The essential relationships between products and competitors in the leather value chain have been preserved. Factors revealing the competitive advantage of BZA will be excluded from this study. Company trade secrets will be excluded from the report.

1.9 STRUCTURE OF THE STUDY

Chapter One provides an overview of the entire study and identifies the value of this research project, and details the objectives. Chapter One identifies the problem statement, allows background information and motivates the aim of the study. It further acknowledges the limitations and the value of the study.

Chapter Two follows as a literature review and details the particular research methodology that is selected. The aim of the project is to determine a successful corporate strategy for the company, BZA. Chapter 2 consists of various strategic analysis tools, and the researcher draws intensively on knowledge from Lynch, Ghauri, Fleisher and Michael Porter, amongst others. Corporate strategy is analysed, and tested in relation to the company in order to assess if the strategy is good. Various analysis techniques are applied, such as the PEST, SWOT, and Porters 5 forces model, amongst others, and are used to determine the current position, and the future direction of the company, as well as the environment in which the company operates. Ultimately, the company must maintain / develop a sustainable competitive advantage, and develop a business level strategy which will lead to this long term sustainable advantage. Competitive intelligence is the key to successful business. The theoretical background is required in order to create a platform from where BZA and the business environment, in which the company operates, can be evaluated. Only a basic comparison will be drawn between the company and its strategic and competitive analysis in order to facilitate the research. Reliable results are a pre-requisite for the Directors of BZA to make a well-informed strategic decision regarding the future of the company in South Africa.

Chapter Three strategically identifies the company and positions it within its current business environment. It continues to introduce recent developments in the automotive leather seat industry and identifies the industrial policy that government has developed to promote and protect the infant automotive industry in South Africa. The chapter further introduces the Motor Industry Development Program (MIDP), the history, goals, principles and objectives of the MIDP. It sets the platform on which the company is measured, and it assists management in better understanding the MIDP and the workings of the MIDP. The influences of the MIDP on a local foreign national company such as Branaa is highlighted, and helps overseas management understand what drives the industry, and whether any directional corrections in the corporate strategy need to be developed and implemented.

Chapter Four is a section of financial analysis, and includes the methods from which the real MIDP calculations are made. The researcher measures the real net benefit offered to the OEM under the current circumstances of the company, and also under different investment options within the South African automotive industry, such as the values future net benefits offered under the MIDP, when the upstream investment in the finishing plant is made. The researcher continues to measure these benefits against local competitors who are using local raw material, versus Branaa, which imports 100% of its raw materials (finished bovine leather hides). The analysis and presentation of results can lead to conclusions, from which management and the directors of the company can strategically align themselves to the benefit of the company, and through this ensure that all objectives are covered. Strategic management tools help to identify in what way the business environment impacts on strategic management and are thus related to the strategic planning process. The researcher ultimately determines the real benefits offered under the current structure of the MIDP, and determines which strategy should be implemented at BZA, and if the proposed strategy is correct in terms of increased financial benefits offered to the OEMs. A strategic decision making process follows after all the relevant data is gathered, and the facts have been identified and evaluated. After a careful comparison of the advantages and disadvantages related to these strategic options, and the consideration of industry opportunities and threats, BZA will be in a beneficial position to implement the relevant business strategy. The future orientation of the company will determine whether it will maintain a competitive advantage and then how to strategically align itself in relation to industry expectations to secure future business.

Chapter Five concludes this study with recommendations to the management team of BZA, and to the Board of Directors of Branaa Global.

1.10 CONCLUSION

According to the author, the strategic direction that Branaa South Africa is envisaging is good. The company would continue to gain a competitive advantage under the current strategic goals which are reviewed annually.

It is recommended by the author that through the effective use of strategic management principles, and by applying these to Branaa South Africa, the company would retain a competitive advantage within the South African Automotive market.

The broad objective of this study is to determine the strategic direction of the company, and to determine whether investing in a new upstream expansion project (leather finishing plant) in South Africa would add value to the organisation, and if an increase in local content value would increase MIDP benefits offered to OEMs. Would these increased financial benefits offered put the company in a stronger competitive position, and would this possibly mean an increase in new business?

Ultimately, this report shows that BZA should strategically invest in a finishing plant in South Africa, and it is shown that the net benefits offered to the OEMs are increased, but the MIDP should not be the only or ultimate consideration. There is another, more important consideration, mentioned in the final pages of this paper.

"The key to successful leadership is influence, not authority"

Kenneth Blanchard (2006)

CHAPTER TWO: LITERATURE REVIEW & RESEARCH METHODOLOGY

2.1 INTRODUCTION

In accordance with Manion, G (2003), the theoretical framework informs the design of the research methodology. Details on the research methodology used are also outlined in this chapter. It also explains how various analyses techniques are undertaken to reach the desired outcome. It is important to identify the most appropriate research method. The chosen method must address the research question as well as the limitations caused by the scope of the topic and the nature of the research conducted.

The link between theory and practice must also be evident. Hence the direction of the literature reviews undertaken. The focus of the research is on the need for strategic planning.

The strategy which the researcher will focus on is concise, direct and to the point. Or, in the words of Larry Bossidy:

> "If you can't describe your strategy in twenty minutes, simply and in plain language, you haven't got a plan. But, people may say, I've got a complex strategy. It can't be reduced to page. That's nonsense. That's not a complex strategy. It's a complex thought about strategy." –
> *Larry Bossidy, Chairman, Honeywell International, in 'Execution: The Discipline of Getting Things Done'*

2.2 METHODOLOGY

Robson (2002:178) defines a case study as "a strategy for doing research which involves an empirical investigation of a particular contemporary phenomenon within its real life context using multiple sources of evidence"

A background view of relevant role players will form the basis to understanding and solving the research problem. These role players are:

- Branaa SA (Pty) Ltd

- The MIDP program in South Africa

The following financial calculations will be tested and evaluated in order to determine the benefits offered by the MIDP program. It will show clearly what strategic direction BZA should take in order to procure increased business.

  - The current financial benefits offered to the OEMs under the MIDP program, will be calculated in terms of the current situation of BZA, where raw materials are imported.
  - The current financial benefit offered to the OEMs under the MIDP program will be calculated in terms of the current situation of industry competitors, where local raw materials are used.
  - The future financial benefit offered to the OEMs under the MIDP program will be calculated in terms of the proposed situation of BZA, where a finishing plant will be built, additional upstream processes are to be added to the leather value chain, and local content will be increased.

The directors of BZA would be able to determine and evaluate the following statements

1. BZA will become more competitive and secure increased business contracts if they implement an ***expansion strategy*** in terms of the finishing plant.
2. BZA will become more competitive and secure increased business contracts if they implement a ***price reducing strategy***.
3. The ***net benefit the OEM receives*** when purchasing automotive leather seat covers from BZA is lower than when they purchase from a local leather supplier.
4. The ***net benefit the OEM receives*** when purchasing automotive leather seat covers from BZA with a local leather finishing plant will increase.

A working / practical example of the MIDP calculations related to BZA in Chapter 4 shows how the OEMs benefit from this program and how a company like BZA which imports the raw material must compete against local suppliers in the automotive leather market. This "unfair advantage" offered to local competitors is offered while there is a shortage of raw materials and leather hides in the local market. Leather hides have to be imported to supply the demand of OEMs. These imported hides must now compete against the "subsidized" local hides. It is the objective of this report to determine the net benefits offered through the MIDP to the OEMs, comparing local hides against imported hides.

In relation to the current situation in which BZA finds itself, Saunders (2003:3) would claim that "it would seem sensible to define the business strategy and this management research as a systematic research process to find out industry specific information about the business and management", and convert this information into sensible data. As cited in Saunders (2003:3), Easterby-Smith *et al.* (2002) argue that there are three things that should be combined to make a business case study a successful focus for research, and are discussed in Table 2.1.

Table 2.1 Factors making a Business Case Study successful.

Author (Saunders, M. 2003)	This Study
"The way in which a manager draws on knowledge developed by other disciplines"	The way in which the researcher draws on industry specific knowledge and applies the findings developed by other disciplines onto the situation at BZA, in order to position the company correctly;
"The fact that managers tend to be busy people. They are unlikely to allow research access unless they see personal or commercial advantages"	The researcher is employed as financial manager at BZA, and BZA is in a situation where the research will allow commercial advantages, in the sense that the company would be able to benchmark itself, and position itself for future business opportunities. The researcher is therefore allowed access, in order to complete the task successfully.
"The requirement for the research should have some practical consequence"	The research undertaken for BZA will have a practical consequence. This means the company will consider the findings of the research, and it will be suggested by the researcher to BZA that

	BZA should take some form of action or take into account the practical consequences of the findings.

According to Saunders, *et al* (2003), business and management research not only needs to provide findings that advance knowledge and understanding, it also needs to address business issues and practical managerial problems. This is the case with BZA, where a specific problem needs to be researched and addressed. The task orientated research is to determine a new strategy in order for BZA to increase its local content portion in its product range in terms of the MIDP benefits offered to its customers. The researcher also shows a direct "intellectual curiosity" (Saunders 2003:4), and addresses this at the same time, and through the research also considerers the practical implications of the findings. Drawing on knowledge from Saunders (2003:4), it is "within these boundaries of advancing knowledge, addressing business issues and solving managerial problems", that this research is undertaken and successfully completed.

Furthermore, the research project also assists in understanding and explaining the impact of the MIDP under the current program, and also under the accelerated review that is taking place, and the effect this will have on BZA as an organization. The research conclusion in Chapter 5 suggests an appropriate action based on the findings of the report.

An in-depth literature review is undertaken, based on two major reasons (Sharp and Howard, 1996). At first, a *preliminary search* is undertaken to help generate and refine the research ideas, and secondly, a *critical review* of the BZA situation is undertaken in order to demonstrate a clear awareness by the researcher of his knowledge of the organization, and more appropriately of the subject and its limitations. The critical review of the research data will assist the managers at BZA to better understand and have insight into previous research that relates to this research problem and objectives. Saunders (2003:75) summarises the critical review and sets "the research in context" by critically discussing industry related work in terms of the MIDP, "that has already been undertaken, and draws out key points", in order to ultimately propose a new strategic position for the company.

Conclusions on important issues, such as the real MIDP benefits offered by BZA to the OEMs, cannot be made unless the research covers the relevant information, and thus all relevant information on the particular subject is gathered. The information is then analyzed, an informed judgment made and a final conclusion about the most suitable solution to the research problem is formulated. In this business study, the researcher works with a task specific problem faced by managers of BZA.

Drawing on knowledge from Ghauri (2002:9), we learn that *without* successful and complete *research, one cannot attend to the* task *specific problem* or other similar questions that may arise while developing new strategy for a company such as BZA. Quality research requires competence in logical reasoning and analysis. Ghauri (2002:35) concludes that the researcher will show a strong "command over the research methodology that will be used". Research methodology is an important aspect of the research plan. The research topic that was chosen is finding, selecting, structuring and solving of an industry specific problem, namely: how to successfully increase local content values in order to increase MIDP benefits in the automotive leather sector, amongst others. In order to grasp, represent and understand these industry specific problems, concepts, theories and models are crucial. Theoretical knowledge and the ability to think conceptually are vital in attempting to solve such a research problem. Problems represent the point of departure in research. The structuring of these problems influences the subsequent research activities. The researcher undertakes a systematic information collection and critical analysis process, through conceptual and methodological insights, in order to understand how the MIDP works, and then applies that knowledge to the applicable organizational situation. After this process has been completed, the suggested ideas are tested, and the new benefits offered in terms of the MIDP is determined to see if the real benefit increased. Once these theoretical calculations are proven, the researcher can suggest an implementation program to the management of BZA.

> Research designs are master techniques...
>
> (Kornhauser and Lazarsfeld, 1955)

In order to conduct research it is necessary to first develop the research design, and Ghauri (2002:47) argues that "the research design is the plan" that will be used in order to conceptualize the research problem in terms of relevant and practical research, and that the "quality of the research" will be influenced by the research design as emphasized in the quote from Kornhauser and Lazarsfeld.

2.2.1 Research Design

Ghauri (2002) teaches that "empirical research is conducted to answer specific research questions", such as the situation with BZA. Research design should be developed in such a manner, that the research problem can be answered in the best possible way – within the given constraints. The research design is effective in producing the required information "within the constraints of the researcher, such as time, skill and budgetary constraints" Ghauri (2002:47). Even though the research results should be produced within strict time constraints, a number of possible research options are considered before finally choosing the specific design. Ghauri (2002) also states that the choice of the research design can also be viewed as the strategy or the way, in which the researcher will get the required information. The next step the researcher was faced with was to determine what data to collect and how it could be collected.

2.2.2 Data Collection

Data collection methods and techniques depends on the research problem and its purpose (Jankowicz, 1991), and in the case of BZA, structured and quantitative methods are used for financial calculations. Financial calculations are not open to interpretation, and to determine financial benefits offered through the MIDP does not require long questionnaires or qualitative data collection.

Ghauri (2002:86) comments and agrees with other writers that "qualitative research is a mixture of the rational, explorative and intuitive, where the skills and experience of the researcher play an important role in the analysis of data. It is often focused on social process and not on social structures, which is often the focus in quantitative research. The skills needed to do qualitative research are thinking abstractly, stepping back and critically analyzing situations, recognizing and avoiding biases, obtaining valid and reliable information, having theoretical and social sensitivity and the ability to keep analytical distance while at the same time utilizing past experience, and having a shrewd sense of observation and interaction (van Maanen, 1983; Strauss and Corbin, 1990)".

A qualitative research approach requires certain skills by the researcher, and according to Reichardt & Cook (1979), the researcher must have some of the following attributes (shortened), as shown in Table 2.2.

Table 2.2 Attributes of the Researcher

Attributes of the Researcher	**Desired Outcome**
Emphasis on understanding	The researcher shows a good understanding of the MIDP and the workings of the MIDP, although it is a challenge to many industry managers, and only a few have a complete understanding thereof. It is left many times to the company auditors who have specialized motor industry departments to calculate the MIDP benefits. This study should confirm level of knowledge of the researcher and should help the researcher in increasing his understanding of the MIDP.
Interpretation and rational approach	Throughout this study the researcher makes decisions based on rational, sensible and intelligent thinking, backed by a thorough knowledge of the industry
Subjective 'insider view' and closeness to data	As the researcher is employed in BZA, as financial manager, the researcher is close to the available data. However, all attempts are made to be subjective in all interpretations.
Explorative orientation	The researcher understands the explorative nature of this study and effectively uses his skills to gain knowledge of the workings of the MIDP.
Process oriented	The researcher must be process orientated

Source: (Reichardt and Cook, 1979)

In this research project, a qualitative data collection method is used, and although sometimes "qualitative research is unstructured" (Ghauri, 2002:88), the researcher employs a number of observations and aims to explain different aspects of the problem area, and several aspects of the research area are analyzed. As this is a case study, the data available to the researcher through his business connection is deemed sufficient (justified) to establish the in-depth study required and in the words of Ghauri (2002:88), are sufficient to provide a *"thick description"* of the business case study. A qualitative method is, therefore, most suitable in the case of BZA, where the objectives of the study demand in-depth insight into the workings of the MIDP.

2.2.3 Data Sampling

When drawing on the knowledge from Ghauri (2002:120), we consider that the purpose of qualitative research, regarding the sampling aspect, is seldom to arrive at statistically valid conclusions, although it is possible in some cases. In the case of BZA, where a qualitative study is undertaken, the objective is to gain insights into what influences the workings of the MIDP, and how strategic decisions can be directed in order to achieve a higher net benefit for the customers of BZA in terms of local content.

2.2.4 Conducting Case Studies

While preparing to undertake this company specific, industry specific case study, of BZA, the researcher realizes that the process of understanding the case study is manifested in various stages and these are clearly defined by Bonoma (1985: 204-6). The theory/data/theory revision cycle, as suggested by Bonoma (1985: 204-6), is quite useful. This revision process goes through four stages: 'drift', 'design', 'prediction' and 'disconfirmation' Bonoma (1985: 204-6). At the beginning of this research project the researcher is in a 'drift' stage, gathering information to understand the automotive industry, the MIDP and the workings of the MIDP. Then the information is gathered in order to position the company, BZA, and to conceptualize the place it has in the automotive industry. The gathering of information provides the knowledge of how the automotive industry operates. This stage widens the perspective of the researcher and often leads to modification in the basic research questions (van Maanen, 1983).

According to Ghauri (2002:174), the researcher then moves to the 'design', or choice of strategy to collect data needed to answer the research questions. At this stage the researcher already has some assumptions of the outcome of the research, and begins to develop explanations of the observations. The researcher then assesses and refines those areas of the research project as suggested by the drift

stage as asserted by Bonoma (1985:205). An automatic reaction occurs when the researchers constantly reverts back to the drift stage to re-determine if the research meets the initial requirements. Ghauri (2002:175), further draws on the knowledge of Bonoma, and comments that during the middle-to-late stage of the project, the researcher has a good understanding of the factors on which the case information may be grouped, and proceeds with further case construction and analysis. At this late stage, the researcher can almost predict the outcome of the research, although the researcher must be careful not to influence the true outcome. The researcher should still remain objective.
In the case study of BZA, the researcher shows a clear understanding of the MIDP process, and what benefits needed to be offered to the OEMs in order to secure more business. Theoretically, the local content portion of automotive leather seat covers should be increased, and the company should invest in up-stream processes in order to achieve this goal. While drawing on these assumptions, the researcher develops a secondary research problem, namely, to quantify the level of up-stream investment, and the impact of foreign direct investment in the automotive leather industry in South Africa. As result the researcher develops some tentative explanations. Similarly the researcher also realizes that some generalizations in the industry are very valid in particular circumstances, settings, and specifically in the automotive industries. One such a generalization, is the narrow statement made in the industry that industry role players should increase local content in order to secure additional business. Although this statement is generally accepted by industry and conceived as correct, this research aims to define the statement, and to add a financial context or value to the statement.

Ghauri (2002:175), states that the final stage of the design and case study preparation research method, is the 'disconfirmation' stage, and refers to the analysis of the results. Here the testing of the generalization statement is done. The researcher realizes that these four stages form a better understanding of the evolution of the research, and is practically applied in the case study of BZA and the MIDP.

Another aspect that is successfully considered and applied by the researcher whilst undertaking this case specific research project of the BZA organization, is the phenomenon of "triangulation" (Ghauri 2002:181) where a "combination of the methodologies are combined" and different kinds of data are collected through different methods. The triangulation process is believed to assist the researcher in improving the accuracy of his results and his final conclusions. Ghauri (2002) explains triangulation as follows:

> "Triangulation can produce a more complete, holistic and contextual portrait of the object under study" (Ghauri, 2002:182)

2.3 BUSINESS STRATEGY

> "The great successful men of the world have used their imagination... they think ahead and create their mental picture in all it details, filling in here, adding a little there, altering this a bit and that a bit, but steadily building - steadily building". Robert Collier (2006)

According to Lynch (2000:5), "corporate strategy is concerned with an organisation's basic direction for the future: its purpose, its ambitions, its resources and how it interacts with the world in which it operates. Every aspect of the organisation plays a role in this strategy – its people, its finances, its production methods and its environment (including its customers)".

Lynch (2000:7), also states that "Corporate Strategy can be described as an organisation's *sense of purpose"*. Commentators such as Ansoff (1969) and Drucker (1961) clearly refer to this aspect of strategy, as: "mapping out the future directions that need to be adopted against the resources possessed by the organisation. Purpose alone, however, is not strategy. Plans or actions need to be developed to put the purpose into practice".

This sense of purpose and its associated actions can be seen in the following definition of corporate strategy as cited by Lynch (2000:8):

> "Corporate strategy s the pattern of major objectives, purposes or goals and essential policies or plans for achieving those goals, stated in such a way as to define what business the company is in or is to be in and the kind of company it is or is to be".
>
> -Andrews, K (1971)

Lynch (2000:11), asserts that there are five key elements to strategic decision making that can be adapted primarily to an organisation's ability to add value and compete in the automotive leather market place.

- *Sustainability*. Management decisions must be made in such a way that it can be maintained over a period of time. For the long-term survival of BZA, it is important that the strategy that is developed, and the strategy that is proposed to management from this research is sustainable.
- *Develop processes to deliver the strategy*. This research will assist BZA management in making the correct decisions when identifying the new corporate strategy. The difficulty however, is how BZA will undertake this task in order to deliver added value to the current strategy. This study should provide recommendations to overcome such a difficulty for BZA in order to evolve towards their chosen purpose
- *Offer competitive advantages*. A sustainable strategy is more likely if the strategy delivers sustainable competitive advantages over its actual or potential competitors. Corporate strategy usually takes place in a competitive environment. The automotive leather seat industry in South Africa is very competitive, as is discussed in Chapter 3 (case study). BZA has to adapt its current strategy in order to remain with a competitive advantage, and it is possible that the proposed investment in the finishing plant should give the company that competitive advantage.
- *Exploit linkages between the organisation and its environment*. Links that cannot easily be duplicated by competitors are important, and this starts with good business relationships with customers, like BZA has, and a cost advantage, which BZA has since it purchases its raw materials from its head office, called CBSA. These advantages contribute to superior performance. The strategy has to exploit these linkages that exist between the organisation and its environment: suppliers, customers, competitors and often the government itself. Drawing on knowledge from Porter's 5 forces model (Lynch, 2002:125), as discussed in Chapter 2 and applied to BZA in Chapter 3, assists to clearly identify the advantages in the environment.
- *Vision.* Innovative management strategies that move the company forward – beyond its current environment.

"Corporate strategy is important because it deals with the major, fundamental issues that affect the future of organisations".

Quinn, JB (1980)

According to Lynch (2002:42), Quinn is one of the most distinguished writers and thinkers in the strategy field. Quinn (1980) commented that, "strategic decisions are those that determine the overall direction of the company".

As outlined by Lynch (2002:17), when an organization makes major errors in corporate strategy, it will suffer the consequences, possibly risking its own survival, and for this reason, it is important that a thorough strategic assessment of BZA is undertaken in order to make recommendations on the corporate strategy.

Lynch (2002:17) also provides some indications of the nature of corporate strategy, and the importance thereof, and these are shown in Table 2.3

Table 2.3 Nature of Corporate Strategy

• *Corporate strategy involves the entire organisation, it covers al areas and functions of BZA.*
• *Corporate strategy is likely to concern itself with the survival of the business as a minimum objective and the creation of value added as a maximum objective.*
• *Corporate strategy covers the range and depth of the organisation's activities.*
• *Corporate strategy directs the changing and evolving relationship of the organization with its environment. .*
• *Corporate strategy is central to the development of sustainable competitive advantage.*
• *Corporate strategy development is crucial to adding value.*

This research, in determining the strategic direction for BZA, follows the sequential approach to corporate strategy, where, according to Lynch (2000:19), one area follows another for reasons of clarity and development.

These areas are shown in Figure 2.1.

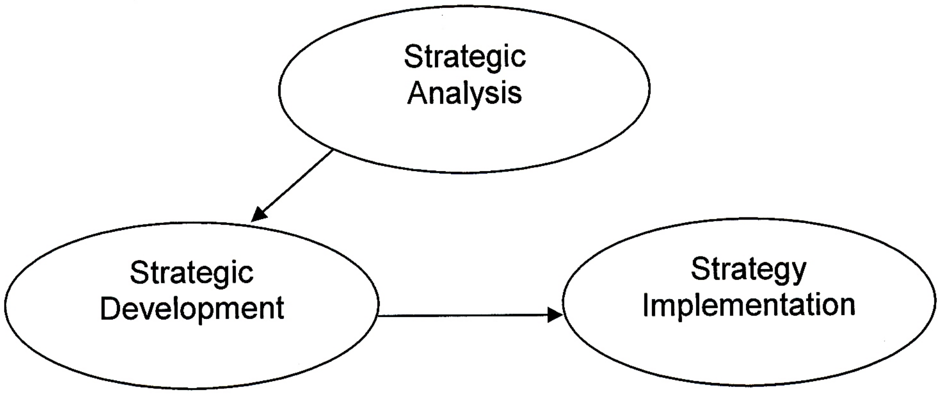

Figure 2.1 Three Core Areas of Corporate Strategy (Lynch, 2002:19)

Some commentators, such as Jaunch and Glueck (1988) and Argenti (1965) commented on corporate strategy, but differ in the way that strategy develops. Some have judged corporate strategy to be essentially a linear and rational process, starting with where-we-are-now and then developing new strategies for the future. A prescriptive approach to corporate strategy is one whose objective has been defined in advance and whose main elements have been developed before the strategy commences.

It is believed by Lynch (2000:24) that "the prescriptive approach takes the view that the three core areas – strategic analysis, strategic development and strategy implementation – are linked together sequentially". It is possible to use the strategic analysis to develop a strategy which is then successfully implemented. The prescriptive approach to corporate strategy is prescribed in Figure 2.2.

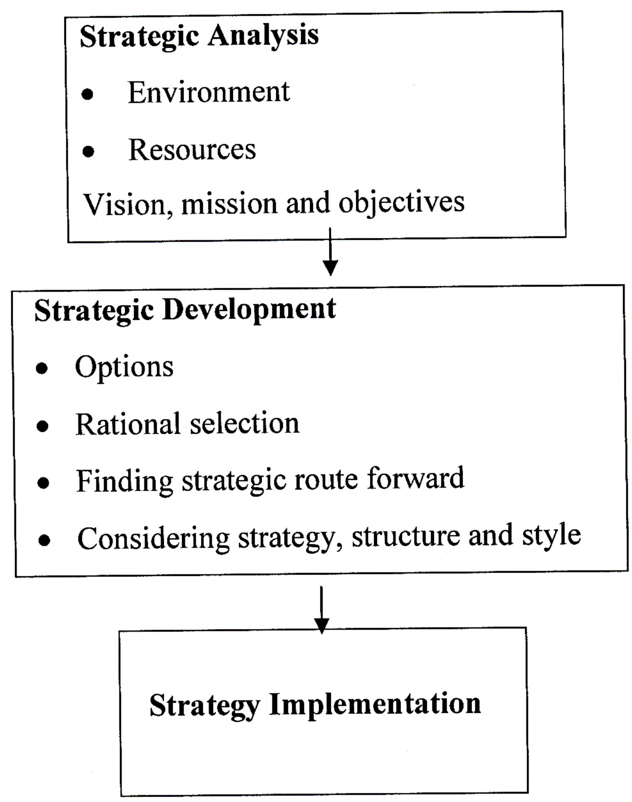

Figure 2.2 Prescriptive Strategic Approaches (Lynch 2000:25)

> "In January-February 1993 issue of the *Harvard Business Review*, Gary Hamel and CK Prahalad, professors at the London Business School and the University of Michigan, turned much of their recent thinking upside down by asserting that the real function of a company's strategy is not to match its resources with its opportunities, as many businessmen assume, but rather to set goals which 'stretch' a company beyond what most of its managers believe is possible"
>
> Extract from an Article in The Economist, 20 March 1993.

In *Competitive Strategy* (Porter M, 1980), Lynch cites Porter as follows: "a firm's profitability is determined by the characteristics of its industry and the firm's position within it, so these should also determine its strategy".

The position of the researcher is that the company must find a balance between "stretch goals", as suggested by Hamel and Prahalad (Harvard Business Review, 1993), where the company should carefully consider its limitations – and specifically financial limitations come to mind. The company should always consider their investors, and their required rate of return. It is suggested, however, by the researcher, that BZA can not consider formulating its strategy on the results of Professor James Quinn's publication, where Quinn suggests that the corporate strategy is constantly revised by trial and error (Quinn 1980).

As outlined by Porter (1980), and considering the position of BZA in the automotive industry, equally important would be the study of the environment in which the company operates, and it is conceivable, at least in theory, that every element of an organization's environment may influence the corporate strategy (Lynch 2002).

According to Lynch (2002:105), a better solution would be too clearly "identify the key factors for success in the industry and then to direct the environmental analysis towards these factors". In spite of these difficulties, it is important to study the environment surrounding BZA for three main reasons as shown in Table 2.4

Table 2.4 Three reasons to study the Environment surrounding the company

1. A study of the environment will provide information on the nature of competition as a step towards developing sustainable competitive advantage. Know your competitors.
2. An organisation must perceive opportunities to be explored and threats to be contained. Opportunities and threats may come not just from competitors but also from government decisions, like the sudden accelerated review of the MIDP program, after Australia complained to the World Trade Organisation (WTO). These changes will have a dramatic change on the motor industry, as well as on automotive leather seat suppliers.
3. There are opportunities to network with customers, in the sense where a company could agree to develop an in house process for customers, such as laminating the seat covers. This will causes the company to have a competitive advantage over competitors, and realise an enormous cost saving to the end customer. Such sustainable co-operative linkages produce better relationships, and strengthen the organisation in its environment by providing mutual support with others.

(Adapted from Lynch, 2002)

Without making any pre-determined assumptions, the proposed strategy for a company should be "good", if the implementation thereof yields the required results to the organisation.

The study will show how to increase the net benefits offered to OEMs in terms of the MIDP structure, and if the increasing local content in the leather seat covers is indeed a suitable option. According to Lynch (2002:28), 'good' strategy "delivers the purpose set out for the strategy in the beginning", and as outlined by Lynch (2002:28), in the end, by using Lynch's approach, BZA management should be able to answer some important questions;

- Was the purpose itself reasonable?
- Was the purpose clearly defined, beyond some general objective? Such vagueness may make it difficult to test whether a 'good' strategy has been developed.
- Can we afford to wait until the strategy has been achieved before we test whether it is good? It is exactly for this reason that this research is undertaken. In order for the researcher to inform BZA management in advance of the financial implications in two aspects:

  - Is the large amount of Foreign Direct Investment justified?

  - With which margin, would the current net benefit offered increase under a proposed increased local content strategy?

Lynch (2002:29), asserts that there are three tests available to assess a good strategy, as shown in Table no 2.5

Table 2.5 Three Tests to Assess a Good Strategy

The value-added test	A good strategy should deliver increased value This might show in increased profitability, but might also be visible in gains in longer-term measures of business performance such as market share, innovative abilities and customer satisfaction.
The consistency test	A good strategy will be consistent with the circumstances that surround a business at any point in time. It will use its resources efficiently in its changing environment cope with the circumstances of those changes. In this sense a company involved in the automotive lindustry

	should be prepared to cope with changes in the MIDP structure, and the accelerated review that is already taking place.
The competitive advantage test	A good strategy should increase the sustainable competitive advantage of the company.

(Adapted from Lynch 2002)

Lynch (2000:29), also states that the next few tests relate to the principles of originality and logical thought when evaluating strategy, as shown in Table 2.6

Table 2.6 Five Tests to Evaluate Originality of a Good Strategy

The originality test.	The best strategy often derives from doing something totally different. Results -In some cases the options are limited; there is not much room for thinking out of the box, or illogical originality. Companies are sometimes also limited by financial implications and calculations.
The purpose test	The strategy should not be confused to only include the aspirations and ambitions of the leaders of the organisation. It should consider the purpose of the organisation.
The logical consistency test	The recommendations should flow in a clear and logical way. We should trust in the evidence – even if it is information received from a competitor?
The risk and resources test	Are the risks associated with the proposed strategy sensible in relation to the organisation? The strategy could be consistent with the overall purpose, but involve such large levels of risk that

	they are unacceptable. Moreover, they may require resources that are substantially beyond those available to the organisation – not just finance, but perhaps people and skills.
The flexibility test	Does the proposed strategy lock the organisation into the future regardless of the way the environment and the resources might change? Do they allow some flexibility depending on the way that competition, the economy, the management and employees and other factors develop?

(Adapted from Lynch 2002)

Although Lynch (2002:29) has concluded that "these tests are not complete in themselves", they provide the researcher with tools to evaluate the proposed new strategic direction that a company should consider.

2.4 STRATEGIC ANALYSIS

Considering the position of some companies supplying the automotive industry, a strong need has developed for research to determine the competitiveness of the organisation. Fleisher (2003:5) would argue that Competitive intelligence (CI), and the successful analysis of data into intelligence is required through various strategic analysis techniques, and the researcher acknowledges that this is required, for management to be able to undertake well informed business decisions. The researcher aims to use a number of these techniques to evaluate the automotive industry. These techniques are used in order to assist the researcher analyse the market and draw effective conclusions from the limited data available in the industry. In-depth analysis of the industry will acknowledge the following statement of Porter (1996).

> A company can outperform its rivals only if it can establish a difference of value to customers that can be preserved over time.
> Michael Porter (1996)

Competitive analysis continues to evolve in an organisation, and CI needs to become a management priority in order to maintain a competitive advantage over industry rivals. The researcher is in agreement with Fleisher (2003), where some organisations still adopt poor strategies in the decision making process, and these decisions are influenced negatively by some factors, such as emotional rather than objective decision making by senior management, also referred to as "groupthink" and "prior hypothesis bias" (Fleisher 2003:17). A company should also caution against prior hypothesis bias, where data that contradicts management is ignored.

2.4.1 PEST ANALYSIS

This form of analysis is used to analyze the general environment in which the company operates, as opposed to a specific industry (such as the automotive leather industry). Lynch (2000:112) states that the PEST analysis serves as a checklist for the Political, Economic, and Socio-cultural and Technological aspects of the economic environment surrounding the company. The quality of the analysis is greatly enhanced by the use of well-thought-out items, rather than just adding any mentionable items to the checklist. Although the items in the PEST analysis reflect on past experiences and events, it can be used as an effective forecast of the future. The PEST analysis will assist management in formulating the new strategic direction of the company Major investments are often made because of assumptions about the future, derived from a company or a markets past performance. Such assumptions can prove to be detrimental to the future of a company, especially when considering a large foreign direct investment and a final financial decision cannot be based on assumptions and past performance only. The Directors of a company and for that matter the shareholders, will need a reliable analysis of the environment, and a PEST analysis will guide then in a certain direction.

According to Lynch (2000:112), the PEST analysis can be described as follows.

- The study of Political, Economic, Socio-cultural and Technological factors – provides a useful starting point to any analysis of the general environment surrounding an organisation. It is vital to select relevant items to explore general automotive leather industry in South Africa, rather than long lists of items that are of no use.

The prescriptive approach which the company will follow in its strategy development, "favours the development of projections because they are often implied in major strategic decisions", as outlined by Lynch (2000:112). Drawing on the knowledge from Lynch (2000:112), a "scenario" will be developed and evaluated for a company as a "picture of a possible future environment for the organisation", and the "strategic implications will be investigated". The researcher is however, less concerned with prediction but more involved in developing different perspectives on the future strategy. The researcher is in agreement with Lynch, and the aim of this research is to "stimulate new strategic thoughts" about the possible consequences of changes in the current business structure of a company.

The well-known strategic writer, Professor Michael Porter has described the industry life cycle as 'the grandfather of concepts for predicting industry evolution', as outlined by Lynch (2000:112). The basic hypothesis is that an industry – or a market segment within an industry – goes through four basic phases of development, each of which has implications for corporate strategy. This is particularly true in terms of the automotive industry, where new car models are continuously developed, and with this, newly developed leather seat interiors. The researcher addresses these phases of development later in the chapter, and these concepts of predicting industry evolution should not be confused with a scenario development and testing in terms of a PEST analysis for strategy renewal

A prescriptive strategic approach is used for this research, and although the most common items in a PEST analysis relies on past events and experience, and according to Lynch (2000:110), the 'analysis can be used as a forecast of the future'. Corporate strategy is concerned with future action, but the organisation should consider that evidence about the future *may* be derived from what happened in the past (Lynch 2000:110). After some consideration of the comments of Lynch, the researcher would agree, that as a prescriptive strategist, he would suggest that it is worth it for the company to invest in an upstream operation, since we could assume the South African automotive market would remain attractive in the near future. On the other hand, in the context of a scenario-based analysis, a scenario is a model of a possible future environment for the organisation, whose strategic implications can then be investigated. Lynch (2000:111) states that scenarios are "concerned with looking into the future, not predicting the future". Prediction takes the current situation and extrapolates it forward. Scenarios take different situations with alternative starting points". The aim is not to predict the future for a company, but to explore a set of possibilities; a combination of events is usually gathered together into a scenario and then this combination is explored for its strategic significance.

2.4.2 SWOT ANALYSIS

> "The interdependence of purposes, policies and organized action is crucial to the particularity of an individual strategy and its opportunity to identify competitive advantage."
>
> Prof Kenneth Andrews (as cited in Lynch 2000:562)

The status of an organization is reflected through the analysis of the strengths, weaknesses, opportunities and threats of the organization. This analysis is called a SWOT analysis. While strengths and weaknesses require a resource-based analysis, opportunities and threats require an environmental-based analysis (Lynch 2000:562). Strengths are resources within the organization that can be utilised to achieve its performance objectives. Weaknesses are existing limitations within the organization that affect the competitiveness of the organization. Opportunities are defined as favourable, prospective or existing situations such as trends, overlooked market need and change, that create a demand for the organization's products or services. Threats are unfavorable situations or future changes that would impact negatively on the organization's ability to compete effectively.

The view is held by Fleisher (2000: 92) that the wide application of the SWOT analysis greatly contributes to its popularity as an analytical tool. This tool will assist a company in determining the correct direction of the company. The organization as a whole, specific units or individuals within an organization can be analyzed. It should be noted that a SWOT analysis is a useful tool, but must be used in conjunction with strategic judgment. A well thought through shortlist of information would be of more value than a lengthy list produced without argument and logic. Fleisher (2000:103) shows that the FAROUT summary rates this method highest on resource efficiency, usefulness and timeliness.
It is believed by Lynch (2000:562) that the following useful guidelines that will affect the quality of the analysis as shown in Table 2.7

Table 2.7 Guidelines affecting the quality of a SWOT analysis

Keeping information to the point
Critical success factors should be accurately linked to strengths and weaknesses.
Being realistic when listing the strengths and weaknesses.
Distinguishing between where the company is now and where it would like to be in the future.
Stating strengths and weaknesses in competitive terms

A SWOT-analysis supplies management with a general framework for managing and understanding the environment in which the company operates. Strategies should be formulated to address key issues. It should be noted that strategic issues normally impact on the whole of an organization and often need greater allocation of resources to address these needs effectively.

Fleisher (2003:92) cites Andrews (1971), in relation to four basic questions that provide the essential raw material for the SWOT model namely:

- What is the expectancy of stakeholders?
- What might we do?
- What do we want to achieve?
- What can we do i.e. strengths and weaknesses?

The company analysis is further enhanced by identifying capabilities, resources and opportunities worth developing, identifying areas of importance to focus on and identifying ways to build shared expectations amongst stakeholders (Fleisher 2003: 92). The analysis will also assist in determining the most suitable plan for the future of a company and will identify what strategic direction should be taken. The implemented strategy should assist the company to increase business, and build a sustainable competitive advantage over its competitors.

Andrews, as cited in Lynch, (Lynch 2000:562) first identified the importance of connecting the organisation's mission and objectives with its strategic options and subsequent activities.

He went on to argue persuasively that the rational analysis of the possibilities open to organisations was an essential part of strategy development. A SWOT analysis is a useful way of summarising the current status of the organisation. According to Lynch, Andrews is generally regarded as the pioneer of SWOT analysis. In 1971, he was one of the first strategy theorists to formally articulate the concept of strategic fit between the firm's resources and capabilities with the external environment. He argued that this methodology was a sound approach to determine a "niche strategy" (Fleisher 2003:92) – the best way for a firm to use its strengths to exploit opportunities and to defend both the firm's weaknesses and strengths against threats.

According to Wheelen and Hunger (1992) (as cited in Lynch 2000:645), the process of corporate strategy involves five major elements, as shown in Table 2.8, and the SWOT analysis of a company shown in Table 2.9

Table 2.8 Five major elements of Corporate Strategy

Environmental scanning	– the external opportunities and threats
Internal scanning	– the strengths and weaknesses as an organisation
Strategy formulation	– the mission and objectives must be clearly identified
Strategy implementation	– including programs and a budget
Evaluation and control	- to ensure that the strategic process remains on its predicted path

Table 2.9 SWOT Analysis

Internal Strengths	**Internal Weaknesses**
• Market dominance in certain models	• Share weakness
• Core strengths such as cutting experience	• Increase core strengths and key skills
• Economies of scale on certain models	• Plant with high costs
• Low-cost position, through having a tanning operation within the group	• Possible finances and cash flow
• Leadership and management skills. The	• Local management skills and

company has been in the Branaa family since 1890.	leadership growth opportunities
• Financial and cash resource global position good	• Lack of innovation and new ideas
• Manufacturing ability and age of equipment	•
• Innovation processes and results	•
• Business network	•
• Reputation in industry	•
• Differentiated products and processes	•
• Product or service quality	•
• **External Opportunities**	• **External Threats**
• New markets and segments	• Growth too fast
• New products and processes like lamination, perforation and embossing	• New market entrants
• Diversification opportunities, offering lamination options to customers	• Increased competition
• Market growth	• Increased pressure from customers and suppliers, global increase in demands
• Competitor weakness	
• Strategic space	• Substitutes, like vinyl
• Demographic change, new plant	• Low market growth on some models
• Change in political or economic environment, such as MIDP	• Economic cycle downturn
• New takeover or partnership opportunities	• Change in political or economic environment
• Economic upturn	• Demographic change
• International growth	• New international barriers to trade

Much of the work centered on the SWOT analysis originates from Fleisher *et al* (2003: 96), and assists managers to apply a general framework of understanding and managing the environment in which a company operates. It assists management to isolate major issues facing an organization. In order to build a successful SWOT analysis, insightful work is required to place the findings in perspective (as shown in Table 2.9).

Fleisher (2003:95) further argues that an environmental analysis helps the researcher to answer critical questions about an organisation in terms of Table 2.10

Table 2.10 Critical questions regarding environmental analysis

What are the industry's main economic traits?
What are the competitive forces and how powerfully will they affect the organisation?
What factors are creating changes in the dynamics affecting competition?
What are our competitor's assumptions about the changing environment?
What are the environmental factors that are key to the organisation's competitive success?
Is the industry's environment attractive or unattractive both now and in the future?

According to Fleisher (2003:95), an environmental analysis must meet the critical information needs of senior management if they are going to be the decision makers. The information that management needs will change over time and the environmental analysis should reflect such changes. It is believed by Fleisher (2003:95) that management should continuously support environmental analysis because it will regularly assist them to make better decisions. Environmental analysts should focus on identifying existing and potential strengths, weaknesses, opportunities, and threats. Business managers must interpret these results in order to increase the in-depth understanding of its operations. The task of the researcher is to share these findings with management in order to increase the strategic skills that contribute to an effective strategy. Managers can then formulate strategies to address key issues.

> According to Fleisher (2003:96), "a strategic issue is a factor that exist either inside or outside the organization and that is likely to have a prominent and long-term impact on the ability of the enterprise to meet its competitive objectives. Strategic issues, unlike their tactical or operational counterparts, occur

> less frequently, typically impact across the entire organization, and require greater allocations of organizational resources to effectively address.
> It should be emphasized that strategic issues do not just arrive neatly labeled on top of a decision makers' desk. Instead, information derived from SWOT analysis assists in the identification of new technologies, market trends, new competitors, and customer satisfaction trends. These require interpretation and translation, that is, analysis, before they are labeled as strategic issues. Often, managers draw upon their experience to categorize issues as controllable or uncontrollable, as threat or opportunities. The categories then determine how an issue appears to an individual manager, how well it can be sold to other managers, and what action, if any, the firm subsequently takes"

Fleisher (2003:97) argues that a SWOT analysis does not always require a great deal of financial resources and can be done quickly and informally. The SWOT analysis is often used by a company's senior banking official in an informal manner to quickly position the company, without the necessity of extensive information. When dealing with complex situations in a limited amount of time, trying to address all the strategic issues involved often does not pay off. On the other hand, a SWOT analysis provides an effective framework for also identifying critical issues.

An effective SWOT analysis offers an enhanced way of thinking through the range of strategies. It also serves as a means for assessing the companies' core capabilities, competences, and resources. SWOT analysis can be an effective team-building method (Fleisher 2003:97). It provides the evidence to stimulate organizational change. It provides insight into why a company is successful or unsuccessful in carrying out its strategy. It provides a foundation from which to guide further strategic analysis in order for the company to achieve a competitive advantage.

The concern of the researcher is to interpret the data gathered on environmental forces, and to decide what to do in response to them. Interpretation represents a form of judgment and will likely differ between managers. One manager could see the industrial policy changes (as referred to earlier in Chapter 2) which the government has developed to protect or promote the industry, as a market expansion opportunity, while another may view this as a threat because of increasing competition from new rivals.

According to Fleisher (2003:98), if a company attempts to implement only those strategies that build on its strengths and mitigate its weaknesses, it may miss out on the most attractive opportunities that are possible only if the firm stretches itself. The researcher needs to point out that weaknesses are often broader than anticipated and strengths are usually narrower than expected, according to Fleisher

(2003:98), and without testing these assumptions, management could be overly optimistic in their assessment of companies' strengths and opportunities versus the company's weaknesses and threats.

In order to overcome these weaknesses, a manager must adhere to the facts and must not be overly influenced by the dominant "beliefs" held in the company. It is for this exact reason that the research project is undertaken, and it is therefore appropriate that an unbiased analysis is done to ensure biases are kept at a minimum. The researcher will also attempt a rigorous, disciplined, yet creative analysis, and the results could be negatively impacted if an extremely long list indicates that the screening criteria used to separate data and information from strategic issues is not tight enough, if the absence of weighting factors indicates a lack of prioritization, and if short and ambiguously phrased descriptions of each SWOT factor indicate that the strategic implications have not been considered.

2.4.3 STEEP ANALASIS

The STEEP analysis covers the social, technological, economic, ecological and political aspects that have an influence on the competitiveness of the company, and the researcher draws widely on the knowledge from Fleisher, *et al* (2003), and Lynch *et al*, (2000). These factors are not directly influenced by any individual organization. According to Fleisher (2003:269), the organizational environment can be defined as a 'number of forces operating from outside' of the company 'that affects the competitiveness of the environment'. An effective evaluation of the environment is crucial for competitively successful organizations, as the environment is a major determinant of the form and behaviors of an organization. The general environment is broad in scope and has long-term implications. The STEEP method is used to break the general environment up into subcategories.

In accordance with Fleisher (2003:272), the 5 STEEP sectors can briefly be described as follow:

Social: This component refers to the social context in which the organization operates. This would include factors like education, geographical distribution, and lifestyles. According to Fleisher (2003:27), the social component of the general environment describes characteristics of the social context in which the organization exists. Demographics, cultural attitudes, literacy rates, education levels, customs, beliefs, values, lifestyles, the age distribution, the geographic distribution and the mobility of the population all contribute to the social component of the general environment. The pace of change in this sector can often be slow, but its effects are commonly both inexorable and profound. It is important that management analyse, monitor and evaluate this sector's impact in terms of the new strategic directions of the company, and also take a proactive role in helping to develop competitive strategy that builds the company's reputation among its key stakeholders. Ethical norms of a society are elements of its culture that specify in more general ways the behaviors that individuals and organizations expect of one anther, but that are not prescribed by law. As the list of laws implies, many ethical norms (e.g. consumer and worker safety and environmental protection) that are important to a society's long-term future, but are seen as receiving inadequate attention, often become translated into laws.

Technological: Science and technology have a great impact on the environment in which a company operates. It can influence aspects of the environment from the acquisition of raw materials right through to the after market sector. The researcher agrees with Fleisher (2003:272), digital communication, biotechnology, chemicals and energy are a few of the fields in which major technological changes have opened new areas to commercial competition. The technological component of the general environment is compounded by the impact of science and technology in product and process innovation as well.

Economic: This component refers to the distribution of resources by society. Economic variables must be closely monitored and identified as they can affect the competitiveness of the company. Fleisher (2003:273) asserts that the economic component of the general environment indicates the distribution and uses of resources within an entire society. It is important because consumption patterns are largely influenced by economic trends such as balance of payment issues, employment rates, exchange rates, interest rates, inflation rates, credit availability, fiscal and monetary policies, debt, spending patterns, and levels of disposable income. The relationship between strategy and the economic sector is not simply that when the economy improves, all companies will do better. Changes in macro-economic variables can often have broad impacts, yet can affect some economic sectors in ways very different from others. Urgent economic issues can require analysis through the development of custom-designed and expensive economic market research. This makes it even more critical that an organization remain vigilant to economic factors and adjust their decisions and policies accordingly so as to maximize their competitiveness, and to maintain a sustainable competitive advantage.

Ecological: This refers to the physical and biological environment within which an organization operates. The so-called "greening" of the environment now points to the power that this sector can exert on organizational performance. Aspects of the ecological environment covered in a STEEP analysis in relation to the automotive leather industry would include such things as the sustainable development (e.g., bovine leather is a natural product, and one must consider the origin of the product is a live animal), cradle-to-grave product life cycles, recycling, pollution, and biotechnological advances (e.g., genetic advances in agricultural products), among others.

Political/Legal: The views held by Fleisher (2003:273), encompasses government and public attitudes towards specific industries, applicable laws and development initiatives undertaken by government. The nature of competition changes when changes occur in this environment. A company must comply with environmental regulations. Local municipal authorities must approve the new industrial operations in the current location of the plant. According to Fleisher, *et al,* the political component of the general environment relates to government and public attitudes toward various industries, including the leather industry, lobbying efforts by interest groups (one must consider the movement regarding the use of animal fur, ands one can only expect a lobbying group to emerge in favour of banning the use of leather products in the interest of animal protection), the regulatory climate and platforms of political parties among others. The legal component of the general environment consists of laws that members of society are expected to follow. In most nation-states, many legal constraints in the form of public policies and regulations affect an organization's discretionary ability to act. Besides being a large consumer and producer in their own right, governments can actually legislate greater or lesser competition and therefore become a critical focus of the competitive and strategy analyst's efforts in this sector. The accelerated review of the MIDP was promulgated in view of a WTO violation threat. The origin of the review is in fact a politically based agenda, originated by the Australian government. For many companies, such as defense contractors, educational institutions, health care organizations, and not-for-profits, the action and mood of public policy makers are absolutely vital inputs to the competitive strategy development process. Naturally, over time many new laws are passed and old ones rescinded. The nature of competition changes because of both procedural and structural changes from this sector.

Fleisher (2003:280) suggests the following 5-step process is used to analyse the STEEP segments, although originally developed by (Fahey, 1984), and shown here in Table 2.11

Table 2.11 Five step process to analyse STEEP segments

Understand the segment of the environment being analyzed
Understand interrelationships between trends
Relate trends to issues
Forecast the future direction of issues
Derive implications

According to the FAROUT summary developed by Fleisher (2003:282), the STEEP analysis rates medium to high on future orientation, and the analysis needs to be reviewed regularly as industry issues change.

> 'Industries are embedded in a wider macro-environment that can significantly impact the competitiveness of industries and the companies within industries. These are generally considered to be beyond the direct influence of an individual organization'.
>
> Fleisher (2003:269)

An organization requires an environmental analysis to help the company achieve their competitive goals, and to retain a competitive advantage. Naturally, some environmental analysis efforts are better than others, and research has demonstrated that companies in some environments can gain an advantage over their competition based on the quality of their environmental analysis (Miller & Friesen, 1977; Grinyer & Norburn, 1977/78 as cited in Fleisher 2003:277). To be successful, an environmental analysis needs the support and encouragement of management.

Although cited by Fleisher (2003:278), Diffenbach (1983) originally identified that certain problems in environmental analysis tend to fall within several categories, and detailed these further below in Table 2.12

Table 2.12 Environmental Analysis Categories

Interpretation	Management has to define what their environment is, and it can be difficult to interpret the results.
Inaccuracy and uncertainty	Management could experience problems that include inaccuracies in the analytical output, or the presence of too many uncertainties
Short-Term Orientation	Must be careful not to pre-empt the environmental analysis process because they are overly occupied other decision making actions
Lack of Acceptance	Management should accept the value of environmental analysis. The importance of this can be overlooked due to a lack of understanding of its value by senior management, or a difficulty in encouraging line managers to participate, resistance to change, and presumptions among the same managers that they are already experts in the implementation or management of this process.
Misperceptions	Managers must be instructed, or taught how to avoid a narrow, limited, or invalid perception about the environment
Diversified business	Although this can be construed as a threat by managers, management should be assisted to understand the complexity of environmental analysis, as they will have to grasp the implications of numerous environmental and organizational interactive dynamics.

2.4.4 INDUSTRY LIFE CYCLE ANALYSIS

As outlined by Lynch (2000:112), industries pass through four different stages namely, introduction, growth, maturity and decline. The corporate strategy of a company must be adapted as the company moves along the industry life cycle. A company has to determine a strategic way forward in which the company can secure new business contracts. A strategic change is needed within the operational process of many companies and entering the next phase successfully with a strong competitive advantage, will be difficult to implement without effective strategic planning.

Professor Michael Porter from Harvard University Business School has described the industry life cycle as 'the grandfather of concepts for predicting industry evolution' (as cited in Lynch 2000:112). Lynch (2000:113) continues to state that the nature of corporate strategy will change as it moves along the life cycle. In the introductory phase, organisations attempt to develop interest in the product. As the industry moves towards growth, competitors are attracted by its potential and enter the market, and from a strategic perspective, competition increases. As all the available customers are satisfied by the product, growth slows down and the market becomes mature. Although growth has slowed, new competitors may still be attracted into the market: each company then has to compete harder for its market share which becomes fragmented.

The development and implementation of new strategies should address the two consequences of the industry life cycle that have a significant impact on industries namely as shown in Table 2.13

Table 2.13 Consequences of the Industry Life Cycle

Advantages of early market entry	The first company to enter a market has a substantial strategic advantage. Early market entry is risky, but there can also be worthwhile long-term advantages that should be considered in strategic development.
Industry market share fragmentation	Fast growing industries attract new entrants

	leading to fragmentation as each company strives to obtain a market share. Strategies should be adapted in a mature market. It might be necessary to focus on different market segments and not the market as a whole, as segments of the industry may be in different stages of the life cycle, thus requiring different strategies.

The concept of the industry life cycle analysis is often criticized, but Smallwood and Baker (1993:100) presents a short defense, and interesting discussion of the main areas. It is sometimes difficult to determine the duration of certain industry life cycles, some industries also skip certain stages, due to technological changes or developments and the nature of competition may differ in certain stages of evolution. However, it is still considered a useful tool to identify the dynamic factors that determine the industry's evolution.

Drawing on knowledge from Lynch (2000:118), a cyclical market refers to the continuous increase and decline of the size of the market. This leads to a price rise during the upswing of the market and a price fall during the downswing, thus affecting the profits of companies. It also impacts on the market demand in 3 different ways:

- A delay in the replacement demand.
- A temporal halt in purchases.
- A reduced demand due to a depressed national economy.

It should be noted that in a mature market the emphasis shifts to the importance of the company and not the industry, as the company should generate growth opportunities by being innovative and looking beyond existing markets.

It is important to remind ourselves of the argument developed by Baden-Fuller and Stopford (as cited in Lynch 2000:118):

"What really matters in strategy is company activity, not the industry"

They argue that many of the firms in mature industries become incapable of generating growth, so that it appears that the industry is mature. However, they believe that it is misleading to see industries as becoming mature: what really happens is that *"each individual company has become mature"* and lacking in innovation. Nevertheless, there is no denying it is the company that will need to act if it wishes to escape low growth. A company needs to react, and develop a new corporate strategy in order to generate its own growth phase. Especially in mature markets, it is the company that matters, not the industry. Lynch (2000:119) further states that *"industries may appear to be mature, the company should be able to generate new growth opportunities by looking beyond its existing markets"*, and develops new offerings to its customer base. Lynch (2000:124) also argues that the key factors for success are the resources, skills and attributes of an organization that are essential to deliver success in the market place. They are related to the industry and are unlikely to provide differentiation between organisations in the industry. An industry analysis usually begins with a general examination of the forces influencing the organisation. The objective of this study is to help identify the competitive advantage of the company to enable it to defeat its rival companies.

2.4.5 PRODUCT LIFE CYCLE ANALYSIS

According to Fleisher (2003:364), the product life cycle analysis is described as:

"The evolution of sales as a function of time"

Fleisher (2003:364) continues to state that the product life cycle consists of 4 stages. Table 2.14 shows the effects of this.

Table 2.14 Four Stages of the Product Life Cycle

Introduction	Referring to the development of a new product and the introduction thereof into a new market. The automotive industry is fast paced, and continuously improving and changing. New vehicle models enter the market with new leather

	seat covers, and with slow ramp up plans, these new models race into full production capacities very fast.
Growth	Customer awareness generated by extensive promotions by the new models entering the market, leads to quick sales and profits rise. This is particularly true in the motor industry.
Maturity	An increase in sales and profit raise will attract many competitors in a market, resulting in a sales plateau. Many new models and "new-look vehicles" all compete for a share of the same market. New competition is fierce.
Decline	A significant drop in sales of current models occur when new models are launched, and sales form the maturity plateau, resulting in an industry shakeout

Fleisher (2003:364) further describes the product life cycle analysis as follows:

> "The product life cycle generally serves a dual function: a descriptive conceptual framework to aid management in understanding market dynamics and a normative product management framework that recommends specific marketing strategies for each PLC stage in order to maximize profitability over the product's life"

When making use of Fleisher's FAROUT summary (Fleisher 2003:378), the PLC analysis rates highest on timelines, and scores high on resource efficiency, objectivity and usefulness. The theory of diffusion and adoption of innovations developed by Everett Rogers (1962) as cited in Fleisher (2003:365) supports the theoretical rationale for the PLC. The rate of diffusion in new product markets is influenced by:

- The real or perceived advantage of new products compared to existing products.
- The real or perceived risk of adopting new products.
- Barriers such as ideological incompatibility and concern for the initial expenditure made to acquire the old product, which influences adoption of new products.

Fleisher (2003:374) has developed a process for applying the Product Life Cycle technique, which consists of 9 steps.

1. <u>Estimating the potential demand for the product</u>

The first step is to understand the market demand. Market research is required to identify the consumer segment, estimate total demand, understand tastes and preferences, and gauge the strength of potential substitutes. This market research must be analyzed to determine whether and where the market exists to support a reasonable probability of success.

2. <u>Determining a competitive price range</u>

A competitive price point can be reached by expert consultation. Ask internal and external sources to suggest a reasonable price. Engineers, operations managers, and other technical staff can offer insights into the technical feasibility of producing the item at a specified price range. Established distribution channels often offer a rich source of information as to the relative value the proposed new product would offer the consumer compared to competitive offerings. Consumer research can be used to determine a reasonable price range such as barter-equivalent analysis and in-depth interview techniques. These techniques will also give the analyst a rough approximation of price elasticity.

3. <u>Drawing up a sales forecast for a range of prices</u>.

Use the concept of customer value analysis to determine the total value of ownership of the proposed product that includes a breakdown of all of the costs and all of the benefits that the product bestows over its life span. This customer value analysis should then be repeated for competing products. Use this analysis as a backdrop to compare the relative competitiveness of the new product as compared to potential and incumbent products at the various price points.

4. <u>Considering the possibility of competitive price cuts</u>.

If a product will not compete directly with any substitutes or will only encroach on a small portion of the incumbent's established market, the probability of a competitive price decline will be lower. If, however, the new product is presumed to displace a significant portion of the incumbent's market share, a competitive price cut can be expected and must be incorporated into any pricing and costing decisions to ensure future product profitability.

5. <u>Developing a fundamental market strategy for the growth stage</u>.

A fundamental decision must be made at this point in the analysis about the selection of the targeted market segment. Incorporating the analysis from the previous four steps, the firm must decide to pursue a skimming or market penetration strategy, as shown in Table 2.15

Table 2.15 Skimming vs. Penetration Strategy

SKIMMING STRATEGY	**PENETRATION STRATEGY**
• New Product is truly unique	• New product shares many qualities with established products so that attribute superiority is small
• Total market demand is forecasted to be small	• High price elasticity of demand
• Demand is price inelastic	• Experience curve effects will probably be realized
• Cross-elasticity of demand is low	• Total market demand is expected to be large
• Promotional elasticity is high	• Steep experience curve
	• High risk of competition

6. <u>Defining the level of aggregation between product class and brand</u>.

The level of aggregation between product class, form, or brand is vital to PLC analysis. While each level of aggregation will offer the company unique insights, practical application criteria usually override theoretical concerns. Product life cycle research has shown a tendency to favour product form as the best level of aggregation. Product class usually does not reveal any trends because it includes too many different product markets. In addition, product class shows trends only over a very long time period. Abel (1980) as cited in Fleisher (2003:375) offers a helpful definition of a product that may help the company:

> "A product is the application of a particular technology to satisfy a specific need or desire of a customer segment. In the final analysis, the final selection of product definition depends in large part on the company's judgment"

7. <u>Forecasting turning points in the economy wide business scale</u>.

At this stage PLC analysis starts to distinguish itself as separate from traditional marketing strategy. In PLC theory, each cycle stage requires radically different strategies. While there are many business and economic forecasting techniques (e.g., research), all of these techniques extrapolate from past data. They are useful only for short-term forecasting, and then only as long as the independent variable assumptions do not radically change. Further, they are most useful for predicting turning points in the economy wide business cycle. Several helpful methods of forecasting these turning points are readily available (Dean, 1950), 1976; Moyer, 1981) as cited in Fleisher (2003:376), and shown in Table 2.16

Table 2.16 Forecasting turning points in the PLC

Declining prices	This indicator of weakening prices will manifest itself in several ways, such as reduced retail prices or the increasing prevalence of discounting, which are often informally negotiated. The important distinction for turning-point analysis is to detect when the magnitude of discounts changes substantially.
Increasing Sales Resistance	A weakening market will require an increasing sales effort such as more sales people, higher frequency of calls, and more attention addressed to individual consumer needs, and increased time that products spend on market floors or shelves.

Increasing Inventories	Declining market demand usually precedes excessive inventory accumulation. While macro-economic measures of inventory build-up will indicate a general slowing of economic growth, the analyst needs to focus on inventory build-up in the relevant product market
Media Analysis	Turning points are often predicated by negative press and editorial commentary regarding the product.
Increasing product Standardization	Decreasing attribute differentiation may signal a turning point into the maturity stage, as commoditization initiates
Common Production Processes	One sign of a maturing market may be the uniform adoption of a particular production process, indicating an increasing focus on benefiting from experience effects across the industry

8. Adapting company strategies according to the applicable stage.

New strategies for each product should be developed and adopted in order for the company to remain with a competitive advantage.

9. Be on the lookout for new product life cycles.

Innovative technology assists a company to recover from the decline stage of the product life cycle.

2.4.6 PORTER'S 5 FORCES MODEL

The well known business model was structured and presented by Professor Michael Porter of Harvard University Business School, and is used to identify 5 basic forces that influence an organization. The views held by Lynch (2000:125) regarding Porters 5-forces model leads us to the objective of the analysis, which is "to investigate how strategies should be formed to ensure the development of opportunities, while at the same time protecting it from threats of competitors". Competitive rivalry forms the essence of such an analysis. The basic principles of this model can be applied to commercial companies and the model is most essential in analyzing the competitive industry environment in which the company operates. In order for the directors of a company to make an important strategic decision, they must clearly understand the complete competitive environment in which the company operates.

According to Hitt, Ireland and Hoskisson (2003:55),

> "An industry is a group of firms producing products that are close substitutes. In the course of competition, these firms influence one another. Typically, industries include a rich mix of competitive strategies that companies use in pursuing strategic competitiveness and above-average returns. In part, these strategies are chosen because of the influence of an industry's characteristics"

Hitt, *et al,* (2003:55) further claims that; compared to the general environment, "the industry environment has a more direct effect on the firm's strategic competitiveness and above-average returns". The intensity of industry competition and an industry's profit potential (as measured by the long-run return on invested capital) are a function of five forces of competition: the threats posed by new entrants, the power of suppliers, the power of buyers, product substitutes, and the intensity of rivalry among competitors, as shown in Figure 2.3

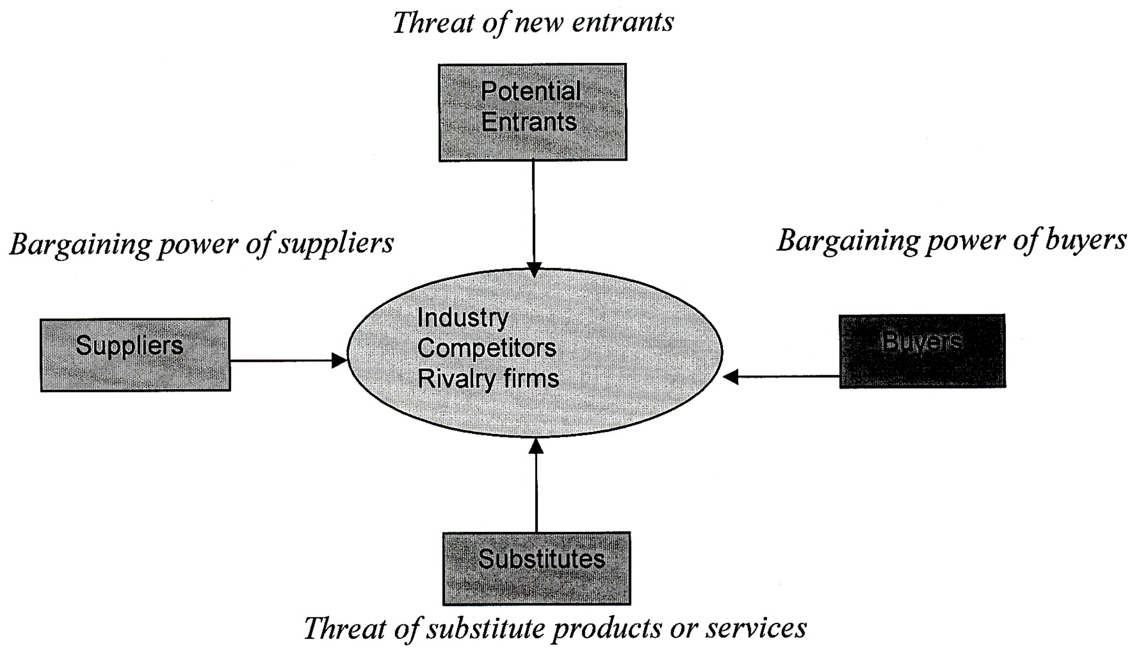

Figure 2.3 PORTER'S 5 FORCES MODEL

Porter (as cited in Lynch 2000:126) further describes these forces in Table 2.17

Table 2.17 Porters' Five Forces

Suppliers	Price premiums, delivery schedules and quality have a big influence on the finished product, and determine the strength or advantage of suppliers in a market
Buyers	The negotiating power and leverage points with regards to quality and price determine the customer's advantage in a market.
New entrants	They are considered a threat if a market can easily be penetrated and if they have a competitive edge like lower costs.

Substitutes	Technological advances and breakthroughs pose a threat to existing products
Competitive rivalry	Strategies must be developed and adapted to adequately protect a company against this threat

Lynch (2000:131) continues with highlighting some criticism of the Five Force Model. Despite the criticism, he concludes that it still remains a useful tool for competitive strategic analysis of a company. When analysing the competitive industry environment, it usually begins with a general examination of the forces influencing the organisation. The objective of such a study is to develop a competitive advantage and to enable the company to defeat rival companies.

The objective of this analysis is to investigate how a company needs to reform its strategy in order to develop opportunities in its environment and protect itself against competition and other threats. The basic assumption of the model is that all organisations will wish to benefit and protect their own interests. Companies wish to protect themselves in an essentially competitive environment.

> "Industry analysis provides a structural analysis and outline of an industry – its participants and characteristics. The objective of this process is to identify the profit potential of an industry; uncover the forces that would harm profitability; driving the profit potential; protect competitive advantage by defending against the forces that would harm profitability; extend competitive advantage by favorably influencing these forces; and proactively anticipate changes in industry structure"
>
> Craig.S Fleisher (2003:60)

The view is held by Fleisher (2003:72) that "industry structure fundamentally impacts strategic choices". Important direction for selecting and subsequently managing the strategy is required by the management of BZA. Each competitive force should be constantly monitored for their impact on the current strategy and the opportunities they represent for extending the companies sustainable competitive advantage.

2.4.7 E-S-P Paradigm: Analyzing the role of Government

As outlined by Kennedy (1990), "politics has been an important driver of industrial growth". It is believed by Lynch (2000:157) that government can introduce and develop initiatives to benefit industries. One such government initiative which this research report covers is the MIDP program of South Africa. These initiatives affect organizations and industries, such as the automotive leather seat industry. The macroeconomic conditions, and economic conditions at industry level and various other areas that are influenced by government, must be analyzed and addressed when forming new strategies. At government policy level, politics and economics are inextricably linked. Corporate strategy is not concerned with forming such policies but does need to understand the implications of the decisions taken. Government can stimulate national economies, encourage new research projects, impose new taxes and introduce many other initiatives that affect the organisation and its ability to develop corporate strategy. The E-S-P paradigm focuses on the impacts of the Environment (E), the System (S) and the Policies (P) on the organisation.
The following areas are of importance when analyzing the role of the government:

- The government system of the relevant country.
- The policies.
- The environment of the nation.

Current Government Incentives which are available to the automotive leather seat industry in South Africa and to BZA are shown in Table 2.18

Table 2.18 South African Governments Automotive Industry Incentives

Motor Industry Development Program – MIDP
Productive Asset Allowance Scheme – PAA
Foreign Investment Grant – FIG
Small Medium Enterprise Development Program - SMEDP
Duty Free Allowance. Customs and Excise Schedule 3 (317.06) and 4 (470.03) – Rebate of Duty program.

As mentioned earlier in the chapter, politics has been a great driver for industrial growth. The view is held by Lynch (2000:159) that much of this growth has come through a combination of wars, the search for power and the exploitation of resources. Corporate strategy will need to take into account the *"opportunities and the moral dilemmas"* that may arise from these changes, and adjustments. For example, the problems in China in the early 1990s did not stop major Western companies investing in that country in the years that followed; indeed, some may argue that such wealth creation is a contribution to overcoming the difficulties. Any corporate strategy that does not take into account the history and momentum of politics is ignoring an essential element of the environment. In relation to the view that Lynch (2000:160) holds, corporate strategy should anticipate that politics will continue to be a part of the equation. Companies may benefit from policies such as higher state subsidies, better education and international trade incentives, but may be hindered by measures such as new laws restricting competition, new taxes on profits, limited investment in infrastructure. Corporate strategists need to be acutely aware of the benefits and problems associated with government policies. It will certainly wish to press for policies that it regards as beneficial during the formation and implementation of strategic decisions. Influencing major political decisions is part of corporate strategy. As long as this is done openly and with integrity, there can be no objection by those with other interests.

Lynch (2000: 161) also argues that governments have some direct control over the economy of a country. It is easier for organisations to launch a growth or survival strategy when the national or international economy is showing steady growth with low inflation. Conversely, if economic decline is likely, the company might be well advised to take a more prudent view of strategic expansion. It follows that the macro-economic conditions – that is, economic activity at the general level of the national or international economy – surrounding an organisation are an important element in the development of corporate strategy.

Whilst drawing on the knowledge of Lynch (2000:161), in practice, when exploring corporate strategy, many organisations, both large and small, use their own managers to make economic forecasts, buy in reputable forecasts or simply use published forecast material. The forecasts are usually made on key macro-economic issues, as shown in Table 2.19

Table 2.19 Key Macroeconomic Issues

Gross domestic product (GDP), total and per head of the population
Growth in GDP
Retail and consumer price indices
Trade flows in imports, exports and the balance of payments
Private sector share of GDP; agricultural share of GDP
Foreign direct investment (FDI), total and as a percentage of total investment.

(Adapted from Lynch 2000:161)

Managers will be familiar with these areas. Lynch (2000:161) further states that for companies operating in more than one country, these forecasts may usefully be estimated for all the major countries in which they operate with the addition of currency fluctuation as another important variable. Lynch (2000:161) argues that *"in addition to changes in the macro-economic conditions, organisations will also be concerned with government changes in the economic environment, specific to the industry in which they are involved"*

- The rising prices of petrol and international environmental concerns have impacted on car engine design in the car industry; in turn, this has meant that companies have altered their model ranges and changed their plant investment strategy. Some companies have coped better than others.
- Changes in government policy regarding the accelerated review of the MIDP program.

Lynch (2000:162) cautions that there can be no generalised list of items, nor any common body of theory in the industry environment that will always influence strategy. The impact that economic changes will have on corporate strategy will vary with the organisation: essentially, the demand and cost structures of the industry and the company will be the prime determinants.

Table 2.20 shows the types of issues that are usually worth considering, according to Lynch (2000:162);

Table 2.20 Typical Economic Issues

Government tax and legislative activity
Specific impact of macro-economic growth on an industry
Cyclicality of demand and investment in an industry
The level of derived demand.
Raw material supplies and costs
Industry negotiations on wages and conditions of work

2.4.8 SUSTAINABLE COMPETITIVE ADVANTAGE (SCA)

"Your most unhappy customers are your greatest source of learning". *Bill Gates*

In order for a company to maintain a competitive advantage, it must regularly analyze competitors and adopt strategies that will ensure a sustainable competitive advantage over an extended period of time. Price, quality, brand or range and service levels must be analyzed, but some of the advantages might be imitated by the competition and will only lead to temporary relief.

> The process of strategic management is coming to be defined, in fact, as the management of competitive advantage – that is, a process of identifying, developing and taking advantage of enclaves in which a tangible and a preserved business advantage can be achieved."
>
> Stephen South, corporate planning director at Clark Equipment (USA)

Lynch (2000:156) asserts that sustainable advantages should be tested against the following criteria:

- It should be "*sufficiently significant*" in order to influence customers.
- It should be able to withstand attacks by competitors as well as environmental changes or challenges.
- Functional advantages for the organization must be linked to customer benefits.

Lynch (2000:152) also wrote that the "*main reason for analysing competitors is to enable the organisation to develop competitive advantages against them, especially advantages that can be* *sustained over time"*. Lynch further continuous that *"sustainable competitive advantage involves every aspect of the way that the organisation competes in the market place – prices, product range, manufacturing quality, service levels and so on"*.

Lynch (2000:152) argues that the real benefits come from advantages that competitors cannot easily imitate, not those that give only temporary relief from the competitive battle. To be sustainable, competitive advantage needs to be *"more deeply embedded"* in the organisation – its resources, skills, culture and investment over time. It is believed that for many strategists, the development of sustainable competitive advantage lies at the core of corporate strategy development. Professor Michael Porter wrote persuasively about its importance in the 1980s in two classic strategy texts – *Competitive Strategy* (1980) and *Competitive Advantage* (1985) – which have influenced both academic and industry developments.

If an advantage is sustainable, then it cannot be quickly copied by others. It is likely that it will have taken some time, possibly years, for the organisation to have developed the advantage. A prescriptive approach, requiring a sustained period of development, is therefore likely to be required. In developing sources of sustainable competitive advantage, in seeking the advantages that competitors cannot easily copy, it is necessary to examine not only the competitors, but also the organisation itself and its resources. It is important for the company to identify some possible sources of advantage as a starting point for developing the companies' strategy. These sources are shown in Table 2.21 and were adopted from the work of Lynch (2000:154)

Table 2.21 Sources of Advantage for Developing Strategy

Differentiation	This is the development of unique features or attributes in a product or service that position it to appeal especially to a part of the total market. Branding is an example of this source
Low costs.	The development of low-cost production enables the firm to compete against other companies either on the basis of lower prices or possibly on

	the basis of the same prices as its competitors but with more services being added.
Niche marketing	A company may select a small market segment and concentrate all its efforts on achieving advantages in this segment.
High performance or technology	Special levels of performance or service can be developed that simply cannot be matched by other
Quality	Some companies offer a level of quality that others are unable to match
Service.	Some companies have deliberately sought to provide superior levels of service that others have been unable or unwilling to match.
Vertical integration	The backward acquisition of raw material suppliers and/or the forward purchase of distributors may provide advantages that other cannot match.
Synergy.	This is the combination of parts of a business such that the sum of them is worth more than the individual parts – that is, 2 + 2 = 5. This may occur because the parts share fixed overheads.
Culture, leadership and style of an organisation	The way that an organisation leads trains and supports its members may be a source of advantage that others cannot match. It will lead to innovative products, exceptional levels of service, and fast responses to new markets.

Lynch (2000:156) believes that ultimately, there is *"no single route"* to achieving sustainable competitive advantage; it is a combined effort by management, directors and workers on the shop floor. If a sustainable competitive advantage does exist in a company, such advantages are shown in Table 2.22 as outlined by Lynch (2000:156):

Table 2.22 Elements of a Sustainable Competitive Advantage

Sufficiently significant to make a difference	Modest advantages that hold no real benefits to the customer or the organisation are unlikely to be persuasive.
Sustainable against environmental change and competitor attack	The market as a whole may move forward in terms of technology or tastes. Equally, competitors may be able to copy advantages developed by the organisation. In both cases, these advantages are not sustainable.
Recognisable and linked to customer benefits	An advantage needs to be translated from a functional advantage inside the organisation – for example, low costs – into something that the customer will value – for example, low prices. Advantages that cannot be linked in this way may ultimately prove to have no persuasive and competitive edge

According to Hitt, *et al,* (2003:118),

"Business-level strategies are intended to create differences between the firm's positions relative to those of its rivals".

Hitt (2003) further states that to position itself, the firm must decide whether it intends to perform *activities differently* or to *perform different activities* as compared to its rivals. Thus, the firm's business-level strategy is a deliberate choice about how it will perform the value chain's primary and support activities in ways that create unique value. Value is delivered to customers when the firm is able to use competitive advantage resulting from the integration of activities. Bowman & Helfat (1999:133-156) argues that "*favourable positioning*" is important in that the "universal objective of all companies is to develop and sustain competitive advantages".

According to Hitt (2003:119), firms choose from among five business-level strategies to establish and defend their desired strategic position against rivals, as shown in Table 2.23

Table 2.23 Five Business Level Strategies

Cost leadership
Differentiation
Focused cost leadership
Focused differentiation
Integrated cost leadership/differentiation

Each business-level strategy helps the firm to establish and exploit a competitive advantage within a particular competitive scope.

When selecting a business-level strategy, firms evaluate two types of potential competitive advantages, namely:

1. Lower cost than rivals,
2. or the ability to differentiate and command a premium price that exceeds the extra cost of doing so

Porter, ME (1994:423-461)

Hitt (2003:119) further explains that having a lower cost derives form the firm's ability to perform activities differently than rivals, and being able to differentiate indicates the firm's capacity to perform different activities.

According to Hitt (2003:122), a cost leadership strategy is "*an integrated set of actions designed to produce or deliver goods or services with features that are acceptable to customers at the lowest cost, relative to that of competitors*". Cost leaders concentrate on finding ways to lower their costs relative to those of their competitors by constantly rethinking how to complete their primary and support activities to reduce costs still further while maintaining competitive levels of differentiation.

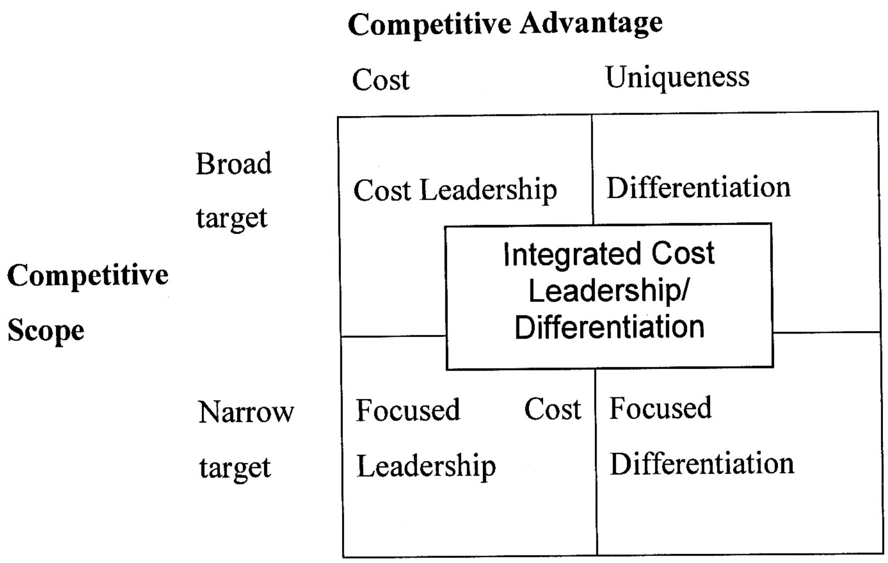

Figure 2.4 Five Business Level Strategies

Hitt (2003:122) argues that cost leaders also carefully examine all support activities to find additional sources of potential cost reductions. Developing new systems for finding the optimal combination of low cost and acceptable quality in the raw materials required to produce the firm's goods or services is an example of how the procurement support activity can facilitate successful use of the cost leadership strategy. Having the low-cost position is a valuable defense against rivals. Because of the cost leader's advantageous position, rivals hesitate to compete on the basis of price.

According to Professor Porter,

> " a low-cost leader in an industry has built and maintained plant, equipment, labour costs and working practices that deliver the lowest costs in that industry"
>
> Porter, ME (1985)

The differentiation strategy, according to Hitt (2003:126), is "*an integrated set of actions designed by a firm to produce and deliver goods at an acceptable cost, and that customers perceive as being different in ways that are important to them*"

Hitt (2003:126) argues that "continuous success with the differentiation strategy results when the firm consistently upgrades differentiated features that customers value, without significant cost increases". Because a differentiated product satisfies customers' unique needs, firms following the differentiation strategy are able to change premium prices.

> "For customers to be willing to pay a premium price, a firm must truly be unique at something or be perceived as unique"
>
> Porter, Competitive Advantage, (as cited in Hitt 2003:127)

Hitt (2003:127) claims that the ability to sell a good or service at a price that substantially exceeds the cost of creating its differentiated features allows the firm to outperform rivals and earn above average returns. Hitt continues that rather than costs, a firm using the differentiation strategy always concentrates on investing in and developing features that differentiate a good or service in ways that customer's value. Overall, a firm who is using the differentiation strategy seeks to be different from its competitors on as many dimensions as possible. The less similarity between a firm's goods or services and those of competitors, the more buffered it is from rivals' actions.

As outlined by Hitt (2003:130), the focus strategy is "*an integrated set of actions designed to produce or deliver goods or services that serve the needs of a particular competitive segment*".

Hitt (2003) further states that firms choose a focus strategy when they want their "core competencies to serve the needs of a particular industry segment or niche at the exclusion of others". Firms can create value for customers in specific and unique market segments by using the focused cost leadership strategy or the focused differentiation strategy.

According to Porter (as cited in Lynch 2000:567), neither a low-cost leadership strategy nor a differentiation strategy is possible for an organisation across the broad range of the market. For example, the costs of achieving low-cost leadership may require substantial funds which are not available. Equally, the costs of differentiation, while serving the mass market of customers, may be too high: if the differentiation involves quality, it may not be credible to offer high-quality and cheap products under the same brand name, so a new brand name has to be developed and supported. For these and related reasons, it may be better to adopt a focus strategy.

In conclusion,

"A firm's strategic competitiveness is enhanced when it is able to develop and exploit new core competencies faster than competitors can mimic the competitive advantages yielded by the firm's current competencies".

Hitt, *et al*, (2003:141)

2.4.9 COMPETITOR ANALYSIS

The view is held by Fleisher (2003:144) that existing and potential competitors in the market place should be identified and then analyzed according to their strengths and weaknesses. Strategies should be formed to protect a company as well as to provide them with opportunities to gain a competitive advantage in the automotive leather seat market.
Fleisher further asserts that competitor analysis has four main purposes namely,

Table 2.24 Competitor Analysis

Identifying or forecasting competitor's future strategies and plans
Predict competitors most likely reaction to competitive initiatives
Compare competitor's capabilities with its strategies
Understand a competitors weaknesses

(Adapted from Fleisher 2003:144)

In addition, the FAROUT summary developed by Fleisher (2003:160) rates this technique as effective with regards to future orientation, accuracy, objectivity and usefulness.

According to Hitt (2003:66) competitor intelligence is "*the set of data and information the firm gathers to better understand and better anticipate competitors, objectives, strategies, assumptions, and capabilities*". Intense rivalry creates a strong need to understand competitors. In a competitor analysis, a company needs to understand the following dimensions:

Table 2.25 Four Competitor Dimensions

What drives the competitor
What the competitor is doing and can do
What the competitor believes about the industry
What the competitors' capabilities are

(Hitt 2003:66)

It is believed by Hitt (2003:66) that information about these four dimensions "helps the firm prepare an anticipated response profile for each competitor". The results of an effective competitor analysis helps a company understand, interpret, and predict its competitors' actions and responses. Useful data and information combines to form competitor intelligence. The company gathers intelligence not only about its competitors, but also regarding public policies in countries across the world. Hitt (2003:66) argues that intelligence about public policies "provides an early warning of threats and opportunities emerging from the global public policy environment, and analyzes how they will affect the achievement of the company's strategy"

According to Fleisher (2003:144), competitor profiling provides a comprehensive picture of the strengths and weaknesses of current and potential rivals. This analysis provides both an offensive and defensive strategic context through which to identify opportunities and threats.

Attanasio (1988:16-19) suggests that corporate strategy has passed through four phases during the 200 years of its existence as a separate body of principles and practice, as shown in Table no 2.26

Table 2.26 Four phases of Corporate Strategy

Phase 1	Companies operated explicitly on financial planning premised on functional efficiency in order to meet annual budget goals
Phase 2	Companies used forecast-based planning through which they extrapolate the past to make inferences about the future. This new technique allowed the development of longer budget periods

	and resource gap analysis.
Phase 3	Firms began to pursue strategic management based on externally orientated analysis. During this phase, the predominance of tactical management yielded to the concept of strategic analysis of trade-offs.
Phase 4	Rather than waiting to react to future challenges when and if they occur, firms are now beginning to position themselves in order to "create the future

(Adapted from Fleisher 2003:145)

Competitor intelligence became increasingly apparent, and Michael Porter rang the clarion call of change for competitor analysis in two of his very influential works, one on competitive strategy in 1980 and the other on competitive advantage in 1985. His essential premise was that since strategy is concerned with finding a unique and differentiated customer value relative to rivals, competitor analysis is quite properly a central component of strategy.

Since Porter's pioneering work in the area of competitor analysis, many others have contributed to this important area of strategy. Today, as more and more firms enter phase 4, competitor profiling has become an integral component of the strategic process needed to 'create the future'. According to Fleisher (2003:146)

> "Porter was one of the first writers to propose a formal and systematic process through which to gather information about competitors. His models have a decided proactive orientation. The forward-looking stance of competitor profiling is intentional, as its primary design is to predict the future strategic actions of rivals. That is, the models encourage the analyst to use current and past information about rivals in order to predict the future strategic moves that a competitor may pursue in response to the firm's own strategies, the strategies of other firms in the industry, or changes in the competitive environment exogenous to business strategies"

Fleisher (2003:149) further argues regarding the weaknesses and limitations of competitor analysis that "the primary criticism of competitor profiling relates to the temptation for firms to make it the allencompassing cornerstone of competitive strategy. The irony of this is that in attempting to become an industry leader, the firm will eventually become a follower if it defines leadership too closely related to current rivals"

Fleisher (2003:149) also states that constantly referencing the firm's strategy to rivals based on the idea of strategic groups or inter-industry competition will eventually blind the firm to innovative approaches of potential rivals in delivering superior customer value from outside the industry. Another related weakness of competitive profiling refers to the copycat nature of outpacing the competition. Critics suggest that such a strategy prevents a competitive advantage from becoming sustainable. Firms should focus solely on customer value in search of innovation, and not imitation.

In applying the technique of competitor profiling, Fleisher (2003:150) has developed nine stages to assist an organisation such as BZA to successfully profile its competitors, as shown in Table 2.27

Table 2.27 Process of Competitor Profiling

1. Determine who your competitors are.
2. Determine who your potential competitors may be.
3. Decide upon the information that is required about these rivals.
4. Build a competitor analysis capability in order to secure this information.
5. Conduct a strategic analysis of the gathered information.
6. Present the information in an accessible format.
7. Ensure that the right decision makers get the right information on a timely basis.
8. Develop strategy based on the analysis.
9. Continually monitor rivals and continually scan for potential rivals.

(Fleisher 2003:150)

2.4.10 BCG GROWTH SHARE MATRIX

Drawing on the knowledge form Lynch (2000:175), the balance of an organization's product portfolio should regularly be analyzed. This method makes use of the relative market share, as well as the market growth rate for each product. This technique is useful as a starting point in the analytical process. According to Lynch (2000:176) the portfolio is divided into four categories namely:

- Stars
- Cash cows
- Problem children
- Dogs

Fleisher (2003:30) holds the view that the BCG matrix "allows a multi-business firm to compare the merits of its individual business units in order to determine appropriate market strategies for each business. The business units are evaluated based on the attractiveness of the industry in which they compete and their relative competitive position. Generic strategies are then recommended depending on the position of the individual business unit in the portfolio matrix".

According to Lynch (2000:174), the majority of companies offer more than one product or service and many serve more than one customer. Lynch (2000:175) holds the view that "there are good strategic reasons for this: to be reliant on one product or customer clearly carries immense risks if, for any reason, the product or service should fail or the customer should go elsewhere. Decisions on strategy usually involve a range of products in a range of markets"

Lynch (2000:175) asserts that "when an organisation has a number of products in its portfolio, it is quite likely that they will be in different stages of development: some will be relatively new and some much older. Many organisations will not wish to risk having all their products in the same markets and at the same stages of development". According to this argument, the key strategy is to produce a balanced portfolio of products – some low risk but dull growth, some higher risk with future potential and rewards. The results can be measured in both profit and cash terms.

As outlined by Lynch (2000:175), the BCG matrix is "one means of analysing the balance of an organisation's product portfolio". According to this matrix, two basic factors define a product's strategic stance in the market place, as mentioned in Table 2.28

Table 2.28 Factors defining a products position in the market place

Relative market share	For each product, the ratio of the share of the organisation's product divided by the share of the market leader. This is important because in the competitive battle of the market place, it is advantageous to be larger than rivals: this gives room for maneuver, the scale to undertake investment and the ability to command distribution
Market growth rate	For each product, the market growth rate of the product category, and is important because markets that are growing rapidly offer more opportunities for sales than lower growth markets. Rapid growth is less likely to involve stealing share from competition and more likely to come from new buyers entering the market. This gives many new opportunities for the right product.

(Lynch 2000:175)

Lynch (2000:175) explains the four distinct areas of the growth-share matrix as follows in Table 2.29

Table 2.29 Four Distinct areas of the Growth-Share Matrix

• *Stars.* Those products with high market shares operating in high-growth markets. The growth rate will mean that they will need heavy investment and will therefore be cash users. However, because they have high market shares, it is assumed that they will have economies of scale and be able to generate large amounts of cash. Overall, it is therefore asserted that they will be cash neutral – an assumption not necessarily supported in practice and not yet fully tested.	• *Problem children.* Products with low market shares in high-growth markets. Such products have not yet obtained dominant positions in rapidly growing markets or, possibly, their market shares have become less dominant, as competition has become more aggressive. The market growth means that it is likely that considerable investment will still be required and the low market share will mean that such products will have difficulty generating substantial cash. Hence, on this basis, these products are likely to be cash users.

• *Cash cows.* Those product areas that have high market share but exist in low-growth markets. The business is mature and it is assumed that lower levels of investment will be required. On this basis, it is therefore likely that they will be able to generate both cash and profits. Such profits could then be transferred to support the stars. However, there is a real strategic danger here that cash cows become under supported and begin to lose their market share.	• *Dogs.* Those products that have low relative market shares in low-growth business. It is assumed that the products will need low investment but that they are unlikely to be major profit earners. Hence, these two elements should balance each other and they should be cash neutral overall. In practice, they may actually absorb cash because of the investment required to hold their position. They are often regarded as unattractive for the long term and recommended for disposal.

According to Lynch (2000:177), the general strategy is to take cash from the cash cows to fund stars and invest in future new products that do not yet even appear on the matrix. Cash may also be invested selectively in some problem children to turn them into stars with the others being milked or even sold to provide funds for elsewhere. Typically in many organisations, the dogs form the largest category and often represent the most difficult strategic decisions. As outlined by Fleisher (2003:45), the use of his FAROUT rating summary, shows that the BCG matrix scores high on resource efficiency and timeliness. This means that an organisation like BZA can make use of the BCG matrix with limited resources (it is easy to use), and quickly (relative market share can easily be estimated).

2.5. Foreign Direct Investment in South Africa

> '... it is in the nature of FDI that statistical information on it cannot be comprehensive enough to allow fine analytical experiments" (Agarwal, 1980:763)

In relation to this research work, it is necessary to comment on FDI, since a foreign multi national company is investigating the possibility of investing in the South African automotive leather industry. A short commentary on FDI in South Africa would be deemed sufficient for the purposes of this paper.

South Africa receives low levels of foreign capital in the form of direct investment, although one important factor contributing to new investment is former South African multi nationals now operating from the UK. According to a research paper written on FDI in SA by the Centre for Research into Economics and Finance in Southern Africa (CREFSA), the UK has been the main source of EU investment, with Germany also being a significant partner. New investments from the US and Japan in the automobile industry contributed to FDI since 2000. Efforts to promote sector specific opportunities are needed. According to an article published on the South Africa Info web page, dated 05 April 2006, "The value of mergers and acquisitions (M&A) involving South African companies climbed by R103-billion, or 63%, from R165.5-billion in 2004 to R269.1-billion in 2005, according to Ernst & Young's latest review of M&A activity worldwide. Crucially, according to Business Day, R57-billion of this was "inward investment" - an amount equal to the foreign direct investment (FDI) in South Africa of the previous five years combined - helping the country to edge past India for the first time ever in the FDI stakes"

In another article published on 15 December, a joint survey by the World Bank and Department of Trade and Industry has found the investment climate of South Africa to be "favourable" in comparison to that of other African countries, and other middle-income countries throughout the world. Conducted by Cape Town-based Citizen Surveys, the survey asked 800 South African enterprises to assess specific factors that shape opportunities and incentives for firms to invest productively, create jobs, and grow. These were benchmarked against countries at the same level of development, such as Malaysia, Kenya, Brazil, Poland and China.

"On many dimensions, South Africa has a good investment climate," the World Bank said. Legal protection of property, labour productivity, low tax rates, reasonable regulation, a low level of corruption and good access to credit were seen as factors contributing to the country's investment climate. Firms also appear to be particularly concerned about at least four areas: skills and education of workers, labour regulation, exchange rate instability, and crime.

Other factors influencing FDI, included productivity, with South Africa being more productive than other countries where World Bank surveys have been conducted. According to the survey, the country's labour productivity is far higher than in Senegal and Kenya, the most productive low-income countries in sub-Saharan Africa. South Africa's labour productivity also compared favourably with other middle-income countries such as Lithuania, Brazil, Poland, and Malaysia - all of which, other than Brazil, have higher per capita income. Productivity was also found to be over three times higher than in China, although slightly lower than in the most productive cities in that country. Other factors included labour costs and skills, and labour regulation. Despite South Africa's relatively strong macroeconomic performance - GDP growth and moderate inflation - macroeconomic instability was a serious problem. This is due to exchange rate instability. This is particularly problematic for exporters, who are paid in dollars or euros, but must pay their workers and suppliers in rand.

According to Roberts (2004), in his work "Investment in South Africa – a comment on recent contributions", growth has consistently found investment to be a significant determinant, especially investment in infrastructure, machinery and equipment (Easterly & Rebelo, 1993; De Long & Summers, 1993; Temple, 1998). The South African government placed investment at the core of the Growth, Employment and Redistribution (GEAR) macroeconomic strategy (Department of Finance, 1996). Yet, few direct mechanisms were put in place to increase investment. It was largely assumed that macroeconomic stabilisation would in itself encourage investment. An understanding of what drives investment is therefore of critical importance.

A further variety of indicators analysis the investment climate in South Africa, namely,

- The economic growth and local market size.
- Openness to trade
- Macro economic stability

- Institutional environment
- Labour markets
- Infrastructure
- Role of FDI in SA's development strategy
- Policies that are in place by the South African government to attract FDI to the country

2.6 CONCLUSION

"What I do best is share my enthusiasm". Bill Gates

In order to contribute to achieving the strategic intent of a company, management must have a clear idea of the strategy, understand how their activities contribute to achieving successful outcomes and acknowledge the impact of their actions on the organisation. To achieve this comprehensive understanding and to create ownership, management and employees must participate in strategy formulation (Colenso, 1998). To facilitate this, visionary, participative leadership is required. Strategic management furthermore involves the inter-related processes shown in Figure 3.3

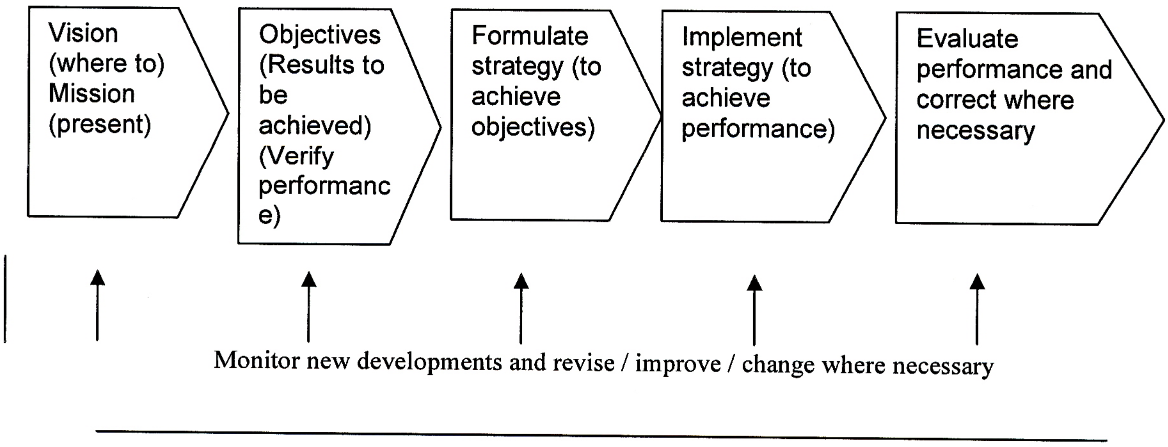

Figure 2.5 The Strategic Management Process (Adapted Thompson and Strickland, 2001: 7)

The various strategic management tools have been designed to assist the strategic process. Organisations should use the most appropriate method for their situation. It is Organisations should select the most appropriate tools or combination of tools, for the respective organisation. It is necessary to link daily activities to strategy by carefully considered organisational design.

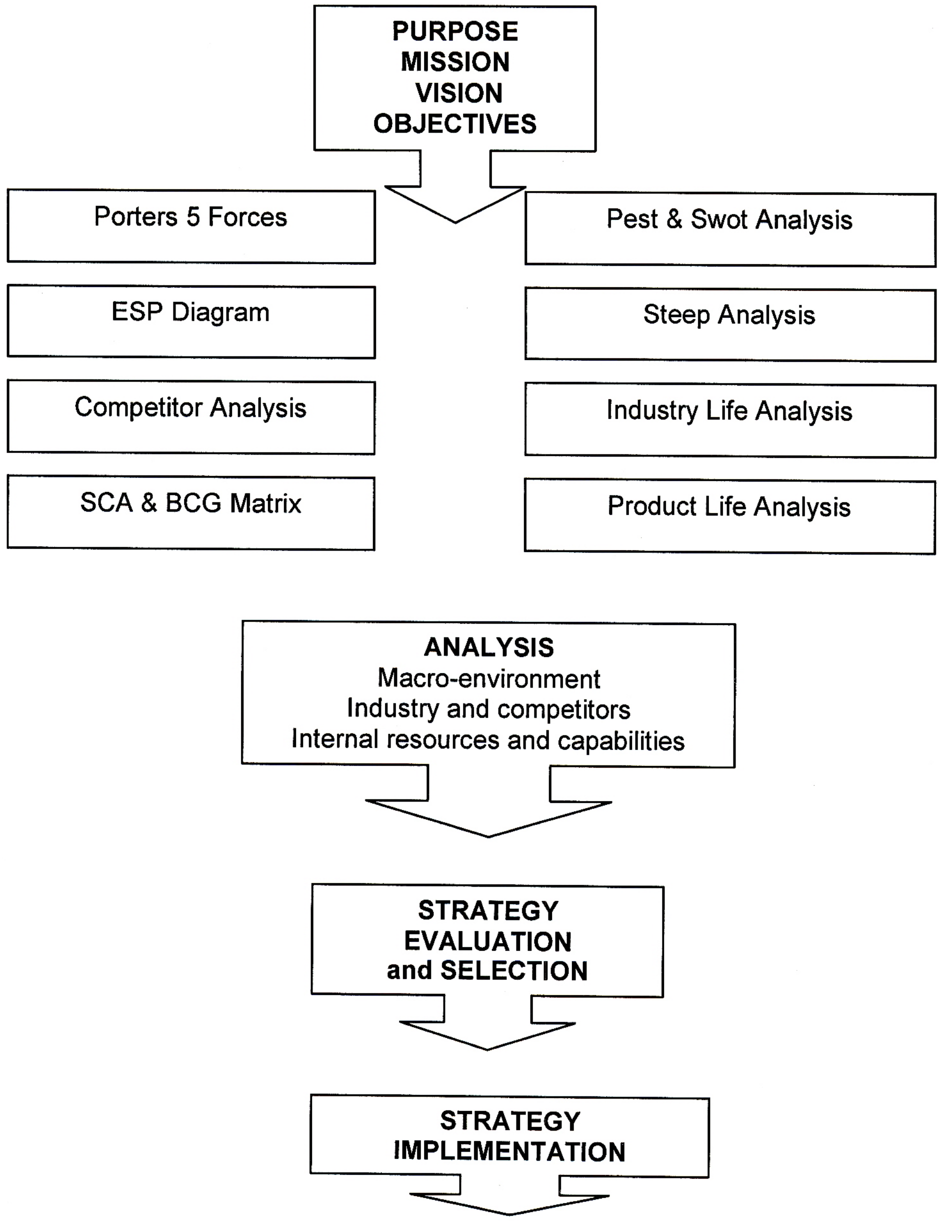

Figure 2.6 Model for Strategic Management

(Adapted from Manion G, 2003)

The strategic concepts are shown in Figure 2.6, and illustrate the flow of the strategic management process in order to achieve successful outcomes.

It is evident from the discussion in this chapter that whether or not a formal planning process is followed, it is essential for organisations to consider all the factors that have a bearing on their operation.

CHAPTER 3 CASE STUDY

3.1 INTRODUCTION

Globalisation is a modern, new world, 21st Century phenomenon with economic opportunities (and possible threats) beyond measurement. Globalisation offers new business challenges to all industries, across international borders. Declining trade and investment barriers, mainly driven through the World Trade Organization, are primarily responsible for new trade development between previously separated national markets. These markets have developed into huge global marketplace. Another driver of globalisation is the fast growth and development technology such as microprocessors, the Internet and e-mail.

International business, and globalisation in effect, is not only dominated by large multi-nationals such as Sony, Ford or General Motors, but there is a tendency for Mini-Multinationals to develop. Substantial opportunities exist for smaller enterprise to direct their future growth strategies towards the global marketplace.

The aim of this research project is to determine a successful corporate strategy for BZA in terms of the future orientation of the company. Through the successful implementation of this strategy, the company BZA will be able to position itself as a market leader in the cutting of automotive leather seat covers in South Africa. The researcher will aim to prove that the proposed strategy is in line with the organizations basic direction.

BRANAA is such a company. A family owned business since 1890; the Branaa family has built and developed a Uruguayan company into a global multi-national company with operations in 5 continents.

As the English mercantilist writer Thomas Mun put it in 1630:

> "The ordinary means therefore to increase our wealth and treasure is by foreign trade, wherein we must observe this rule: to sell more to strangers yearly than we can consume of theirs in value"

Considering this fundamental shift in the world economy, the strategic focus of the Group of BRANAA Companies (hereafter referred to as Branaa Global) is to continue to strategically adjust to the global needs of the automotive leather seat industry in which they operate. It s under this "strategy umbrella", that this study is undertaken.

3.2 INTRODUCTION TO BRANAA

3.2.1 A GLOBAL PERSPECTIVE

Branaa Global is group of companies operational on 5 continents. It is a multi-national operation with the international company head quarters situated in Montevideo Uruguay. The head quarters are based in the same operational location as Curtiembre Branaa SA (Sociedad Anoniem) (CBSA). CBSA is the main supplier of raw materials (finished bovine hides) to BZA. CBSA has the same board of directors as BZA, and BZA management reports to CBSA.

CBSA in Uruguay is a leather manufacturing plant, (tannery) and consists of the tanning operations (from purchasing raw hides and tanning these into crust), to the finishing section (where crust is further reworked into finished hides by adding painting and embossing techniques as specified by the final customer). For this purpose, bovine leather is mainly sourced and used.

The main business of Branaa Global is to manufacture high quality automotive leather, and to supply the automotive industry with leather car seats in the concentrated automotive regions. As a downstream process, Branaa Global have developed various strategically positioned cutting facilities, where the already finished bovine leather hides are cut according to the automotive seat templates, ready to be sewn by third party participants within the automotive seat value chain.

BZA is one of these cutting facilities, situated in Pretoria, South Africa. The complete leather requirement for this cutting facility is imported as finished bovine leather hides for use in the automotive leather seat industry from CBSA.
BZA started their local seat cutting operation in 1997 in a small factory in Rosslyn, Pretoria, and in early 2001 relocated to much larger premises in Waltloo, Pretoria. This new site is strategically situated directly opposite Ford South Africa, Motor Vehicle Assembly plant. Furthermore, also directly across is located the seat sewing plant, contracted to Ford SA, namely Johnson Controls. BZA secured certain leather seat options for specific Ford and Mazda models, and the relocation later proved to be a strategic strength in terms of continuous supply to Ford & Mazda, and new model ranges added to the supply list of BZA. This strategic location also developed into the supply of certain Nissan models for the local market, through the same sewing plant, Johnson Controls, who later implemented JIT supply to the Original Equipment Manufacturers (OEMs).

The BZA Pretoria operation currently operates from a 8000 square metres factory, and employs 85 permanent employees and make use of temporary staff at peak cutting times, pushing the staff compliment up to 125 employees when required.

Figure 3.1 Branaa South Africa: Cutting operation

The BZA operation is managed by a Uruguayan General Manager who oversees the operational requirements of BZA on a daily hands-on basis. He is supported by a team of local managers. CBSA receives daily operational feedback, through teleconferencing, and weekly reports through video conferencing facilities in all the plants.
The CBSA operation in Montevideo Uruguay, currently operates from a 35 000 square metre factory, and employs 720 people. CBSA currently supplies 100% of the finished bovine leather requirement of BZA, and BZA purchases 20% of the production capacity of CBSA.

In addition to these facilities, Branaa Global also consists of various operational plants, which are discussed under Branaa Group Structure.

Figure 3.2 CBSA, Montevideo Uruguay. Company Headquarters

3.2.2. <u>Branaa – Group Structure</u>

As shown in Figure 3.1, the Board of Directors, are referred to as the "DG" and consist of 3 Directors, namely:
MB (Marcel Branaa), RG (Roberto Garcia), and JLR (Jose Luis Rodriques). Each director has taken a direct responsibility over different aspects of the operations. MB is responsible for the wet tanning processes and leather finishing process in Uruguay, Argentina and the proposed new finishing plant in

South Africa. RG is responsible for overseeing the cutting facilities in Uruguay, Germany, Mexico, America and South Africa. JLR is the financial director.

In addition to these responsibilities, each director has also taken a management interest in the central process of the organisation which has been split between the automotive team and the furniture team. The central processes of which the directors have taken a personal interest are also known as the following business functions: Commercial, Logistics, Purchases, IT, HR, Finance and others.

Group Structure

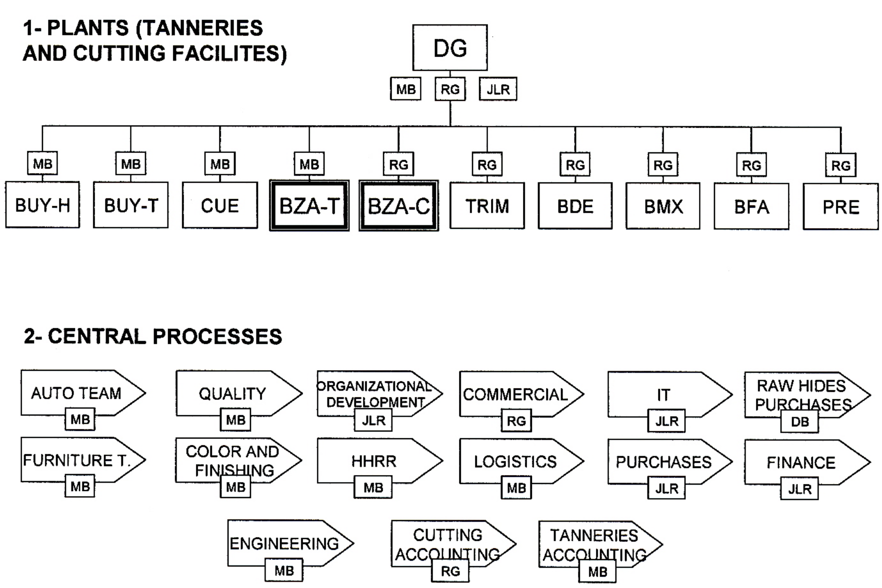

Figure 3.3 Group Structure and Directors Control
Source: Rodrigo Cabanas (CBSA, 2006)

- Branaa Trim. A similar automotive leather cutting and sewing facility, situated in Montevideo, Uruguay. Trim currently operates from a 16 000 square metre factory, and employs 300 people.

- Branaa Argentina. A leather tanning operation, known as Cuesset, situated in Magdalena, Argentina. Cuesset currently operates from a 14 000 square metre factory, and employs 180 people. The Cuesset operation is mainly considered a wet end process, and supplies the CBSA tannery with a product known as crust, where it is further processed in to the final product – called finished bovine leather.

- Branaa Mexico (BMX). A similar automotive leather cutting facility as BZA, situated in Saltillo, Cuahullo, Mexico. BMX currently operates from a 4 000 square metre factory, and employs 85 people. BMX is strategically located in order to gain entrance into the North America automotive leather seat market.

- Branaa Germany (BDE). A similar automotive leather cutting facility as BZA, situated in Waldfischbach, Pirmasens, Germany. BDE currently operates from a 7 800 square metre factory, and employs 120 people. BDE is strategically located in order to serve the large automotive cluster market in Germany, and mainly supplies leather seat sets to OEMs such as BMW and AUDI.

- Branaa USA. Further to these plants, Branaa Global operates a distribution leather warehouse, mainly for furniture leather supplies from Hickory, NC, USA. The company is also known as Friitala-Branaa of America, where Friitala is a well known brand in the furniture retail market. Friitala-Branaa currently operates from a 5 000 square metre factory, and employs 28 people.

Branaa Global Sales Office is situated in Michigan, Detroit. The heart of the automotive market in the United States. Here, Branaa has a sales representative who is promoting the high quality automotive leather products to prospective US customers.

Branaa Global uses a hands-on approach in managing all of its operations globally. In the same sense, the responsibilities and managerial authority of the Directors of Branaa Global Group of Companies, is practically divided in order to maximize stringent controls over the operations and the central processes involved on the business. The Directional control over the plants (Tanneries and Cutting facilities), is effectively displayed in Figure 3.3

3.3 RECENT INDUSTRY DEVELOPMENTS

In order to better understand the automotive leather seat industry in South Africa, it is necessary to fully understand the industrial policy which the government has developed to protect or promote the industry.

BZA, as a successful role player in the leather seat industry is bound by regulations set by the MIDP, and needs to operate within the boundaries set by policy makers. Industrial policy in South Africa in the past decade has been broadly aimed at encouraging investment, technological improvements, exports, and small, medium and micro enterprises.

The motor vehicles and parts and accessories sectors (inclusive of the leather seat market) stands out as having recorded high rates of output growth and investment, but is not particularly capital-intensive. Drawing on industry related experience and knowledge of the researcher, one concludes that the leather seat cutting operation is more labour intensive, and since capital equipment has not yet been successfully developed to substitute the manual cutting processes, the industry should remain more labour intensive and less capital intensive for another few years. Although these machines are in development in Europe, and should reach South Africa within a few of years, they would never completely substitute human labour, since leather is a natural product with many natural defects (which machines can not yet successfully identify). The development of the leather sector has been strongly influenced by the Motor Industry Development Program, and in particular influenced by the MIDP Accelerated review, which is discussed further in this chapter.

According to Machaka and Roberts, 2003, (as cited by Black 2002) "the best performing sectors in terms of value-added growth from 1994 to 2004 were furniture, leather, other chemicals, basic non-ferrous metals and basic iron and steel. In broad terms, liberalization and increased trade appear to have reinforced the existing patterns of comparative advantage based on natural resources, cheap energy and previous government support".

Considering the industrial policy, there were some relative success stories, such as plastic products, furniture and leather products, whose performance needs to be understood through a wider understanding of, for example, the performance of leather products is intimately related to the effects of government's MIDP and on decisions of motor vehicle assemblers or OEMs.

Notwithstanding these performance patterns within the manufacturing industry like the automotive seat sector, firms are not taking advantage of local actions to develop industry skills and advancements in technological capabilities. This is partly due to generally weak industry organizations and a lack of co-ordination by government, but also by a lack of commitment by industry role players, and management of these organizations to identify the needs, and to work closer together with government. Manufacturing sectors characterized by many small and medium firms can be expected not to be as effective in organizing themselves and lobbying government as those dominated by a few major players. The researcher is of the opinion that the automotive leather market is dominated by a few major role players, and a closer *Ubuntu-relationship* could easily be promoted to develop a collective industrial relationship in the leather industry. A greater onus rests on government to address the bias towards resource and capital intensive industry. South Africa has an enormous opportunity to develop a home-based industry where disadvantaged people could become successful producers of small leather items, and compete successfully against a country like China.

The importance of industry management leadership in taking the necessary steps to build production capabilities at the industry level through establishing strong institutions and taking policy steps to realize collective gains is highlighted by the experience of the auto industry. It is the one manufacturing sector with a specific government program designed to support restructuring and improve competitiveness in the industry– in the form of the MIDP, introduced by government in 1995. The export-import complementation program at the heart of the MIDP requires ongoing increases in local content exports to be able to make the same level of duty free imports. This 'moving target' has induced the major OEMs to collectively examine steps to improve the competitiveness of input sectors in the medium term, and included in this competitiveness target is the automotive leather seat industry. The incentive program offered through the MIDP in terms of the automotive leather sector proved very successful, until the South African government received a challenge from the Australian Government, claiming an unfair advantage was offered under WTO rules.
During a recent meeting held between a South African delegation led by Dr Alistair Ruiters of the International Trade Administration Commission of South Africa (ITAC), and an Australian delegation, solutions were explored for the challenge received in view of South African leather exports to Australia under the terms of the MIDP program. A view was held by the Australian delegation that

the benefits derived from the MIDP program offered to the South African leather industry stakeholders are impacting negatively on the leather industry of Australia. The meeting was aimed specifically at minimizing the negative impact it had on the Australian industry.

Deliberations ended with the two sides coming to an agreement known as a "Record of Understanding". Since all agreements constitutes a give and take, or win and loose, situation, it is possible to assume that ITAC had to give up something.

A platform meeting held during September 2004 confirmed this assumption. Present at the meeting were many of the South African stakeholders directly involved in the automotive leather sector. These role players were informed by Dr Alistair Ruiters of the agreement reached and during this platform meeting all the relevant shareholders were informed of the concerns of the Australian delegation and Dr Ruiters significantly identified that fundamental changes were expected in respect of the current structure of the MIDP program.

The following allegations (Table 3.1) were made and some issues (Table 3.2) were raised during this meeting:

Table 3.1 Allegations made by Australian Government regarding MIDP

The South African MIDP program has fundamental WTO violations
The MIDP program is an unfair trade instrument, and is not complying with WTO regulations
The MIDP benefits offered under the "local content" scheme is an unfair subsidy under the WTO rules

Table 3.2 Issues raised by Australian Government regarding MIDP

Bi-lateral discussions agreement to review and check compliance.
Australia requested immediate trade relief, in terms of all South African automotive leather exports to Australia with accelerated relief in the future.
South Africa to review exports
General MIDP scheme to change to become WTO compliant.
MIDP Review undertaken regarding Leather Industry only. No effect on other automotive components or catalytic converters
Australian claimed "illegal MIDP subsidy" led to severe job losses in the Australian leather industry,

specifically at Howe – an industry role player in Australia.
Australia claimed South Africa pays third world wages in "sweat shop-like" automotive industry. This perception was indicated in the Australian media and is now also the perception of the Australian public. South African delegation appalled by the suggestion, and promoted SA as efficient, effective and productive.

Possible suggestive remedies were not formally agreed to, but were suggestions during the bi-lateral discussions are shown in Table 3.3

Table 3.3 Possible suggestive remedies

No MIDP benefit paid to South African exporters on all leather exports to Australia from Quarter 1 2005.
No existing contract will be affected until April 2006 regarding the Import Rebate Credit Certificates (IRCC) issued.
Request for 2 bi-lateral forums per annum between South Africa and Australia.
Re-instrument the MIDP program to become WTO compliant.
Downscaling of MIDP benefit and change to MIDP Policy Parametres.
No further WTO reaction from Australian government for 2 years.
Immediate exclusions of MIDP benefits regarding the exports to Australia.
Australia to offer inputs and experience and to participate in the review of the MIDP for it to become WTO compatible.

It was made very clear during these discussions that the workings and success of the motor industry development program in South Africa is a "commercial secret", and that the successes experienced in the automotive industry is due to competitive advantages within the SA economy, and that these successes are not only due to government assistance.

3.4 THE MOTOR INDUSTRY DEVELOPMENT PROGRAM - MIDP

3.4.1. History of the MIDP

The Motor Industry Development Program (MIDP), introduced in 1995, was intended to run for 5 years, but after some recommendations during the midterm review, the program was extended until 2007. The MIDP is widely regarded as a major success of South Africa's post-apartheid trade and industry policies. The program has been modified and/or extended several times, and is currently scheduled to continue until 2012. A Department of Trade and Industry (DTI)-funded review, the third since the program's inception, is now under way and is considering further adjustments to and possible extensions of the program after 2012.

The goal of the program is summarized in Table 3.4 (Info doc C/2003)

Table 3.4 Goals of the MIDP program

Provide high quality and affordable vehicles and components for the local and international markets.
Increase employment through increased production.
Stimulate economic growth.
Increased volume of locally produced vehicle for export.
Upgrade automotive industry.
Facilitate global integration process

The program comprised four principal elements as shown in Table 3.5 (Info doc C/2003)

Table 3.5 Four Principle elements of the MIDP

A gradual reduction in import duties on both vehicles and components
An export-import complementation scheme under which vehicle and components exporters can earn tradable IRCCs to offset duties on imported vehicles and components. Import rebates are earned through the export of eligible exports, and the value of the IRCC is calculated using a formula measuring the Eligible Export Performance (EEP).
Access to the standard duty drawback program for exporters, under which all import duties paid on components and intermediate inputs used in exported vehicles and components can be rebated, and

A duty free allowance on imported components of 27 percent of the value of vehicles produced for the domestic market.

Some the objectives already achieved under the program are shown in Table 3.6 (Info doc C/2003)

Table 3.6 MIDP objectives already achieved

Increased vehicle and component exports.
Increased investment in automotive industry.
Job growth.

According to Roberts (2004:27), the MIDP stands out as an industrial policy strategy developed on the basis of understanding the dynamics of a specific industry and the levers that would change the decisions of large firms. The MIDP, however, largely came into being because government had committed to a tariff liberalisation program which saw tariffs on completely built up cars being reduced from over 100 per cent at the beginning of the 1990s to 35 per cent in 2004. The industry was faced with a direct and immediate threat which motivated the development of a concrete industrial policy framework and engagement with government for its adoption.

Roberts (2004), further comments that the MIDP is essentially an import-export complementation program which works because the tariff protection on built-up vehicles, while being reduced, is still significant. To encourage local manufacturers to reduce the number of models produced locally and to increase the scale of production to reap scale of economies, the program allows for the duty free importation of built-up vehicles for the equivalent export of locally manufactured vehicles and components. There is a sliding scale in operation where in order to import a built-up vehicle a progressively larger amount of exports are required.

Roberts (2004) claim that, as a result, most assemblers focus on one model, and import the others. An example of this is the BMW Rosslyn plant, where only the 3-series models are built for the local market and export market. Other BMW models such as the 5- and 7 –series are imported completely built up. In addition, efforts went into identifying components which could be competitively manufactured in South Africa. Indeed, some firms only focused on component exports in order to earn credits for the import of built-up models.

Roberts (2004) continues that the second notable element of MIDP is that it has been adapted to evaluations of its impact. The components exported have been dominated by three product groupings – catalytic converters, seat leather and aluminium wheels (although engine parts overtook wheels in 2003). These are very capital-intensive products, (although the leather cutting process is less capital intensive than the leather sewing operations) and the catalytic converters value derives from their platinum content. It thus amounted to an additional reward to exporters of platinum. The MIDP was revised to place a cap on the credits that could be earned from the export of catalytic converters.
In accordance with Roberts (2004), increased demand from the motor industry, competitive rivalry and economies of scale, explains the good performance of automotive leather products, in terms of seat covers, door inserts and steering wheel covers, with this increased demand for high quality seat leather enabling the industry to grow despite the collapse of the local footwear sector.

As previously commented by the researcher, an independent review of MIDP economic benefits and costs is long overdue, and after the comments from the Australian Government, it is recommended that such an exercise be conducted and that its findings be taken into account in making any changes to the program and in considering MIDP as a model for more general industrial policy strategies in South Africa. The DTI is currently in the process of an accelerated review of the MIDP.

Flatters (2005) views the MIDP in a more positive light and in his work comments that the MIDP has until now provided time and generous assistance for the motor industry to adjust to liberalisation of the domestic automotive market. The industry has responded with major internal restructuring. There have been substantial investments, accompanied by rapid growth of both exports and imports.
Flatters (2005) continues with the background of the MIDP, and states that the MIDP was initiated to assist the motor industry to adjust to South Africa's reintegration into the global economy. The MIDP was designed to help the industry to increase its competitiveness in the new post-apartheid trade policy environment.

According to Flatters (2005) the incentives in respect of components apply only to those components sold directly to OEM manufacturers. This excludes from the program after-market components, a sector in which South Africa might have some regional and maybe even global comparative advantage.

Flatters (2005) also mentions that the MIDP has been expanded to include a direct investment subsidy in the form of a "Productive Asset Allowance" (PAA) that provides import duty credits equal to 20 percent of the value of qualifying investments.

3.4.2 The MIDP and the Automotive Leather Industry

This research report concentrates only on the MIDP in relation to the automotive leather seat industry, and does not analyze the economic impacts of any of the other programs and policies. It focuses on the impact of local content contributions in BZA as a leather cutting facility, and also considers the local content contributions of the sewing plants, in order to determine the benefit offered to the OEMs on the exported value added product. The MIDP is believed to create substantial incentives for foreign direct investment, and this research report aims to determine how Branaa Global could adjust its strategic position to expand further into the South African economy. Branaa Global will invest in an upstream South African operation in terms of a leather finishing plant, in order to increase the local content portion of its leather supply to the OEMs, and through this directly increase the net financial benefit offered to the OEM under the MIDP scheme. This new leather finishing facility will strategically place BZA in a position to increase production capacities, and BZA will be in a position to increase its service to the export and the domestic markets.

Flatters (2005:4), concludes that the MIDP works by subsidizing the production of vehicles and OEM components for both the domestic market and for the export market. The aggregate amount of subsidy provided to the motor industry is large. The values of the MIDP subsidies given to individual producers and investors are complex. This value has changed over time as import duties on vehicles and components have fallen and as some of the parameters of the program, most importantly the value of IRCCs granted per Rand of vehicles and components exported, have been reduced.

According to Flatters (2005:7), recent investments in the South African motor industry have been made to produce two joint products – vehicles (or components) and IRCCs. The high value of the IRCCs means that investments can be quite uncompetitive in the manufacturing business and still highly profitable. This is because losses from vehicle and/or components production can be offset by high-value IRCCs. He argues that a detailed examination of the cash flows of the investments demonstrates that factories might better be viewed as producers of IRCCs rather than vehicles or components. In terms of contribution to profits, IRCC production is really their core economic activity.

Flatters (2005:12) then continues to comment that components that are exported, have been dominated by a narrow range of products, for example leather seat covers and catalytic converters. Leather seat covers are technologically similar to up-market garments, with the main operations involving cutting and sewing. Flatters (2005) argues that leather is mostly sourced locally, but due to raw material shortage of hides in the South African market, a large portion of locally produced leather seats depend on imported hides. BZA is one the role players who import 100% of the finished bovine leather hides, and uses this to cut and supply export requirements of the OEMs. Other inputs such as the electrical heating elements in seats for foreign markets are also imported. A large portion of the local leather used in seat covers would almost certainly be utilized in footwear or other similar products if it were not used for the export purpose in the form of seat covers. The researcher agrees with Flatters (2002) that the large demand in leather for the automotive market does have an effect on the footwear industry. Representatives of the domestic footwear industry have complained about difficulties in sourcing leather as a result of the need to compete against the subsidized producers of automotive leather products.

In accordance with Flatters (2005), the researcher agrees that the MIDP is highly complex and administration and compliance are difficult and costly. Even senior financial officers of major firms in the market admit to an incomplete understanding of the requirements and procedures involved. Partial descriptions of the program can be found on the NAACAM (National Association of Automotive Component & Allied Manufacturers) and NAAMSA (National Association of Automobile Manufacturers of South Africa) web sites, but complete official descriptions are difficult to find anywhere, including the DTI. Most policy makers and administrators, not to mention potential investors and producers, have at best only a very weak and incomplete understanding of the values of the incentives created, their economic costs and who bears them.

Flatters (2005) comments that vehicle assemblers participating in the program face special Customs procedures that require them to remit duties on a quarterly basis, based not only on their own imports, but also those of their local OEM components suppliers, and, of course, claims in respect of duty credits and duty-free allowances earned under the program. A small group of industry consultants, including a number of former DTI officers, has developed to assist investors through the maze of MIDP requirements.

As previously mentioned, and Flatters (2005:13) confirms this, it is the view of the Australian Government that export subsidies such as those provided by MIDP are forbidden by the WTO. Procedurally, however, a complaint needs to be lodged by a WTO member in order for any action to be taken. Since the MIDP has been designed for the benefit of global OEM suppliers who can source vehicles from South Africa with the assistance of MIDP subsidies and use the resulting IRCCs to earn more profits from sales in the South African market, they have had no particular incentive to launch an action against the South African subsidy.

Recently, however, an Australian components producer facing competition from South African leather seat exports and in danger of losing contracts to local OEM manufacturers decided to issue a challenge. After an initial attempt to cover it up and negotiate a "private" settlement, the DTI acknowledged the problem and the search for a solution is one of the major drivers of the current MIDP review (Flatters 2005:13).

WTO compliance is an issue that should be addressed in the design of any trade or industrial policy. However, whether we can "get away" with a policy under WTO rules is certainly not sufficient to ensure good policies. The first question in evaluating the MIDP or any alternative is whether it is in the national economic interest of South Africa. For a clear set of recommendations to continue the MIDP after 2012, to maintain investor benefits at no less than their current levels and to ensure that they are WTO-compliant. Lacking alternative guidance from any other sources, reports suggest that the Review Task Team has accepted this as its primary mandate (Flatters, 2005:14).

Flatters (2005:14) continues that under the leadership of the DTI, the Review Task Team has pursued a busy schedule of data collection and meetings with stakeholders, primarily associations and firms in the domestic motor industry. It has invited participation, in the form of attendance at meetings, by a range of other government departments. But it appears to have no clear plans for analyzing the broader economic impacts of the program and alternative sectoral strategies.

Flatters (2005:15) conclude that the MIDP was designed to help an inefficient, high cost and uncompetitive motor industry. It has done so with very generous subsidies. The aim of the MIDP was to assist the industry to achieve international competitiveness. Firms that have already or will achieve this goal by 2012 will not need further subsidization, and there can be little justification for a continuation of the program that has been given to foreign shareholders over the past decade.

Flatters (2005:15) is concerned that a continuation of subsidies to firms that cannot compete without them will generate even more economic waste, paid for by South African consumers and taxpayers. Workers losing jobs in uncompetitive firms that might close if MIDP subsidies were sharply reduced could be compensated at a fraction of the cost of the subsidies. The MIDP, and in particular the export-import complementation program, was modeled on a similar program in Australia that was designed, as in South Africa, to assist the local industry to convert itself from a high cost import substitution structure to an outward oriented one in which firms could reduce costs by producing fewer models at higher scales of output. The program provided a duty free allowance of 15 percent (compared with South Africa's 27 percent) and import duty rebate credits similar to those in South Africa. It ran from 1984 to 2000, by which time the import duty on vehicles had been reduced from 55 to 15 percent. In 2000 the export subsidy was replaced by a general duty credit arrangement that provided credits of 25 percent of the value of production times the rate of duty, whether for export or the domestic market, and it was announced that the import duty would be reduced to 10 percent at the end of 2004.

It is the recommendation of Flatters (2005:17) that such subsidization of an "infant industry" or "industry in transition" cannot be permanent. Among the policy scenarios considered should be a set of parameters for the final transition of the industry to a normal economic environment. In evaluating alternatives, the review must look beyond producers and examine the national interest, including that of consumers, taxpayers, and workers in downstream industries that have suffered as a result of high prices and restrictions on used car imports. At a broader level, the government should reflect on the lessons from the MIDP for the future of sector-specific industrial policies in South Africa.

According to Black (2002), the actual assembly costs for local operations such as BMW and DaimlerChrysler are well below in-plant costs in their respective German plants. Where these South African operations incur significant cost disadvantages is in the area of inbound and outbound logistics. This is a function of high transport costs and long distances to foreign markets as well as high levels of imported content. Higher volumes in the region of 100 000 units per annum would enable higher local content and the resulting reduction in logistics costs would enable South African plants to compete without any support.

Black (2002) acknowledges that achieving higher levels of local content is not easy. Given the very large investments involved, volumes of 40-50 000 units per annum do not justify the investments required to raise local content above a level of approximately 60 percent. Considering this acknowledgment by Black (2002), the researcher would agree that BZA is in exactly this situation. A large foreign direct investment is required in order for the company to increase its local content portion. The only reasonable measurement to justify such an investment is to determine to required rate of return (ROR) on the project. The investors would require a certain premium for their market risk, and for BZA to achieve this ROR, there would have to be a presence of economies of scale – something that can only be achieved when the amount of business appointed by the OEMs are large enough. The fact is BZA has to make the investment on the assumption that it would secure new business. It is a case of the chicken and the egg. There are no guarantees from the OEMs that additional business would be successfully sourced or allocated to BZA.

Black (2002) continues that while a wide range of components are exported, much of the expansions have been in a small range of products such as catalytic converters, and automotive leather. Some of these components could be described as 'peripheral' in the sense of being relatively minor components, which have high raw material content and not being particularly complex in terms of incorporating large numbers of sub-components. The researcher agrees that this statement is true in terms of the leather seat industry. Specifically the cutting plants only add labour, overheads, and profits to the raw material cost. Components such as heater panels are only added in a downstream process through the sewing facilities. The industry supplying leather seat covers amounted to 12.9 percent of total component exports in 2001. It supplies the bulk of BMW's global requirements and is an important supplier to a number of other foreign vehicle manufacturers. BZA supplies to BMW and Audi as export customers and to Nissan, Ford and Mazda as local market customers.

Black (2002) further comments that, during the Mid Term Review of the MIDP, automotive leather was regarded as the sub-sector that was dominating component exports and enabling assemblers to rebate duties on large scale component imports. Exports in this category have now declined in relative terms partly due to a shortage of local leather. For this reason, imported finished bovine leather hides are sourced in South America and even Russia, by Branaa Global, and imported substantially by BZA. The import of crust as an upstream raw material process by BZA, would increase the local content portion of the South African operations, and increase MIDP benefits to the OEMs.

Another key question raised by Black (2002), concerns the sustainability of the large investments that have been made. This is exactly the case with BZA. A large investment needs sustainable long term business contracts. The automotive leather industry is volatile, and the supply chain management side of the industry is most crucial. Firms are quick to argue that they will relocate if benefits are seriously reduced. The second largest component export, automotive leather, is a very labour intensive process. However in this sector, the leather value chain (raw hides – wet blue hides – semi finished hides – finished hides – cutting – sewing – pulling – fitting process) has become increasingly embedded with the development of world class capabilities ranging from tanning of high quality leathers to JIT logistics. BZA is currently supplying automotive leather seat covers to JCI Pretoria, who in turn supplies Ford and Mazda on a JIT basis. Sustainability and long term business contracts under an MIDP program of reducing assistance, is a function of other factors such as cost competitiveness, which depends on the cost of labour, materials and logistics (Black, 2002).

Black (2002) concludes that the export growth in components such as leather, has, in fact, not been all that unusual, and compares well with levels of exports into the EU from other countries such as Hungary, Poland and Turkey. Components exports such as automotive leather and wiring harnesses are, in fact, very labour intensive and this was a factor in encouraging the location of these sub-sectors in South Africa. BZA experiences the same phenomena, in the sense that the cutting costs per square metre of leather in the Germany plant (BDE), is substantially higher than the BZA plant (even though productivity in the BZA plant is below average when compared to the other Branaa Global facilities). In the same sense, BZA costs are much higher than the cutting facility in Uruguay (TRIM). TRIM is currently the most cost effective operation in the Branaa Global Group. Considerations on the sustainability of supply under the current MIDP structure are shown in Table 3.7, and include:

Table 3.7 Sustainability of supply under the current MIDP structure

Industry structure and comparative advantage	Low volume production and complexity. Firms have developed expertise in low volume, flexible production, but this counted for little in the international market place, which requires cost minimization and the achievement of optimal performance from a world scale plant
Demonstration effects	The MIDP encouraged BMW to embark on a major vehicle export program. Credibility to the system of incentives showed that South African firms could successfully build and export high technology vehicles.
Investment determines competitiveness	There is a significant shift in global production to middle income countries, which have lower cost bases. Vehicle assembly in South Africa is highly competitive in terms of actual plant costs, but in the medium term higher levels of local content will be required to offset high logistics costs. This is the strategy of BZA, to do a complementary investment in order to secure sustainable growth, and this research aims to convince the shareholders of this proposed strategy.

Adapted from Black (2002)

3.5 THE PRODUCTIVE ASSET ALLOWANCE

The Productive Asset Allowance (PAA) was added to the MIDP to encourage investments in the industry. These proposed investments include both foreign direct investment and local expansion projects. Exporters registered to qualify as eligible exporters earn import rebates in order to offset duties on imported vehicles, either CKD or CBU, and vehicle components.

3.6 STRATEGIC ANALYSIS TOOLS

3.6.1 PEST Analysis

According to Lynch (2000:5), "corporate strategy is concerned with an organisation's basic direction for the future: its purpose, its ambitions, its resources and how it interacts with the world in which it operates. Every aspect of the organisation plays a role in this strategy – its people, its finances, its production methods and its environment (including its customers)". For this reason, BZA should consider a strategic fit that would ensure a competitive advantage.

In this practical situation of BZA, the following influences are justified in terms of the PEST analysis, as shown in Table 3.8

Table 3.8 PEST Analysis

Political	– The post-apartheid political environment is more stable, and attractive for increased foreign direct investment (in the opinion of the researcher). Although BZA has been active in South Africa since 1997, it is only 9 years later, in 2006, that an investment in land and buildings is considered.
Economic	– Growth has been remarkable, and with the assistance of the MIDP incentive scheme, the

	economic forecast for the automotive sector and BZA, remains attractive. Currency strength has made imports cheap, and BZA is more competitive now, than previously.
Socio-Cultural	– There seems to be an improvement in skills development and an increase of black managers in the automotive industry. This is long overdue, since the participation of black senior management in an organisation, broadens the motivation base, and the attitudes of shop floor workers.
Technological	– Various new developments in the leather finishing process in CBSA, will force a skills transfer from overseas to the South African market as soon as an investment in BZA is approved. These new skills will be transferred into the local industry.

Corporate strategy is concerned with future action, but the organisation should consider that evidence about the future *may* be derived from what happened in the past (Lynch 2000:110). After some consideration of the comments of Lynch, the researcher would agree, that as a prescriptive strategist, he would suggest that it is worth it for the company to invest in an upstream operation, since we could assume the South African automotive market would remain attractive in the near future.

In the case of BZA, the researcher will define the purpose of the organisation and then develop a range of strategy options that will assist the organisation to achieve that purpose.

3.6.2 SWOT Analysis

The view is held by Fleisher (2000: 92) that the wide application of the SWOT analysis greatly contributes to its popularity as an analytical tool. This tool will assist BZA in determining the most suitable direction of the company. A SWOT-analysis supplies BZA management with a general framework for managing and understanding the environment in which BZA operates.

The analysis will also assist in determining the most suitable plan for the future of BZA and will identify what strategic direction BZA should take in order to secure a higher net benefit for the OEMs in terms of an increased local content contribution. The strategy which BZA will implement should assist the company to procure increased business, and build a sustainable competitive advantage over its competitors.

When a SWOT analysis is undertaken at an organisation like BZA, there are dangers in generalising. In a multi-national organisation, like Branaa Global, the group's SWOT analysis is usually initially undertaken at corporate level in CBSA, and it is also the headquarters that define the overall mission and objectives. The reason is that only CBSA has the overview needed to direct the strategy and they know which resources are available and required for the different processes. The results are then passed down for the strategy option process to be developed by BZA. As outlined by Fleisher (2003:93), a SWOT analysis is 'conceptually simple and comprehensive; and it can be applied to many facets of an organisation'.

The researcher has assessed the relative importance of each issue and the issue's potential impact on a company and its strategy. BZA managers should realize that the relative importance of each issue may vary between functional levels of the organisation.

A well developed SWOT analysis will force managers to better understand and respond to the strategic issues that have the greatest importance for BZA performance.

3.6.3 STEEP Analysis

The STEEP analysis covers the social, technological, economic, ecological and political aspects that have an influence on the competitiveness of BZA, and the researcher draws widely on the knowledge from Fleisher, et al (2003), and Lynch et al, (2000). BZA has developed a social responsibility program, which extends to all employees of the company.
Science and technology have a great impact on the environment in which BZA operates. They can influence aspects of the environment from the acquisition of raw materials right through to the after market sector. Recent industry developments made it possible to produce chrome free leather hides, where in the past chrome had to be used in the "wet" side of leather manufacturing. An increased number of BZA customers are changing their requirements from chrome content leather to chrome free leather. Chrome content leather has a negative impact on the environment. Interfacing with Branaa Global's R&D functions is an important requirement for competitive and strategy analysis.
The economical component refers to the distribution of resources by society. Economic variables must be closely monitored and identified as they can affect the competitiveness of BZA. Of importance to BZA management is the identification, monitoring, and forecasting of those economic variables to which BZA's strategic competitive efforts are most sensitive. As outlined by Fleisher (2003:273), the ecological environment encompasses both the physical and biological environments within which BZA interacts, and in which the proposed finishing plant will interact. BZA must comply with environmental regulations when building the proposed leather finishing plant. Local municipal authorities must approve the new industrial operations in the current location of the plant. In the case of BZA, the accelerated review of the MIDP was promulgated in view of a WTO violation threat. The origin of the review is in fact a politically based agenda, originated by the Australian government. An organization like BZA requires an environmental analysis to help the company achieve their competitive goals, and to retain a competitive advantage.

In relation to the STEEP analysis, recent industry developments made it possible to produce chrome free leather hides, where as in the past chrome had to be used in the "wet" side of leather manufacturing. An increased number of OEMs are changing their requirements from chrome content leather to chrome free leather. Chrome content leather has a negative impact on the environment. This applies very well to technological advancements in the producing of automotive leather seat covers, both in the hide manufacturing process, through the cutting operations, and in the sewing portions of the value chain. This includes new approaches to producing goods and services; new procedures as well as new equipment. The effects of technology and technological change can be felt by an organization from the acquisition of raw materials right through to the repair and recovery of the product after its use by customers. The task of managers is to identify and monitor the effects of technological change as it affects competitive strategy. This can be seen in the final goods and services market as well as in new product and process innovation, and even communication, human resource attraction, and marketing methods. Chrome content leather versus chrome free leather has a substantial ecological effect on the environment. A modern chemical water treatment plant will be part of the BZA finishing plant in South Africa.

3.6.4 Industry Life Cycle Analysis

As outlined by Lynch (2000:112), industries pass through 4 different stages namely, introduction, growth, maturity and decline. The corporate strategy of BZA must be adapted as the company moves along the industry life cycle. BZA started their operations in 1997, and experienced a very fast growth phase. During 2004 BZA entered the maturity phase in terms of new business, and has through various value adding processes, now arrived at a point where a strategic directional change is required. BZA has to determine a strategic way forward in which the company can secure new business contracts. In terms of the current MIDP benefits offered to the OEMs, the local content portion of the product lines that BZA offers are limited. In order for BZA to secure new contracts, the company should increase their local content portion, and the strategic fit would be to expand into an upstream operation, which would require an additional substantial foreign direct investment. If this strategic decision is not implemented in the short term, BZA will start entering a decline phase, in terms of the competitive advantage it holds in the industry. From there the company would experience a very slow recovery. A strategic change is needed within the operational process of BZA, and entering the next phase successfully with a strong competitive advantage, will be to build a leather finishing plant in South Africa, thereby extending the operations upstream, and adding further value to the local leather supply chain. BZA entered the fast growing automotive leather seat industry early in 1997, and has remained competitive for the past 6 years. Competitive pricing structures from BZA, and unsurpassed quality supply, guaranteed the company a large portion of the market share.

BZA is continuously exploring new growth opportunities and are implementing innovative product add-ons to existing product lines in order to offer the customer the most convenient options. During the year three new line processes were added at BZA, namely the perforation process of seat cover panels, the embossing of specific panels in accordance with customer requirements, and the lamination of foam to leather -process. These new services offered to BZA customers, increased the company's competitive advantage, and helped develop a niche market for BZA, where competitors were not willing to offer the same services, and causing the company to enter new growth stages in other areas of its operation.

3.6.5 Porter's 5 Forces Model

The basic principles of this model can be applied to commercial companies and the model is most essential in analyzing the competitive industry environment in which BZA operates. In order for the directors of BZA, and Branaa Global to make an important strategic decision, they must clearly understand the complete competitive environment in which the company operates. The analysis focuses on the forces that drive the automotive leather seat industry, and identifies the competition and rivalry in the industry. This model is often criticized but remains a useful tool for competitive strategic analysis of a company like BZA. When analysing the competitive industry environment, it usually begins with a general examination of the forces influencing the organisation. The objective of such a study is to develop a competitive advantage for BZA to enable the company to defeat rival companies. The objective the analysis is to investigate how BZA needs to form its strategy in order to develop opportunities in its environment and protect itself against competition and other threats. The basic assumption of the model is that all organisations will wish to benefit and protect their own interests. Companies wish to protect themselves in an essentially competitive environment. When building on the knowledge of Porter and Lynch (2000:126), the researcher can position BZA more effectively in the automotive leather environment.

The Bargaining power of Suppliers

BZA imports raw materials from CBSA which are used to produce the final automotive leather seat covers. Porter suggested that suppliers are more powerful under the following conditions.

Table 3.9 The Bargaining power of Suppliers

If there are only a few suppliers	This means that it is difficult to switch from one to another if a supplier starts to exert its power. BZA purchases 100% from its own tannery, and are obliged to accept the raw materials they get – even when inferior quality is produced
If there are no substitutes for the supplies they offer	This is especially the case in BZA, where the raw material purchased from CBSA is a finished hide. BZA is a cutting facility only, and does not add any value to the final product, except labour, overheads and profit. The hides form a crucial ingredient in the BZA production process and a continuous supply is vital to smooth production.
If suppliers' prices from a large part of the total costs of the organisation	The raw material portion in leather hides form up to 85% of the total cost of specific BZA products. Any increase in price would impact on the organisation if it was not able to raise its own prices in compensation
If a supplier can potentially undertake the value-added process of the organisation	Occasionally a supplier will have power if it is able to integrate forward and undertake the value-added process undertaken by the organisation; this could pose a real threat to the survival of the organisation. This would not be the case at BZA, since the only supplier is CBSA.

The Bargaining power of Buyers

In this model, Porter used the term buyers to describe what might also be called the customers of the organisation. Buyers have more bargaining power under the following conditions:

Table 3.10 The Bargaining power of Buyers

If buyers are concentrated and there are few of them	When the organisation has little option but to negotiate with a buyer because there are few alternative buyers around, the organisation is clearly in a weak position
If the product from the organisation is undifferentiated	If an organisation's product is much the same as that of other organisations, the buyer can easily switch from one to the other without problems. The buyer is even more likely to make such a shift if the quality of the buyer's product is unaffected by such a change. This could occur in the supply chain of the automotive leather industry, where different suppliers could offer the OEM the same specification leather, which is developed model specific
If backward integration is possible	As with suppliers above, the buyer's bargaining power is increased if the buyer is able to backward-integrate and take over the role of the organisation
If the selling price form the organisation is unimportant to the total costs of the buyer.	

The threat of potential new entrants

According to Porter, new entrants come into a market place when the profit margins are attractive and the barriers to entry are low. The allure of high profitability is clear and so the major strategic issue is that of barriers to entry into a market. Porter argued that there were some major sources of barriers to entry:

Table 3.11 The threat of potential new entrants

Economies of scale	Unit costs of production may be reduced as the absolute volume per period is increased. Such cost reductions occur in many industries and present barriers because they mean that any new entrant has to come in on a large scale in order to achieve the low cost levels of those already present. The automotive leather seat industry is one where such cost reductions are vital.
Product differentiation	Branding, customer knowledge, special levels of service and many other aspects may create barriers by forcing new entrants to spend extra funds or simply take longer to become established in the market. Leather characteristics are developed in conjunction with the OEMs, and these R&D costs are very high. New entrants will have difficulty developing these leather specifications

Capital requirement	Entry into the automotive leather seat markets involves major investment in technology, plant, distributions, and other areas. The ability to raise such finance and the risk associated with such outlays of capital will deter some companies.
Switching costs	When a buyer is satisfied with the existing product or service, it is naturally difficult to switch that buyer to a new entrant. The cost of making the switch would naturally fall to the new entrant and will represent a barrier to entry.
Government Policy	For many years, governments have enacted legislation to protect companies and industries, such as the MIDP program, where entry has been difficult for foreign companies to compete. It is for this reason that the Australian government has reported the MIDP as an unfair advantage to the WTO.

The Threat of Substitutes

According to Porter, substitutes do not entirely replace existing products but introduce new technology or reduce the costs of producing the same product. Effectively, substitutes may limit the profits in an industry by keeping prices down. In the case of BZA, and more widely, the automotive leather seat market is threatened by the introduction of vinyl and a new product called scirroco. These synthetic products are produced at a much lower price, and are visually the same as leather. These products are replacing full leather options in terms of B-panels, and head rests, and are introduced by the OEMs as a cost saving option.

From a strategy viewpoint, these key issues should be analysed, and are:

Table 3.12 The Threat of Substitutes

The possible threat of obsolescence;
The ability of customers to switch to the substitute;
The costs of providing some extra aspect of the service that will prevent switching;
The likely reduction in profit margin if prices come down or are held

The extent of competitive rivalry

Some markets are more competitive than others. In highly competitive markets, such as the automotive leather industry, where the role players are limited, and everybody knows everybody, companies engage in regular and extensive monitoring of key competitor companies. For example:

Table 3.13 The extent of competitive rivalry

Examining price changes and matching any significant move immediately;
Examining any rival product change in great detail and regularly attempting new initiatives themselves;
Watching investment in new competing plant and having regular drives to reduce their own costs levels;
Attempting to poach key employees.

All of the above have a direct relation to the leather seat industry, and even the following conditions in the industry may lead specifically to higher competitiveness.

- *When competitors are roughly of equal size and one competitor decides to gain share over the others,* then rivalry increases significantly and profits fall. In a market with a dominant company, there may be less rivalry because the larger company is often able to stop quickly any move by its smaller competitors.

- *If a market is growing slowly and a company wishes to gain dominance,* then by definition it must take its sales from its competitors – increasing rivalry.
- *Where fixed costs or the costs of storing finished products in an industry are high;* then companies may attempt to gain market share in order to achieve break-even or higher levels of profitability. Car production and seat production are both examples of industries where there is a real case for cutting prices to achieve basic sales volumes – thus increasing rivalry.
- *If extra production capacity in an industry comes in large increments,* then companies may be tempted to fill that capacity by reducing prices.
- *If it is difficult to differentiate products or services*
- *When it is difficult or expensive to exit from an industry*
- *If entrants have expressed a determination to achieve a strategic stake in that market*

In the case of the corporate strategy of BZA, the strategy implications from the general industry and competitive analysis should be considered.

- *Is there a case for changing the strategic relationships with suppliers?* Could more be gained by moving into close partnership with selected suppliers rather than regarding them as rivals?
- *Is there a case for forming a new relationship with large buyers?*
- *What are the key factors for success that drive an industry and influence its strategic development?* What are the lessons for the future that need to be built into the organisations strategy?
- *Are there any major technical developments that rivals are working on that could fundamentally alter the nature of the environment?* What is the time span and level of investment for such activity?

3.6.6 E-S-P Paradigm: Analyzing the role of Government

One such government initiative which this research report covers is the MIDP program of South Africa. These initiatives affect organizations and industries, such as the automotive leather seat industry, and BZA in particular. The macroeconomic conditions, and economic conditions at industry level and various other areas that are influenced by government, must be analyzed and addressed when forming new strategies.

Each one of these programs and incentives are measured and analyzed in terms of the net benefit of each scheme in relation to BZA. A clear understanding of these net benefits will assist the Directors of the company to make an informed decision regarding the strategic choice of investing substantially in the new proposed leather finishing plant and securing through that increased sustainable business opportunities in South Africa.

3.6.7 Competitor Analysis

Existing and potential competitors in the market place should be identified and then analyzed according to their strengths and weaknesses. Strategies should be formed to protect BZA as well as providing them with opportunities of gaining competitive advantages in the automotive leather seat market. The results of an effective competitor analysis helps BZA understand, interpret, and predict its competitors' actions and responses. Useful data and information combines to form competitor intelligence. BZA gathers intelligence not only about its competitors, but also with regard to public policies in countries across the world. The company should:

Determine who your competitors are

(Bader, Seton, EOSA)

Determine who your potential competitors may be

(Aunde)

Decide upon the information that is required pertaining to these rivals

(Diversification and expansion strategies)

Continually monitor rivals and continually scan for potential rivals

3.6.8 Sustainable Competitive Advantage (SCA)

Sustainable advantage will be derived from numerous sources, such as niche marketing (lamination, perforation and embossing options offered to customers), low costs (increased productivity through in house incentive scheme), new technology implementations (new finishing plant), and the use of resources and skills within an organization. To be sustainable, competitive advantage needs to be *"more deeply embedded"* in the organisation – its resources, skills, culture and investment over a period of time.

The new proposed finishing plant of BZA should continue to deliver economies of scale.

In an organisation like BZA, primary activities, such as inbound logistics and outbound logistics account for significant portions of the total cost of producing goods. A substantial portion of the raw materials imported by BZA are air freighted, and downstream sewn seat covers are exported by air as well. Thus, cost leaders seeking competitively valuable ways to reduce costs may want to concentrate on the primary activities of inbound logistics and outbound logistics.

BZA implemented such a differentiation strategy, where the lamination process of foam onto leather, differentiated its products from competitors, and this process also meant a cost saving for the sewing plants. Firms must be able to produce differentiated products at competitive costs to reduce upward pressure on the price customers are required to pay BZA also implemented a leather perforation process and added an embossing option to differentiate its product line. When a product's differentiated features are produced through non-competitive costs, the price for the product can exceed what the firm's customers are willing to pay. When the firm has a thorough understanding of what its customers value, and the importance they attach to the attainment of certain needs, and are therefore willing to pay a premium, the differentiation strategy can be used successfully. BZA, through the differentiation strategy, produces non-standardized products for customers who value differentiated features more than they value low costs.

3.6.9 BCG Growth Share Matrix

Drawing on the knowledge form Lynch (2000:175), the balance of an organization's product portfolio should regularly be analyzed. This method makes use of the relative market share, as well as the market growth rate for each product.

The idea is to determine under which portfolio the current products of BZA falls. Lynch (2000:176) further argues that the four categories "*merge into one another*". BZA offers their automotive leather seats to a range of customers, i.e., BMW South Africa (through the sewing plants, ALC and Aunde), Audi (through Lear Sewing sewing plant), Nissan SA, and Ford SA (through JCI sewing plant). Potential customers include Volvo, VWSA and Delta (Opel & Chev).
Different products fall in different categories, and the BCG Matrix will assist in identifying which products are "good runners" (stars), and which ones are problem children.

As outlined by Fleisher (2003:45), the use of his FAROUT rating summary, shows that the BCG matrix scores high on resource efficiency and timeliness. This means that an organisation like BZA can make use of the BCG matrix with limited resources (it is easy to use), and quickly (relative market share can easily be estimated).

3.7 CONCLUSION

The researcher identifies the company BZA and strategically positions it in its business environment. He continued with recent developments in the automotive leather seat industry and identified the industrial policy that government has developed to promote and protect the infant automotive industry in South Africa. The chapter concludes with the impacts of the MIDP on the automotive leather industry and sets the platform on which the company is measured. A better understanding of the MIDP and its workings are offered, and the influences of the MIDP on a local foreign national company such as BZA are highlighted. Foreign management can now better understand what drives the industry, and whether any directional corrections in the corporate strategy are needed.

CHAPTER FOUR: PRESENTATION & ANALYSIS OF RESULTS

"The greatest lesson in life is to know that even fools are right sometimes".
Winston Churchill

4.1 Introduction

Strategic decisions have to be made in order for BZA management and shareholders of the company to enable them to make the correct strategic directional changes, and to develop a new corporate strategy. They need to understand what drives the industry, what the customers (OEMs) motivations are for allocating new projects to potential suppliers, and how BZA as a company could reach the goals and targets which are in place. The presentation and analysis of results will allow BZA management and the directors to do exactly this.

The MIDP was introduced in 1995, and it was intended to run for 5 years, but after some recommendations during the midterm review, the program was extended until 2007.
The program comprised four principal elements as shown in Table 4.1.

Table 4.1 Four principal elements of the MIDP

A gradual reduction in import duties on both vehicles and components
An export-import complementation scheme under which vehicle and components exporters can earn tradable IRCCs to offset duties on imported vehicles and components. Import rebates are earned through the export of eligible exports, and the value of the IRCC is calculated using a formula measuring the EEP.
Access to the standard duty drawback program for exporters, under which all import duties paid on components and intermediate inputs used in exported vehicles and components can be rebated, and
A duty free allowance on imported components of 27 percent of the value of vehicles produced for the domestic market.

It is under these MIDP parameters that BZA has to compete against industry competitors. The calculations of benefits under the current MIDP program are based on a reducing beneficial basis (see Figure 4.1 to 4.4), where the qualifying values of eligible export performance are reduced every year. This is due to the fact that government wants industry to develop an independent sustainable advantage. Industry should be globally competitive without the assistance of government. It is only under these rules that the automotive industry was promoted in the first place.

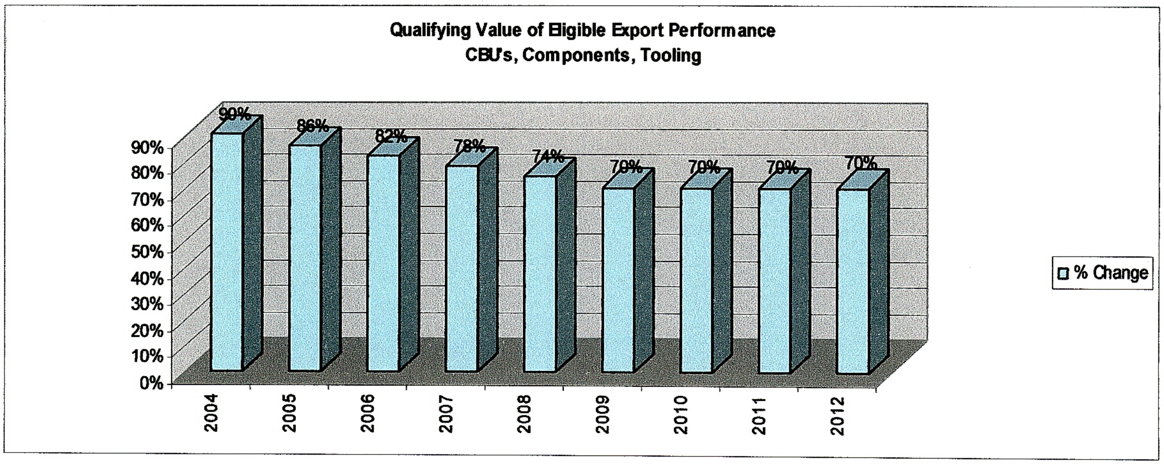

Figure 4.1 MIDP PARAMETRES AS ANNOUNCED BY DTI 06 DECEMBER 2004

Figure 4.1 demonstrates a single aspect of the MIDP parameters which we announced on 06 December 2006 by the DTI. Figure 4.1 shows the qualifying value of imported Completely Built Up Units (CBU), components and tooling. One must take note of the declining value per annum, which signifies a decline in the possible net benefits offered to the OEMs. It is significant, due to the nature of the MIDP to promote independence of the industry. Every year the benefits would decrease with the same effort being put in by the role players. This parameter reduces the qualifying value of the eligible export.

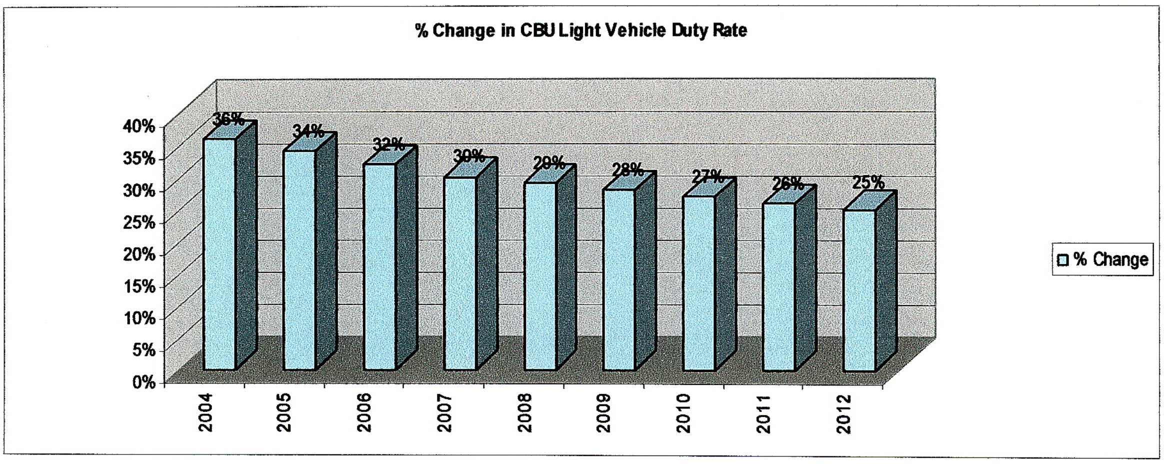

Figure 4.2 % Change in CBU Light Vehicle Duty rate

Figure 4.2 demonstrates the percentage change in the import duty rate per annum, and shows a declining value per annum, which signifies a decline in the cost of importing Completely Built Up Units (CBU). This is in line with one of the objectives of the MIDP to reduce the costs of imported vehicles.

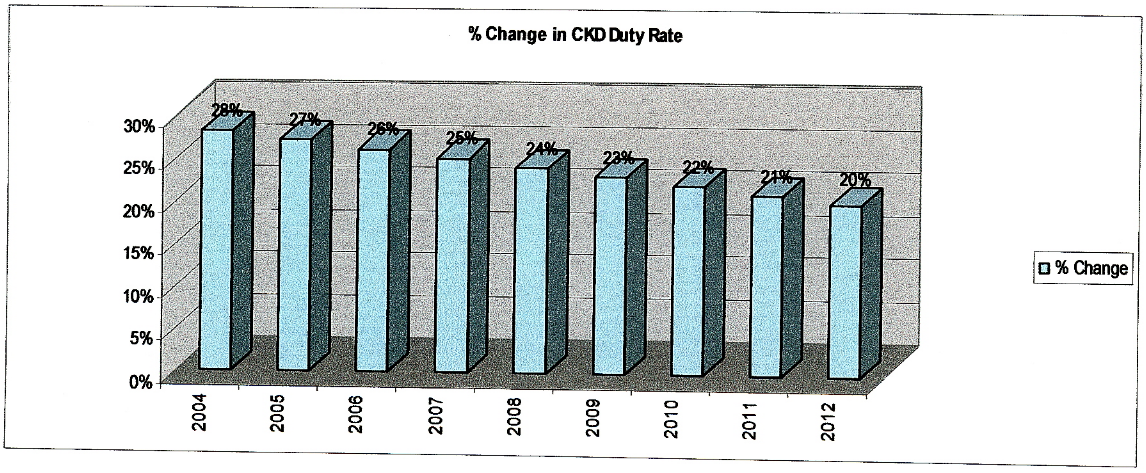

Figure 4.3 % Change in CKD Light Vehicle Duty rate

Figure 4.3 demonstrates the percentage change in the import duty rate per annum, and shows a declining value per annum, which signifies a decline in the cost of importing Completely Knock down Units (CKD). This is in line with one of the objectives of the MIDP to reduce the costs of imported vehicles.

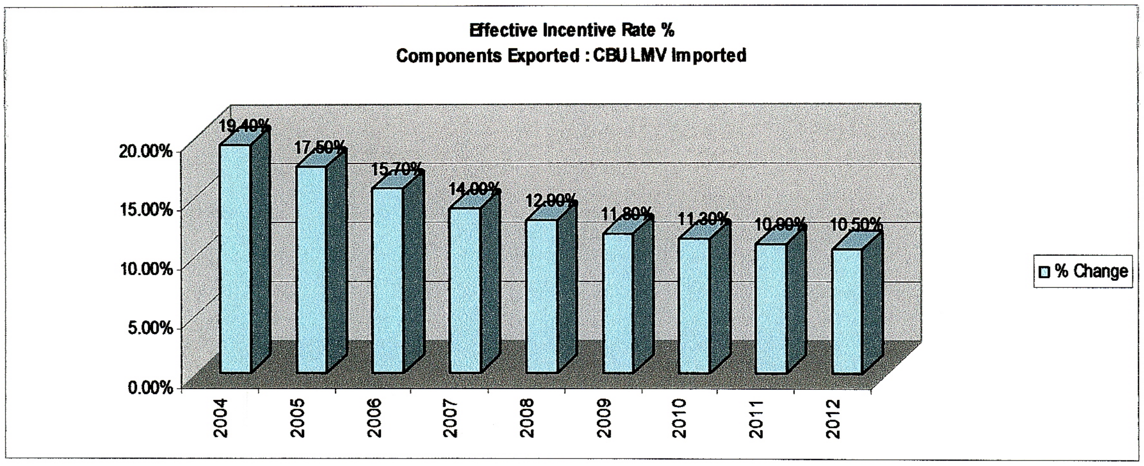

Figure 4.4 Effective Incentive Rate

Figure 4.4 demonstrates the percentage change in the effective incentive rate per annum, for components exported in relation to CBU Light Motor Vehicles Imported. This is in line with one of the objectives of the MIDP to reduce the costs of imported vehicles.

In order to understand the workings and calculation methods of the MIDP program, the researcher must have a clear understanding of the term local content.
The local content portion of an exported leather seat cover must be seen as the accumulated value, adding the values of all the contributing components in the complete value chain of the exported product. In this sense, each supplier in the value chain has a contribution to the final product. One must consider that BZA competes in the South African market with local raw materials, and these materials have a local content advantage over imported raw materials. In this consideration, BZA offers its own portion of local content, and can not influence the local content portions of other suppliers in the same value chain. In order to be a successful supplier of automotive leather seat covers in the South African market, industry has to work very closely together. Value chain partners are developed, and this is a perfect example of where synergies are developed in order to maintain and offer combined financial benefits to the OEMs.

It is under these conditions that one must realize that the calculation of local content can be made in two completely different contexts.

When the OEM therefore refers to the local content of a company, the OEM must clearly state in which context it is referring to,

1 The local content of BZA products in relation to the value of the BZA portion of the value chain.
2 The local content of BZA products in relation to the value of complete product value chain, meaning the export value of the product.

For the purpose of this important and often misunderstood calculation, the researcher has chosen a single automotive leather seat cover, and the commercial export value of the seat is used to calculate and evaluate the MIDP workings and compare the financial benefits in terms of the MIDP benefits of one seat cover offered to the OEMs. These calculations are shown in Table 4.2

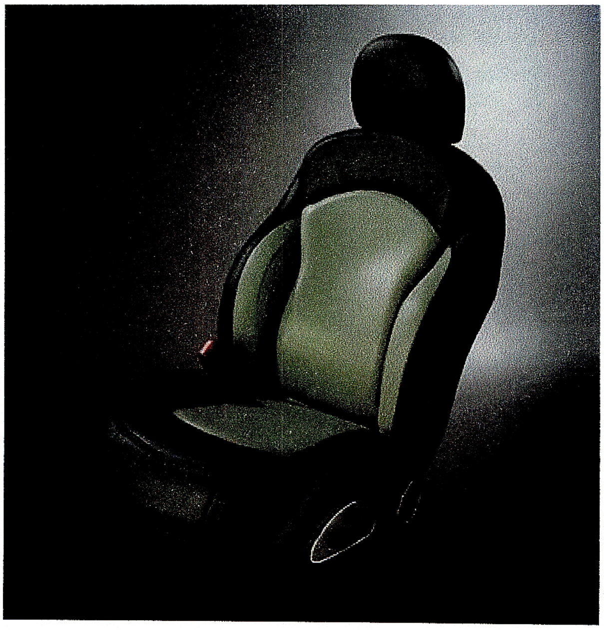

Figure 4.5 Automotive Leather Seat – Sport

AUTOMOTIVE LEATHER SEAT – SPORT SET
CURRENT SITUATION – BZA
QUARTER 1 – 2006 F   Financial data

Table 4.2 MIDP Benefits offered under current situation- BZA

MODEL	BZA	BZA
	CURRENT SITUATION	CURRENT SITUATION
SPORT SEAT SET	EURO	ZAR – Local Currency
One m2 Bovine Leather Imported	EURO 25.00	
One m2 Bovine Crust Imported	EURO 20.00	
BZA Selling to Local Sewing Plant (per m2)	EURO 29.00	
Exchange Rate (ZAR EUR)	7.5200	
Selling Price per m2	EURO 29.00	ZAR 218.01
Size of Sport Seat Set (m2)	5.70 m2	5.70 m2
Selling Price of Sport Seat	EURO 165.30	ZAR 1 242.64
Cost Price of Sport Seat	EURO 142.50	ZAR 1 071.24
Forex Value of Sport Seat	EURO 142.50	ZAR 1 071.24
Local Content Portion	EURO 22.80	ZAR 171.40
Percentage Local Content	**14%**	**14%**
EEPV (Eligible Export Performance Value)	EURO 22.80	ZAR 171.40
IRCC (Import Rebate Credit Certificate)	**82%**	**82%**
IRCC Face Value	EURO 18.70	ZAR 140.55
CBU Duty Rate	**32%**	**32%**
Rebate Value offered to OEM per Sport Seat Set	EURO 5.98	ZAR 44.98
Net Benefit to OEM per Sport Seat Set	EURO 5.98	ZAR 44.98
Gross Leather Area of Sport Seat Set (m2)	5.70 m2	5.70 m2
Net Benefit to OEM per m2	EURO 1.05	ZAR 7.89
Benefit % Offered to OEM	**3.62%**	**3.62%**

It can be seen from this calculation that the local content percentage that BZA offers in the current situation with only the cutting operations in South Africa is 14% of the selling price.

The financial benefit that BZA offers the OEM is Euro 5.98 for every sport seat set that is supplied, and this equates to a benefit of 3.62% of the selling price.

AUTOMOTIVE LEATHER SEAT – SPORT SET
WITH PROPOSED EXPANSION – FINISHING PLANT – BZA
QUARTER ONE, 2006 - Financial data

Table 4.3 MIDP Benefits offered under expansion situation- BZA

MODEL	BZA	BZA
SPORT SEAT SET	WITH FINISHING PLANT	WITH FINISHING PLANT
	EURO	**ZAR – Local Currency**
One m2 Bovine Leather Imported	EURO 25.00	
One m2 Bovine Crust Imported	EURO 20.00	
BZA Selling to Local Sewing Plant (per m2)	EURO 29.00	
Exchange Rate (ZAR EUR)	7.5200	
Selling Price per m2	EURO 29.00	ZAR 218.01
Size of Sport Seat Set (m2)	5.70 m2	5.70 m2
Selling Price of Sport Seat	EURO 165.30	ZAR 1 242.64
Cost Price of Sport Seat	EURO 114.00	ZAR 857.00
Forex Value of Sport Seat	EURO 114.00	ZAR 857.00
Local Content Portion	EURO 51.30	ZAR 385.65
Percentage Local Content	**31%**	**31%**
EEPV (Eligible Export Performance Value)	EURO 51.30	ZAR 385.65
IRCC (Import Rebate Credit Certificate)	**82%**	**82%**
IRCC Face Value	EURO 42.07	ZAR 316.23
CBU Duty Rate	**32%**	**32%**
Rebate Value offered to OEM per Sport Seat Set	EURO 13.46	ZAR 101.19
Net Benefit to OEM per Sport Seat Set	EURO 13.46	ZAR 101.19
Gross Leather Area of Sport Seat Set (m2)	5.70 m2	5.70 m2
Net Benefit to OEM per m2	EURO 2.36	ZAR 17.75
Benefit % Offered to OEM	**8.14%**	**8.14%**

It can be seen from this calculation in Table 4.3 that the local content percentage that BZA offers with the inclusion of the finishing plant as a strategic investment option in South Africa is increased from 14% to 31%. This is a substantial impact in terms of the MIDP benefit offered to the OEM.

The financial benefit that BZA offers the OEM is increased from Euro 5.98 for every sport seat set is supplied to Euro 13.46, and this equates to a benefit of 8.14%, as shown in Figure 4.5.

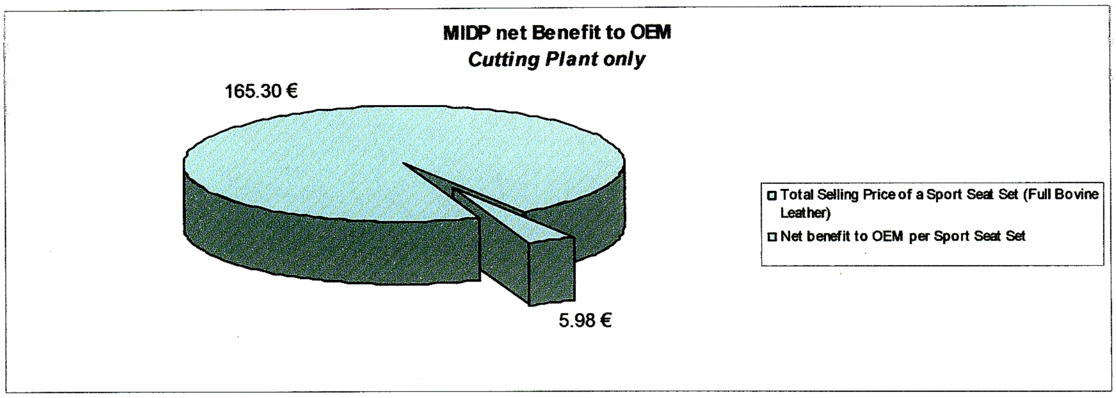

Figure 4.6 MIDP benefit offered to OEM – Current

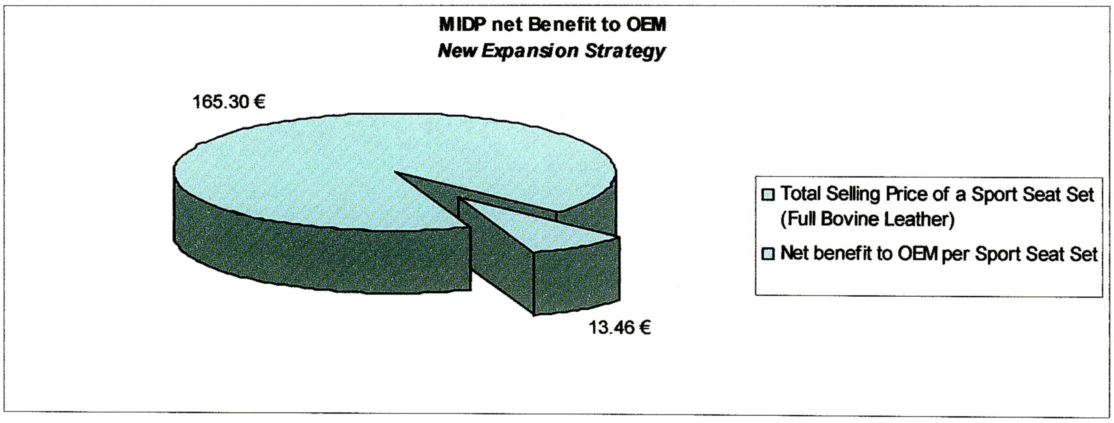

Figure 4.7 MIDP benefit offered to OEM – Proposed

The increase of the MIDP benefit through the expansion strategy of BZA can clearly be determined in terms of the MIDP benefits, and with the direct foreign investment in South Africa, the real benefits offered to the final customer is increased from Euro 5.98 to Euro 13.46 per seat cover set exported as shown in Figure 4.6.

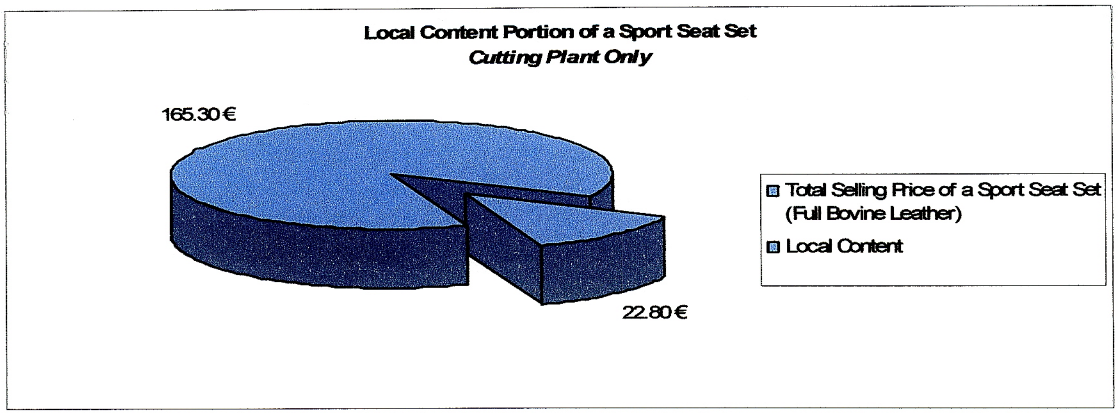

Figure 4.8 Local content Portion of a Sport Seat Set - Current

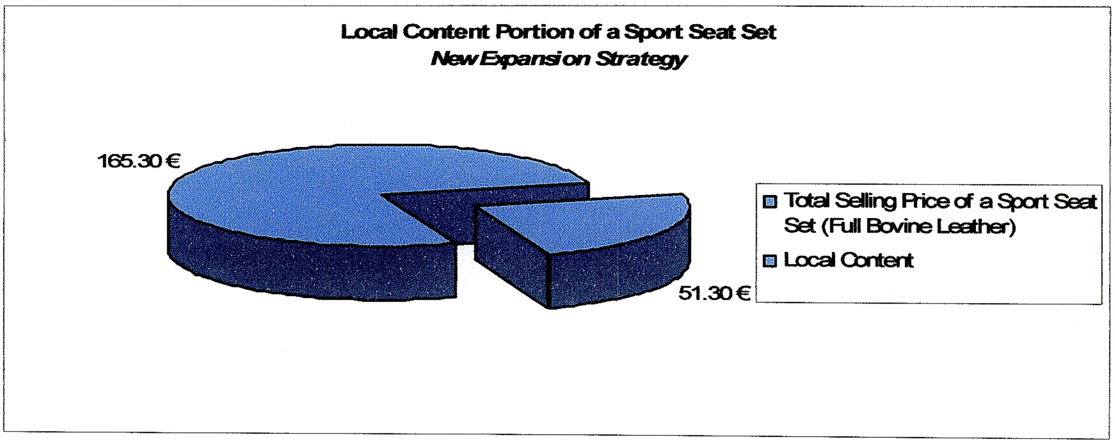

Figure 4.9 Local content Portion of a Sport Seat Set - Proposed

By comparing the two pie charts in Figure 4.8 and Figure 4.9, we see how the local content portion of a sport seat set, increases from Euro 22.80 to Euro 51.30, with the proposed new expansion strategy, and the building of an upstream process such as the new finishing plant strategically envisaged by BZA.

Foreign exchange movements also impact dramatically on the local content portion of a product. A foreign exchange profit will be experienced when the local currency strengthens against the import currency. When bovine leather hides are imported at Euro 8.00 to the ZAR for a certain period, and in a next period the same product is imported at Euro 7.500, the imported product is cheaper. If one assumes that the product is sold at the same foreign price into the leather value chain, only converting into local currency at the daily prevailing rate, it means that the local content portion is higher (increases). This equates to an increased financial benefit to the OEMs. These currency fluctuations are shown in Figure 4.10

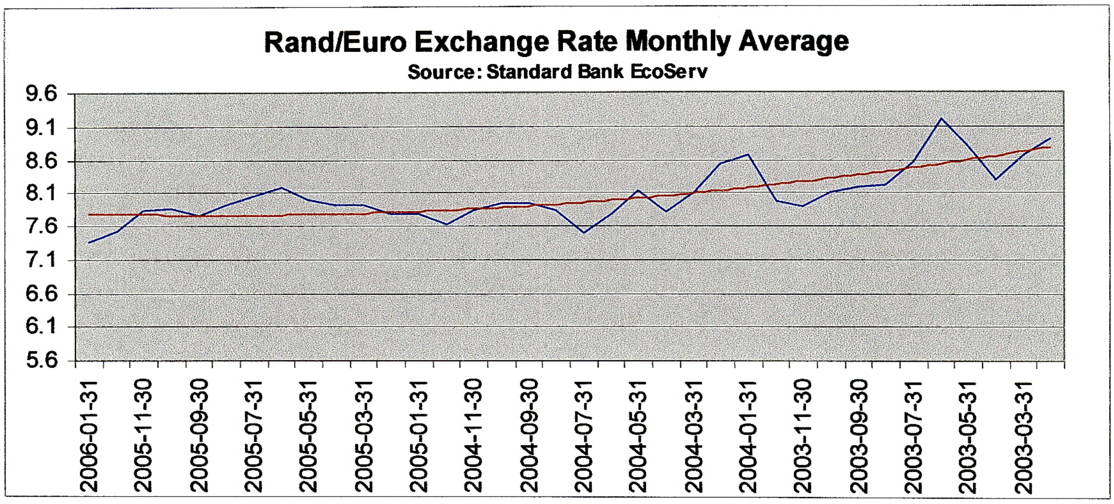

Figure 4.10 Rand/Euro Exchange Rate Monthly Average

These local content calculations apply only to the cutting portion of the value chain, which BZA offers within the complete value chain, and should not be confused with the local content achieved in terms of the complete value chain.

In order to determine the impact that the proposed finishing plant of BZA will have on local content in terms of the full value chain, one must consider the final export price of the seat cover.

The following financial calculations will be evaluated in order to determine the benefits offered by BZA in terms of the MIDP program. From these financial calculations, BZA management should be able to clearly determine what strategic direction BZA should take in order to procure increased business.

The calculation in Table 4.4 determines the current financial benefits offered to the OEMs under the MIDP program, in terms of ***local competitors using local raw material***, and selling to the OEMs, through the same value chain, and in relation to the full value chain, where the final products are exported. In order to effectively calculate these benefits and to compare them more accurately, the assumption is made that the export price of the leather seat sets are the same for all suppliers.

Table 4.4.1 South African Competitor Buying Local Hides (parametres)

Year	2004	2005	2006	2007	2008	2009	2010	2011	2012
(1)IRCC	90%	86%	82%	78%	74%	70%	70%	70%	70%
(2)Ratio I:E	60%	60%	60%	60%	60%	60%	60%	60%	60%
(3)MIDPRate	36%	34%	32%	30%	29%	28%	27%	26%	25%
(4)E.Rate	7.52	7.52	7.52	7.52	7.52	7.52	7.52	7.52	7.52
(5)SP BZA H	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00
(6)SP BZA C	20.00	20.00	20.00	20.00	20.00	20.00	20.00	20.00	20.00
(7)I.C.Costs	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
(8)GLA m2	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70

(1) Import Rebate Credit Certificate
(2) Ratio of Exports against Imports
(3) Effective Rebate Rate for CKD Units
(4) Effective Exchange Rate used
(5) Selling Price of Full Hides from CBSA to BZA
(6) Selling Price of Crust products from CBSA to BZA
(7) Imported Chemicals Costs
(8) Gross Leather Area of a Sports Seat Set

Table 4.4.2 South African Competitor Buying Local Hides (example)

a)	1775	1775	1775	1775	1775	1775	1775	1775	1775
b)	70%	70%	70%	70%	70%	70%	70%	70%	70%
c)	30%	30%	30%	30%	30%	30%	30%	30%	30%
d)	15%	15%	15%	15%	15%	15%	15%	15%	15%
e)	25%	25%	25%	25%	25%	25%	25%	25%	25%
f)	319	319	319	319	319	319	319	319	319
g)	1455	1455	1455	1455	1455	1455	1455	1455	1455
h)	90%	86%	82%	78%	74%	70%	70%	70%	70%
i)	1310	1251	1193	1135	1077	1018	1018	1018	1018
j)	60%	60%	60%	60%	60%	60%	60%	60%	60%
k)	36%	34%	32%	30%	29%	28%	27%	26%	25%
l)	282	255	229	204	187	171	165	158	152
m)	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70
n)	49.65	44.80	40.21	35.86	32.88	30.03	28.96	27.89	26.81
o)	**2.80%**	**2.52%**	**2.26%**	**2.02%**	**1.85%**	**1.69%**	**1.63%**	**1.57%**	**1.51%**

a) Export Price – Invoiced by Exporter
b) Leather Content % of Exported Product
c) Sewing Content % of Exported Product
d) Imported Content % in Leather Portion
e) Imported Content % in Sewing Portion
f) Total Imported Content Value of Exported Product
g) Eligible Export Performance Value = Local Content Value
h) IRCC compensation factor
i) IRCC Certificate Face Value
j) Compensation Factor for CBU units

k) Rebate Rate
l) Net Benefit Value offered to OEM
m) Total square metres of a Sports Seat Set
n) Net Benefit Value to OEM per square metre of leather supplied
o) Percentage of Net Benefit offered to OEM

The calculation in Table 4.5 determines the current financial benefits offered to the OEMs under the MIDP program, in terms ***of BZA using imported raw material***, and selling to the OEMs, through the same value chain, and in relation to the full value chain, where the final products are exported.

Example of BZA Current Situation – with the cutting facility only

Table 4.5.1 MIDP Benefits - BZA Current situation

a)	1775	1775	1775	1775	1775	1775	1775	1775	1775
b)	1526	1526	1526	1526	1526	1526	1526	1526	1526
c)	248	248	248	248	248	248	248	248	248
d)	90%	86%	82%	78%	74%	70%	70%	70%	70%
e)	223	213	203	193	183	173	173	173	173
f)	60%	60%	60%	60%	60%	60%	60%	60%	60%
g)	36%	34%	32%	30%	29%	28%	27%	26%	25%
h)	48	43	39	34	32	29	28	27	26
i)	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70
j)	8.48	7.65	6.86	6.12	5.61	5.13	4.94	4.76	4.58
k)	**0.48%**	**0.43%**	**0.39%**	**0.34%**	**0.32%**	**0.29%**	**0.28%**	**0.27%**	**0.26%**

a) Export Price – Invoiced by Exporter
b) Total Imported Content Value of the Exported Product
c) Eligible Export Performance Value = Local Content Value
d) IRCC compensation factor
e) IRCC Certificate Face Value
f) Compensation Factor for CBU units
g) Rebate Rate
h) Net Benefit Value offered to OEM
i) Total square metres of a Sports Seat Set
j) Net Benefit Value to OEM per square metre of leather supplied
k) Percentage of Net Benefit offered to OEM

Table 4.5.2 MIDP Benefits - BZA Current situation (net results)

*ZAR	41.17	37.15	33.34	29.73	27.27	24.91	24.02	23.13	22.24
**US$	5.47	4.94	4.43	3.95	3.63	3.31	3.19	3.08	2.96

* Difference in Net benefit (value in ZAR) between Local Competitor and Branaa Current situation
** Difference in Net benefit (value in US$) between Local Competitor and Branaa Current situation

The calculation in Table 4.6 determines the possible financial benefits offered to the OEMs under the MIDP program, in terms of BZA using imported raw material (crust), ***but after the successful implementation of the proposed upstream investment***, of finishing the hides in South Africa, and selling to the OEMs, through the same value chain, and in relation to the full value chain, where the final products are exported.

Example of Branaa Situation with Proposed New Finishing Plant

Table 4.6.1 MIDP Benefits - BZA Proposed Strategy

a)	1775	1775	1775	1775	1775	1775	1775	1775	1775
b)	900	900	900	900	900	900	900	900	900
c)	875	875	875	875	875	875	875	875	875
d)	90%	86%	82%	78%	74%	70%	70%	70%	70%
e)	787	752	717	682	647	612	612	612	612
f)	60%	60%	60%	60%	60%	60%	60%	60%	60%
g)	36%	34%	32%	30%	29%	28%	27%	26%	25%
h)	170	153	137	122	112	102	99	95	91
i)	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70	5.70
j)	29.84	26.93	24.17	21.55	19.77	18.05	17.41	16.76	16.12
k)	**1.68%**	**1.52%**	**1.36%**	**1.21%**	**1.11%**	**1.02%**	**0.98%**	**0.94%**	**0.91%**

a) Export Price – Invoiced by Exporter
b) Total Imported Content Value of the Exported Product
c) Eligible Export Performance Value = Local Content Value
d) IRCC compensation factor
e) IRCC Certificate Face Value
f) Compensation Factor for CBU units
g) Rebate Rate
h) Net Benefit Value offered to OEM
i) Total square metres of a Sports Seat Set
j) Net Benefit Value to OEM per square metre of leather supplied
k) Percentage of Net Benefit offered to OEM

Table 4.6.2 MIDP Benefits - BZA Proposed Strategy (net results)

*ZAR	19.80	17.87	16.04	14.30	13.12	11.98	11.55	11.12	10.70
**US$	2.63	2.38	2.13	1.90	1.74	1.59	1.54	1.48	1.42

* Difference in Net benefit (value in ZAR) between Local Competitor and Branaa proposed situation with new Finishing Plant
** Difference in Net benefit (value in US$) between Local Competitor and Branaa proposed situation with new Finishing Plant

The difference in benefits offered between a local competitor and BZA with the new proposed finishing plant is much smaller as shown in Table 4.6. In other words, BZA is in a position to offer a benefit much closer to the benefit that a local competitor is currently offering.
These calculations are based on the assumption that raw materials are sourced and supplied at the same cost, for both BZA and their competitors, even though some raw materials are imported and other raw materials are from local supply.
The difference in benefits offered are solely influenced by the portions of local content and imported content as shown in Tables 4.6.

As the aim of this work is to understand and show how the MIDP functions, how benefits are calculated, and how these benefits eventually impact on the industry, it was essential to undertake the above calculations. The results of these calculations support the theory, that adding more local content to the value chain of the automotive leather seat will indeed increase the amount of financial benefits received by the OEMs. These calculations clearly show that the benefits offered through the MIDP, increase when increasing the local content portion of a product, and this is the key motivation of the MIDP – to stimulate local South African industry.

In relation to what this study will suggest, BZA should possibly apply a prescriptive approach to its new corporate strategy, and this research project aims to assist management at BZA to determine the most suitable strategy. The BZA objective has already been clearly defined as follows: "determine what the impact of increased local content will have on the net benefits offered to the OEMs, in terms of the MIDP, and how the company could best achieve the set goal" (Strategic Management meeting held at BZA, 2005).

How the OEMs make best use of these financial benefits offered through government to them, in order to stimulate growth in the automotive sector is another research topic of its own. The researcher can only hope that the OEMs show the vision and commitment which are still lacking, in uplifting and developing South African communities.

4.2 Conclusion

Now that it has been shown that the financial calculations clearly indicate the route that BZA should take, i.e. to increase local content, it is now necessary to detail the strategy the company should follow. This information also takes into consideration the analysis from the various strategic management tools recommended and used in Chapter 3 and state how they actually impact on the strategic direction that BZA should take.

Further to foreign direct investment in South Africa, active state policy can also be seen in other manufacturing sectors that have increased investment, such as motor vehicles and leather products. These sectors have been heavily influenced by the MIDP (Black, 2001). It is notable that the performance of leather products contrasts with footwear, which performed poorly. Growth in leather products is mainly accounted for by leather seat-covers for cars. The motor vehicle sector itself also had above-average rates of growth in investment. It is notable that the incentives of the MIDP rely on the ongoing protection of the local market, as this provides the benefit of earning duty-free import licences. The scheme is similar in some ways to the program used to develop the car industry in South Korea, where firms were forced to export if they were to be allowed to import some foreign manufactured models (Amsden, 1989). This achieved the dual goal of forcing firms to work for competitiveness in international markets, while maintaining a level of protection in the domestic market to enable capabilities to be developed. The MIDP is also notable as a sector-specific programme based on a clear understanding of the structural changes required in the sector, such as the rationalisation of models and the achievement of scale economies. It had clearly specified objectives, time-frames and mechanisms. Its weakness is perhaps that it favours the export of very high-value items, such as catalytic converters and seat leather, rather than more labour-intensive components.

As an automotive supplier in the South African Automotive Industry, BZA need to develop new capabilities to create value for their customers. An effective supplier, with a sustainable competitive advantage, needs to move away from the current practice of being a mere parts and modules supplier to becoming a solution provider. Suppliers who play an active role towards helping their automotive customers tackle challenges pertaining to cost; quality time to market and innovation will succeed as winners. Those who do not adapt, will loose market share and become extinct.

A full case analysis was done on BZA in order to fulfill the objectives this study sought to achieve. The final objective is in relation to the recommendations and these are discussed in the following chapter.

CHAPTER FIVE

5.1 RECOMMENDATIONS AND CONCLUSION

An important fact to remember before recommendations and conclusions are made, culminates in the words of Andrew Carnegie:

> "No person will make a great business who wants to do it all himself or get all the credit"

The overall objective of this paper is to solve a specific business problem, one which the Directors of BZA have to make, and successfully implement; i.e. a strategic decision about the future of BZA and the effects that the MIDP have on the company in the short term future (the next 12 to 24 months), and in the long term future of the company; i.e. until the end of the current structure of the MIDP which runs until 2012.

BZA has been very successful as an "early entry player" in the cut and supply of automotive leather seat covers. When they started their operations in 1997, the company experienced a strong growth curve and was concerned on how to maintain this growth and also make it sustainable in the long term. The directors and management at BZA were concerned with this strategic MIDP, slash local content requirements. The researcher undertook a strategic investigation into the business environment in which the company operates, and through implementing strategic analysis methods, it was found that the local content value of the seat covers sold to the OEMs, were not sufficient. The net benefits earned by the OEMs were lower (when purchasing at BZA) than when they purchased the same covers from BZA competitors with a higher local content structure.

In order to measure the success of this report, we have to determine if the original objectives of the study was met:

- The environment in which BZA operates is now better understood, through the utilization of various strategic analysis techniques.
- The value of the MIDP benefits offered under the current investment structure (BZA cutting facility only) was determined, measured and identified.
- The value of the MIDP benefits offered under the proposed new investment structure (BZA cutting facility and finishing plant) was determined, measured and identified.
- The increased benefits derived from an increased investment are enough to satisfy the current requirements of the OEMs.
- It was established how BZA should position itself in order to become more competitive and how to develop a sustainable competitive advantage.
- A new strategy was proposed, and should be implemented at BZA, especially in relation to: an *expansion strategy* in the South African automotive leather seat industry.
- The strategy suggested by the directors of BZA is correct in terms of the increased financial benefits offered to the OEMs through increased local content.
- Recommendations that will provide BZA with valuable information and strategic evaluations in order to re-position and align itself with the possibilities of increasing the actual net requirements of the OEMs in terms of the MIDP program, through increased local content contributions.

The recommendation of the researcher is that BZA should increase their local content contribution to such a level as to become more competitive, and to offer to the OEMs the same benefit as local suppliers. The aim of this research is to determine the level of this increase in local content, in other words, how far upstream the company should invest in relation to finishing processes. The recommendation of the researcher to BZA is to import crust which is an up stream process, and to start finishing the hides (an added local content process) in South Africa. The benefits and costs of this additional process have been determined, evaluated and analysed to show how the benefits offered to the OEMs are increased. The recommendation is that the proposed strategy then be implemented with immediate effect in order for BZA to secure future business. Through the analysis results of this research project the Directors of BZA are enabled to implement this expansion strategy option which will place BZA in a positive growth framework and by adding improved organizational performance in addition to the expansion strategy, the company would be able to show a sustainable growth as required. The goal to secure a long-term sustainable business growth model would be achievable and a solution to the concerns of BZA.

In addition to the conclusions already reached from the research paper, it is also the recommendation of the researcher that the consideration of expanding into the South African automotive market in terms of strategically investing in a new leather finishing plant, is that the MIDP should not exclusively be the deciding factor. The Directors of BZA must take very seriously, the considerations of the South African government regarding incentive schemes, and in particular the current MIDP review that has not yet been finalised. One must note that any change to the current MIDP structure, or calculation methods of the MIDP benefits, would have the same financial impact for all the role players in the industry. This includes BZA and their competitors. However, the vision of the company BZA should go beyond the monetary benefits required by the MIDP.

Yes, BZA should strategically invest in a finishing plant in South Africa, but not only to increase the local content of its products, but more importantly to increase the global capacity output of finished bovine leather hides for the global automotive market. Newer, bigger and faster growing markets are waiting to be explored in the east, and South Africa is strategically positioned as a jumping block for Branaa Uruguay to expand its operations into the Chinese market.

In a recent paper called "Strategies for the Automotive Supplier Industry" (Dec 2005) by Infosys, the future of automotive suppliers could readily be summarized as follows:

> *"Suppliers should accelerate current initiatives towards globalization and increase their focus on product development and cost reduction, and suppliers should proactively work with the OEMs in meeting critical challenges within the industry".*

This new finishing plant in South Africa is not only an expansion project for Branaa South Africa, it is absolutely necessary as an expansion project for Branaa Global.

The increased local content benefits attained under the MIDP program, are only an added bonus.

The proposed strategy offered through this research paper, the formulation thereof, and the successful implementation thereof, should become the main focus and the ultimate vision of the Branaa family, or in the words of William Shakespeare:

> "Be not afraid of greatness. Some are born great, some achieve greatness, and some have greatness thrust upon 'em".
>
> *Shakespeare, Twelfth Night, II: 5*

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Industry Associations and Organisations

Automotive Industry Development Centre (AIDC) - responsible for stimulating technological development, etc.

Website: http://www.aidc.co.za

Automotive Industry Export Council (AIEC) promotes and co-ordinates export activities - email:

Website: http://www.aiec.co.za

National Association of Automotive Component & Allied Manufacturers (NAACAM) - the component makers' organisation
Website: http://www.naacam.co.za

National Association of Automobile Manufacturers of South Africa (NAAMSA) - representing the vehicle assemblers and most of the major importers
Website: www.naamsa.co.za

National Union of Metalworkers of South Africa (NUMSA) - the dominant union in both manufacturing and the aftermarket
Website: www.numsa.co.za

Retail Motor Industry Organisation (RMI) - the federation embracing aftermarket enterprises

Export Marketing and Investment Assistance Scheme (EMIA)

Industrial Development Corporation
Website: http://www.idc.co.za

Small/Medium Enterprise Development Programme (SMEDP)
Skills Support Programme (SSP)

South African Bureau of Standards
Website: http://www.sabs.co.za

Department of Trade & Industry
Website- www.thedti.gov.za

Motor Industry Development Council - responsible for the monitoring and implementation of the Motor Industry Development Programme
Trade and Investment South Africa