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Rover and Out? Globalisation, the West Midlands Auto Cluster, and the end of MG Rover
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ABSTRACT
This paper sets the scene for this Policy Studies special issue on plant closures by outlining the form of the auto cluster in the West Midlands, the nature of structural changes unfolding in the industry, and the decline and eventual collapse of MG Rover (MGR). Structural changes highlighted include: greater pressure on firms to recover costs when technological change has been intensifying, driving up the costs of new model development; increased international sourcing of modular components; and a shift of final assembly operations towards lower cost locations. All of these make maintaining mature clusters such as the West Midlands more challenging for firms and policy makers. The paper then looks a ‘what went wrong’ at MGR. Given long run problems at the firm and its inability to recover costs, BMW’s sale of the firm in 2000 left MGR virtually dead on its feet, and by 2002/3 it was clear to many that the firm was running out of time. Whilst recognising that the firm’s demise was ultimately a long-term failure of management, the paper also looks at other contributing factors, including government policy mistakes over the years, such as the misguided ‘national champions’ approach in the 1950s and 1960s, a failure to integrate activities under nationalisation in the 1970s, a mistaken privatisation to British Aerospace in the 1980s, and a downside of competition policy in ‘allowing’ the sale to a largely inappropriate owner in BMW in the 1990s. The considerable volatility of sterling in recent years hastened the firm’s eventual demise.

Keywords: Automotive industry; Globalisation; West Midlands; MG Rover; Industrial Policy.

1. INTRODUCTION
The structural changes and shifts unfolding in the auto industry have been vividly illustrated through recent events in the West Midlands. These have included the collapse of MG Rover in 2005 and closures of Jaguar’s Brown’s Lane plant in Coventry and Peugeot’s Ryton plant. Add in continuing uncertainty over the future of the Jaguar and Land Rover plants given (at the time of writing) Ford’s attempt to sell-off the brands owing to ongoing losses at Jaguar, and fears over a ‘meltdown’ of assembly activity in the region seem justified. These events have also highlighted the difficulties involved in supporting and developing the auto ‘cluster’ in the region.

This paper explores the background to the MG Rover (MGR) collapse and sets the scene for this special issue. In section 2 it outlines the form of the auto cluster in the West Midlands, putting this into broader context by examining structural changes in the industry. These include: greater pressure on firms to recover costs when technological change has been intensifying, driving up the costs of new model development; increasingly global sourcing; and the growth of assembly operations in lower cost locations in South and Eastern Europe. All of these make maintaining the West Midlands cluster both more necessary and yet also more difficult for policy makers.
The paper then looks a ‘what went wrong’ at MGR, agreeing with the analysis of Holweg and Oliver (2005) which stressed long term problems, the ‘cycle of doom’ at the firm and its inability to recover costs for new model development. Given this position, BMW’s sale of the firm in 2000 left MGR in an unsustainable position, with only a very limited time horizon in which to find an investment partner. Indeed, by 2002/3 it was clear that the firm was running out of time. The paper goes further, however, and examines wider environmental factors contributing to the demise of MGR, in particular government policy mistakes over the years, including a misguided ‘national champions’ approach involving forced mergers in the 1950s and 1960s, a failure to integrate activities under nationalisation in the 1970s, a mistaken privatisation to British Aerospace in the 1980s, and a clear downside of competition policy which resulted in the sale to an inappropriate owner in BMW in the 1990s. Add in the considerable volatility of sterling in recent years, and the firm’s eventual demise came as no surprise to many analysts.

2. THE WEST MIDLANDS AUTO ‘CLUSTER’ IN A RESTRUCTURING GLOBAL INDUSTRY

Shifts in the Global Auto Industry

In the course of its history the auto industry has arguably undergone radical changes described as three “revolutions” by Womack et al (1990), the first two being the introduction of assembly line production by Ford and so-called ‘lean production’ by Toyota.\(^2\) In the past four decades, further radical changes have affected the entire value chain, from manufacturers and suppliers to service providers and dealers (Chanaron 2004, MacNeill and Chanaron 2005)\(^3\) and, since the mid-1990s, a ‘third revolution’ has focused on change through flexibility, with consequent affects on product creation, production and life cycle.

The main drivers of this development are the pressures of cost recovery which, together with intense competition, has led car-makers to seek economies of scale by increasing production volumes, standardising platforms and components and outsourcing ‘non-core’ activities. In addition, increasing regulatory pressures and consumer demands for quality and capability have led to the development of new technologies for more efficient powertrains, reduced weight, hybrid/electric vehicles and bio-fuels, as well as high value electrical, electronic and communications componentry. Finally, market pressures have led to the growth of new segments, such as minivans or small ‘city’ cars, and the need to offer increasing numbers of radical variations whilst still maintaining common ‘under-skin’ platforms.

One result of these developments is too much overall assembly capacity, with around 25% under-utilisation in Western Europe and more than 30% in the developing markets of Central and Eastern Europe. Thus the weakest firms are under intense pressure and although MGR was the first to go under others have also struggled. For example, Fiat was in such difficulties that GM paid $1.5 billion in a divorce settlement in 2005 (although new model launches have since helped the company). More recently Peugeot Citroen has seen disappointing sales and declining profits such that in late 2007 the company announced 8,000 job cuts across Europe. A second outcome has been the rising costs of new model development. In contrast with what is expected under the ‘life cycle’ model of industry development, the ‘crisis of cost recovery’ facing firms has intensified over time. In today’s prices, the cost of getting a
genuinely new model to market lies somewhere between £400 million and £1 billion. As a result, large scale production over different models and brands using a platform sharing approach is vital to generate the cash for future model development, yet at the same time carries with it the risk of diluting brand image, as evidenced by Jaguar’s problems with X-type model, which shared the same platform with the Ford Mondeo and Mazda 6.4

Simultaneously, major manufacturers are developing assembly operations in low cost locations in emerging markets such as central/eastern Europe, or the southern states of the US. Indeed, as well as declining profitability, a key factor in the recent decision by Peugeot-Citroën to close its Ryton plant near Coventry with 2,300 immediate job losses was the opening of a new plant in Slovakia where labour costs are around one quarter those in Britain. Once the decision was taken to expand capacity in Eastern Europe, Ryton was particularly exposed for a number of reasons. Firstly, it was a small plant assembling only the Peugeot 206 from parts brought in from France and secondly cutting each job in France would have been up to three times as expensive. (Bailey and Cowling, 2006). The UK’s flexible labour markets make it as easy to destroy jobs as to create them and the lack of significant domestically-owned manufacturing means that activities in Britain are exposed when transnationals look to cut auto assembly capacity.

Restructuring at a Local Level
With the collapse of MG Rover, and the closure of the Ryton plant, volume assembly in the region has in effect ended. Remaining activity is high-value luxury branded niche-production under the current control of Ford, notably Land Rover and Jaguar in Birmingham/Solihull, with smaller scale production by a newly-independent Aston Martin at Gaydon and at a range of other less known but still significant producers such as LDV Vans (commercial vehicles), Morgan and Westfield (sports cars) and Carbodies (taxis). However, much of the ‘old’ high volume supply matrix still remains with manufacturing concentrated in the main conurbations.

With losses of over $12 billion in 2006, Ford announced in 2007 its intention to sell Jaguar and Land Rover, prompting fears about further capacity cuts and the future of 17,000 Jaguar and Land Rover jobs if a private equity firm acquires them (although at the time of writing, the Indian firm Tata seems the most likely buyer). Meanwhile, Nanjing Auto has plans to re-start small-scale MG sports car assembly at Longbridge in late 2007 with complete ‘knock-down’ kits shipped in from China (although eventual production volumes are uncertain). Longer term there is much scepticism over Nanjing’s ability to develop new models and their commitment to production in the West Midlands, especially given plans to produce and develop models in Oklahoma. However, the takeover in late 2007 of Nanjing by the larger state-owned Chinese firm Shanghai may offer more hope in this regard, given Shanghai’s much larger size and its commitment to R&D activities in the region through its joint venture with Ricardo.

Amongst first tier suppliers there has also been a process of concentration and specialisation around global players, a process accelerated by recent takeover activity. In the West Midlands this leaves first tier firms such as GKN (drivelines), Dana (axles), Bosch (lighting), Delphi (engine management), Johnson Controls (air conditioning and heating), Faurecia (seating), Lear (seating and interiors), Denso
Significant second tier suppliers include Sarginsons Precision Components and Zeus (aluminium castings), Brandaur (pressings), Radshape (sheet metal forming) and Premier Stampings (die forgings) amongst many others.

The cluster is underpinned by research, consultancy and support organisations including Ricardo (engine and drivetrain), Prodrive (performance engineering and motor sport) MIRA (research development and testing centre), the Warwick Manufacturing Group, and the Society of Motor Manufacturers and Traders (SMMT) Industry Forum. The region also benefited from the decision by Ford in 2006 to invest £1 billion in research and development into cleaner technology and hybrid engines, with significant funding coming to Ford’s development centres at Gaydon and Whitley, although there are question marks as to the future if Ford sells Jaguar and Land Rover. Finally, a joint R&D venture (‘Ricardo 2010’) between Ricardo and Shanghai continues to develop the model initially envisaged as the replacement for the Rover 45, reflecting the on-going R&D strengths of the region’s auto cluster despite the MGR collapse. Strengths also remain in engine production and research, as evidenced by the number of patents in this area and BMW’s investment in its Hams Hall engine plant near Birmingham.

Not surprisingly, despite recent plant closures, the West Midlands is still seen as the core of the British automotive industry with some 53,000 jobs (ABI, 2005) under the NACE (EU) industry classification code for motor vehicle and component manufacture, (approximately 30% of the UK total, and around 6% of regional GVA (EMCC, 2004). Local activity includes the manufacture of electrical equipment, around half UK tyre production and some 20% of jobs in processing and shaping glass (e.g. windscreen) as well as retail sales and the distribution of spares and parts (often more profitable than assembly itself) (DTI, 2001). The metal, plastics and rubber products clusters also support the industry and a significant proportion of jobs in the wider manufacturing sector are also automotive related. The industry has also been a major focus for inward investment over the last decade, with nearly 40% of all jobs created by FDI being in auto or auto-related industries (RTF, 2000).

However, recent assembly plant closures and job losses in the components industry have had a major impact. Indeed, from 1998-2005 employment in the region under NACE Code 34 declined by 32% compared with a 23% decline in Great Britain as a whole. (ABI, 2005).\(^5\) In a sense every maturing economy witnesses a shift from manufacturing to services and therein a process of natural ‘de-industrialisation’, with a fall in manufacturing’s share in total employment (Rowthorn and Wells, 1987). However, using Rowthorn and Wells’ (1987) classification, we can differentiate between ‘positive’ and ‘negative’ variants of de-industrialisation. The ‘positive’ type is associated with the ‘normal’ process of industrial dynamism in a ‘developed’ economy, where rapid manufacturing productivity growth releases workers who are absorbed by an expanding service sector. Major auto manufacturers, for example, generally operate on the basis of 5% productivity rise per year. In this positive scenario, unemployment remains low and is frictional in nature as workers search and/or retrain for new service sector employment in an expanding economy where real incomes are rising. In contrast, the ‘negative’ variety is a sign of economic distress; manufacturing is in difficulty and displaced workers are unable to take up

(starters and alternators), TRW (steering, and safety systems), Rockwell (chassis,) and Siemens-VDO (instrumentation).
employment in the service sector. This is associated with rising unemployment and the stagnation of real incomes. Whilst unemployment in the West Midlands is just below the UK average at around 5.3% (on a Labour force survey measure), in Birmingham it remains significantly higher, at around 7.5%. In this sense the auto sector and manufacturing more generally have exhibited signs of both types of de-industrialisation.

An Inter-Regional Network?
Whilst centred in the West Midlands, the ‘cluster’ connections clearly extend to adjacent English regions and Wales. For example, in 2001 there were over 40,000 employees in the neighbouring East Midlands region with some 9,000 in auto assembly (including the Toyota plant at Burnaston) and 8,000 in manufacturing parts and accessories. Another 20,000 were employed in manufacturing autos, parts and accessories in the South East region (plus 1,600 in the motor sport cluster); 13,000 the South West (which includes the Honda plant at Swindon); 12,000 in Wales (suppliers for Honda and engine manufacturing for Ford and Toyota); and 24,000 in the North West (15,000 in motor vehicle assembly via GM and Jaguar/Land Rover in Merseyside, VW Bentley at Crewe and Congleton and Paccar trucks in Leyland, and 9,000 in manufacturing parts and components). Whilst the North West is seen by the DTI (2001) as a ‘distinct’ cluster, component manufacturing is under-represented, indicating supply from elsewhere (notably the West Midlands), and that these are inter-related clusters or even part of a single national cluster. This has implications for the region given, for example, recent uncertainty over GM production at the Vauxhall plant at Ellesmere Port. If a West Midlands ‘cluster’ can be identified, in reality it forms part of an inter-regional or national auto network extending into several other regions. Indeed, the transfer of some Land Rover production by Ford from Birmingham to its Halewood plant on Merseyside, and the sourcing of engines by Ford from Wales and by BMW from Birmingham for MINI production in Oxford are all indicative of the inter-linkages across administrative regions.

Diversity and Challenges to the WM Auto ‘Cluster’
The diversity of component manufacturing in the region is a strength that enables it to supply a wide range of products, as noted by Tilson (1997) a decade ago. At that time many component manufacturers were dependent on local assemblers, with 70% selling their products in the region (ibid; RTF, 2000). With the decline in volume production, suppliers have had to seek markets elsewhere. In this regard, the interconnected nature of the industry and the reach of purchasing provide opportunities. However, most local activities are in the traditional mechanically based areas of vehicle engineering with relatively little involvement in the new high value electronic and electrical componentry making up an increasing proportion of the value of a new car (EMCC, 2004). The lack of a significant ‘home owned’ electronics or telemetry industry puts the region, and the UK as a whole, at a disadvantage.

Tilson (1997) also found, perhaps unsurprisingly, that many companies were experiencing reduced profits through downward pressure on costs from the vehicle makers and major suppliers. The so-called ‘lean paradigm’ which seeks to squeeze out costs and improve productivity has since intensified, leading to significant consolidation at all levels in the supply matrix. Thus only those companies able to innovate and adapt are able to survive. However, firms’ differing levels of competencies are not only reflected in their technological and organisational
trajectories, but also in the way they are networked, engage in collaboration, the markets they serve and their openness beyond the cluster. Tully and Berkeley (2004), drawing on Gordon and McCann’s work on cluster types, identify three groupings of firms in the West Midlands auto ‘cluster’. The first (30% of the sample) does not cooperate or interact with competitors or customers, reflecting a ‘pure agglomeration model’. Firms here are atomistic, and their co-location is in line with a Marshallian view of urban-based firms co-locating to access labour, infrastructure and a flow of ideas and information. The second group (45%) cooperates up and down the supply chain, with more sophisticated, stable and long-term relationships with customers and suppliers underpinned by OEM-driven schemes to drive up quality and productivity. A final group (25%) also collaborates with competitors and agencies in a Granovetter type ‘social network model’, characterised by trust and a lack of opportunism. This group encompasses more complex interpersonal relationships, reflecting a recognised need to work together for common, beneficial goals. As Tully and Berkeley (2004) stress, the more sophisticated a firm’s relationships, the more positive is their outlook, the more informed they are about market trends and the more likely they are to have links with universities. Such firms also invest more in new technologies, have better extra-regional links, and are more likely to be market leaders. They are also more likely to have shifted from high volume, low-value standardised production towards higher value, customised and design-led niche activity. Given the structural changes in the industry, such strategic moves are seen by many as vital for firms to survive yet are also risky. As Donnelly et al (2005) highlight, many regionally-based SMEs “lack the capacity to upgrade their skills, processes or R&D capacities on their own”, noting that “outside assistance is required otherwise many small firms will fail”.

Modularisation, post ‘Japanisation’ and the end of a ‘Geography of Proximity’?

These global trends threaten established local production systems such as in the West Midlands. Under the ‘lean manufacturing’ model OEMs demand high ‘QCD’ (quality, cost and delivery) performance and deal with fewer suppliers to ease coordination costs in managing the supply chain (in effect passing these to first tier suppliers). The overall effect has been to force suppliers to become ‘world class’, leading to a wave of consolidation similar to that for OEMs, with first tier suppliers taking on greater R&D roles (Bergner, 2000) and, in some cases, responsibility for whole systems (e.g., drives or steering), modules (e.g., interiors, ‘front ends’ or ‘corners’) or even assembly work7, as witnessed, for example, at Jaguar’s Birmingham facility where assembly of the aluminium XJ model is undertaken in a joint venture with Stadco. In turn they exert greater power over lower level suppliers (McIvor et al, 1998) as they themselves outsource a range of design and development functions. Thus a ‘post-Japanisation’ phase characterised as ‘at supplier cost’ is emerging where innovative capability is required at all levels in the value chain (see Wells and Rawlinson, 1994). In addition, the internationalisation of component sourcing by assemblers has accelerated (Sadler, 1999; RTF, 2000). Thus, GKN, the region’s largest auto business, has more than 80% of purchasing outside the UK, BMW shifted £1 billion of Rover’s £4 billion annual components spend out of Britain (Financial Times, 24/6/99; 27/04/02), and even MGR was planning significant sourcing from China before its collapse. Of course modularisation, and the outsourcing of bulky components, inevitably results in major suppliers setting up in geographic proximity to the vehicle makers. Thus the list of major suppliers is replicated in most automotive regions including where there is new assembly capacity in Central and Eastern Europe, China and India. However, component sourcing for these plants enables low cost imports to
Western Europe and changes the supply ‘filiere’ (Lagendijk, 1997). Those West Midlands firms that concentrate on high volume, single material and single process parts are at risk in this scenario. As Larsson (2002) notes, first tier suppliers may have little incentive to source components locally for the modules they prepare.

The key points to emerge from this brief overview of the industry and ‘cluster’ are threefold. Firstly, increasingly global sourcing, and a shift to lower wage cost locations, threatens established ‘clusters’ such as the West Midlands, making a cluster policy in this area simultaneously more necessary but more difficult to sustain. The ending of volume car production in the West Midlands through the collapse of MGR and the closure of the Peugeot plant and the shift to smaller scale higher-value production is itself evidence of this. Secondly, even major firms are under intense pressure given the rising costs of new model development, necessitating large scale production, platform sharing strategies and/or joint ventures in order to survive. Thirdly, at the local level, the West Midlands cluster ranges from low-tech ‘metal bashing’ to high-tech composite materials, engines and environmental technologies, with a series of interlinked networks ranging from local supply to global supply chains dominated by the big players. However, as we have highlighted a number of technological and organisational trends pose both opportunities and threats and raise a number of crucial points about the role for policy.

3. MG ROVER: A BRIEF ANATOMY OF FAILURE
At the time of its collapse in 2005 MGR was producing just over 100,000 units a year when it needed to be in the 2-3 million range to generate enough cash for new model development. Not surprisingly, much media attention focused on the short-term failure of the Phoenix management over the proceeding five years and the tiny size of the firm. However, from a wider perspective MGR can be viewed as the unsustainable rump of a government-created giant which never sufficiently integrated activities and which was never in a position to recover the rising costs of new model development. Its long-term decline and ultimate collapse is tied up in a complex vortex of long-running and inter-related factors, including macro-economic instability, the particular short-termism of British finance-industry relations, fratricidal industrial relations, misguided government policy interventions, and above all the firm’s perennial inability to generate the cash needed for new model development (Williams et al, 1994). As noted, this ‘crisis of cost recovery’ has actually intensified over time.

Long-Running Problems and the Failure of a ‘National Champion’
MG Rover itself was the remnant of a government creation of the 1950s and 1960s, the British Leyland Motor Corporation (BLMC, later BL, Austin Rover and finally Rover). As Williams et al dryly observed, the name often changed but the underlying problems remained the same (Williams et al, 1994a). The firm was brought together by the government in effect merging smaller auto manufacturers (Austin, Morris, Triumph, Rover and Jaguar) through various stages into a single firm, in probably the most prominent and infamous example of the misguided policy of creating so-called ‘national champions’. As Owen (1999) commented, the merger “was a mistake both in concept and in execution, reflecting a naïve belief in the advantages of size and in the ability of charismatic individuals to revive declining companies”. Rather than a ‘champion’, a mega-merger was forced on reluctant and resistant incumbent managers. Not surprisingly, suspicion and rivalry across brands hampered efforts to
integrate activities, share high-value components and to strip-out costs leading to continued loss-making. This inability to recover development costs, or the ‘cycle of doom’ as Holweg and Oliver (2005) term it, went back to the 1950s and 1960s, and plagued the firm across decades. After the oil-price shock of the early 1970s, nationalisation in 1975 cost the government, and British taxpayers, billions of pounds in subsidies which went in buying industrial relations peace and limited new model development.

By 1978, the then Austin Rover still assembled over 600,000 units, and exported 40% of them. Its UK market share (for Austin, Morris, Rover and Triumph) was 23.5%, or almost a quarter of all cars sold in the UK that year (Williams et al, 1987). Exports collapsed after this point, however, and never recovered, falling from 40% of Austin Rover output to just 20% in the mid 1980s when the firm assembled around 300,000 cars. This export collapse was linked to the ending of assembly operations by Austin Rover on the continent and the high value of sterling during the early 1980s. Under Thatcher, the company was privatised in 1985 through a sale to British Aerospace (BAe) which was diversifying away from aircraft. After the failure of its regional jet business, BAe sold Rover to BMW for £800 million. As Hutton (1999) noted, the sale of Rover to a foreign firm reflected the twin factors of British short-termism (BAe’s desire for cash) and the openness of British industry and government to penetration by foreign investment. Thereby Rover became part of BMW, but probably for the ‘wrong’ reasons. BAe needed cash and BMW wanted the four wheel drive Land Rover division - as at that time the company did not have the resources to develop its own model to compete in an expanding market segment - and also to double production volume (at the time both had annual sales of around 440,000.) At the time many commentators recognised the difficulties of achieving economies of scale whilst the cars were so different in design and driveline (Bailey et al, 1994). Although some criticism has also been levelled at the government’s failure to heed these warnings it is noteworthy that the Rover Management Board were in favour of a BMW purchase since there was an historic connection between the companies and they saw the possibility of joining BMW in the profitable premium segment.

Life under BMW: The ‘English Patient’
Whatever the precise reasons for BMW’s acquisition, problems were immediately apparent. Rover under government and then BAe ownership had relied heavily on a joint venture (JV) with Honda through which Honda designs were badged and sold as Rovers to European markets, saving Rover considerable R&D costs and periodically enabling it to make modest profits. Honda executives were unimpressed when Rover was abruptly sold to a competitor, and Honda subsequently sold its 20% stake. As commentators warned at the time, it was not clear what BMW would actually make after the JV with Honda was terminated. Thus, although one joint Honda-Rover model programme, the Honda Civic - Rover 400/45 continued into production, BMW was now on its own. As observed by Williams et al (1994a), BMW did not have the capacity to develop the Rover brand and style of car and therefore jobs were at risk. Logic suggested that, since the UK was the company’s second market after Germany, the BMW -3 series should be made at Longbridge. However, concerns about quality and worries about dilution of the BMW brand prevented this ever happening.

Not surprisingly, through a combination of model obsolescence (as BMW struggled to bring on line new models), marketing mistakes, and macro-economic factors such as
the rise in the value of sterling, Rover sales declined and losses grew to £500 million a year by the late 1990s. Whilst BMW invested heavily in the Land Rover plant at Solihull (Birmingham) and at Cowley (Oxford), the position of Longbridge was always vulnerable, with BMW threatening early on to switch production of the new MINI elsewhere if productivity did not improve and deals on working conditions were not agreed (Bailey, 2003). Similarly, in March 1999 BMW threatened to shift production to Hungary if a state aid package was not agreed by the government to build a new model, the R30. A £152 million subsidy package was agreed with the government in mid-1999 in return for a planned £1.7 billion investment by BMW in Longbridge. After a complaint by Porsche, however, the European Commission decided to investigate the aid package under EU state-aid rules. Before the prolonged investigation was finished, however, BMW announced in March 2000 that it was pulling out, leading to the buy-out by Phoenix.

It was clear to several commentators (Williams et al, 1994; Bailey et al, 1994) that BMW’s purchase of Rover in 1994 was a corporate mistake for BMW and likely to cause severe problems for Rover. As Wolf later commented (Financial Times, 22/03/99), “BMW did not realise how bad a buy Rover would be”. The ‘failure’ of competition policy contributed to this problem by allowing BMW to buy Rover when it was clear to many that it was an inappropriate owner (Bailey et al, 1994). It is widely accepted that local production systems can be improved by firms - whether domestic or foreign - that bring new technology and investment but can also be damaged through takeovers (Harrison, 1994). Whilst BMW was seen by many as an inappropriate owner at the time of its takeover of Rover, Volkswagen (which had earlier shown interest) might have been much more suitable in that it could have extended its strategy of sharing platforms across brands to MGR as worked so well with VW, Audi, Seat and Skoda. It should be stressed that the case here is not anti-inward investment per se but rather focuses on the suitability of acquiring firms (whether domestic or foreign) for the local production system. None of this, of course, was considered by the government as the only perceived role for intervention was on a narrow competition basis.

Not surprisingly, despite the substantial investment in the late 1990s, BMW decided in 2000 to break up the company, selling Land-Rover to Ford, retaining the Cowley factory in Oxford (for the new MINI) and the Hams Hall engine plant and selling the remaining Rover division with its Longbridge factory for a symbolic £10 to the Phoenix consortium. Despite the hopes raised in 2000, BMW’s withdrawal left MGR virtually dead on its feet. The cancellation of the R30 project, which was the key mid-sized model being developed under BMW as a replacement for the R45 meant that a whole cycle of model development had been missed (Holweg and Oliver, 2005). The firm was now brutally exposed as its aged model line became increasingly unattractive to buyers and it had only a very limited time horizon in which to find a partner; by 2002/3 it was clear to many that the firm was running out of time (Bailey, 2003). The unsustainable position of the firm was evidenced by the way it consumed what assets it had.

Exchange Rate Volatility
Another view is that BMW acquired Rover not only for its 4WD competencies but also to obtain a manufacturing base “in a country which had lower labour costs than Germany and… a stable labour relations climate” (Owen, 1999). Any such relative
unit labour cost advantage was soon eliminated by the sustained and marked appreciation in the value of sterling from 1994 onwards. At the time of the takeover in 1994, sterling was valued in the range DM2.40 – 2.50, making auto assembly in the UK attractive to firms such as BMW. BMW budgeted for a turnaround plan at Rover with sterling at around DM2.90, yet by January 2000 sterling had risen to DM3.20, and Church (1999) estimated that by July 1999 the Sterling effective exchange rate was overvalued by around 20%. This over-appreciation exacerbated Rover’s problems, making exports (of increasingly aged models) extremely difficult at a time when the company was losing home sales and trying to re-orientate its sales towards export markets.

Such exchange rate volatility continues to make conditions for the region’s manufacturers extremely difficult and has accelerated the shift to sourcing overseas, as Bailey (2007) notes. At the time of writing, Sterling is at a twenty-six year high against the dollar of over $2. This weak dollar makes selling to the US very difficult and has impacted severely on firms such as Jaguar as over a half of its sales are in the US market, especially for the large XJ model. As much as a half of Ford’s Premier Auto Group’s losses in recent years could be down to this exchange rate issue. This exchange rate pressure accelerates the trend towards smaller-scale luxury branded production as noted in section two. More broadly, cluster policies and development goals in a manufacturing-orientated region can be undermined by such major exchange rate fluctuations. There may be good reasons for Britain remaining outside of the Eurozone, but the ‘cost’ of exchange rate volatility has not gone away, and MGR’s most recent difficulties are a stark illustration of this – the story could have been quite different in the absence of such sterling over-appreciation. Indeed, the reduction of exchange rate risk through Euro membership could be a significant benefit to auto assemblers based in the UK, although this would not help Jaguar and Land Rover in selling to the key US market.

**Phoenix: An Unsustainable Strategy**

On taking over in 2000, the Phoenix management set four strategic objectives for the firm: maintaining production at 200,000 units, bringing a new model to market (the replacement for the medium-sized R45); finding a partner for new model development; and returning to profit. But with a limited and aging product range, and in particular the lack of models in key growth segments (such as compact cars, people carriers and sports utility vehicles), this was always going to be a huge challenge. Whilst sales held up reasonably well in 2000, thereafter they declined rapidly and by 2002/3 it became increasingly clear to commentators that the firm had limited time in which to find a partner to bring new models to market (Bailey, 2003).

Some imaginative re-badging of aged Rover designs as MGs bought a little time, but over the next few years MGR sold off its only real assets (land, the profitable parts business and finance arm and later its intellectual property rights) in an increasingly desperate attempt to keep going. By 2004, output had dwindled to around 115,000 units and R&D spending had dried up. No partnership deal had been delivered other than an agreement with Tata to supply the small ‘City Rover’ model – which was marketed at an uncompetitive price and failed to sell in significant numbers. With limited room for manoeuvre in that many of the big players had already entered partnership deals, it became clear that the very survival of MGR depended on a deal with Shanghai Automotive to jointly develop models. However, Shanghai became
increasingly concerned about the financial viability of MGR and feared picking up sizeable redundancy and pensions liabilities and talks dragged on for several months before ending in failure in April 2005. At that point the firm was forced into administration, with the remaining assets later bought for £60 million by Nanjing, another Chinese firm. All but two production lines, along with the Powertrain engine production plant, were then stripped out from Longbridge in a ‘lift and shift’ move to China.

New Hopes or False Dawn?
Nanjing aimed to re-start small scale production of MG TF sports cars at Longbridge in late 2007, with complete knock-down kits being imported from China. However, production has been delayed given quality concerns, and to-date only a very limited number have been made. The eventual production volume is as yet unclear and likely to be far smaller than the 100,000 units a year initially suggested by Nanjing at the time of takeover. Thus whilst of considerable significance in terms of redeveloping the Longbridge site, only ‘a few hundred’ jobs at best will be created. Initially it seemed that there would also be no substantial R&D centre, with the latter likely to be located at Nanjing’s new MG plant in Oklahoma. This represented something of a missed opportunity when compared with what was potentially on offer from a Shanghai Auto takeover of MGR. More recent developments look more promising, however. Shanghai Auto (which brought the intellectual property rights to the Rover 25 and 75 and the replacement model for the R45 in development at the time of the MGR collapse) has developed a joint venture with Ricardo to develop the new model. Nanjing has also reversed its previously announced strategy and has stated that it will bring its R&D base to Longbridge. Most recently, in late 2007, Shanghai acquired the car making operations of Nanjing with Chinese government encouragement. This is likely to strengthen the likelihood of genuine R&D coming back to Longbridge. Auto assembly (even if on a small scale) and R&D may be returning to Longbridge, albeit under Chinese state ownership.

4. SUMMARY AND CONCLUSIONS
A number of technological and structural changes are unfolding in the auto industry, including: more rapid technological change which has driven up the costs of new model development, in turn increasing the pressure on firms to recover costs; more international sourcing of components with a greater role for larger first tier suppliers; and a shift of labour-intensive assembly operations towards lower cost locations as trade barriers have come down and as globalisation proceeds. All of these make maintaining the West Midlands cluster more challenging for firms and policy makers through cluster policy. Manufacturers and policy makers are aware of the ‘threat’ from low cost competitor locations in Central and Eastern Europe, and in the longer term, from India and China. At the same time, possibilities for cooperation are evident in the recent Shanghai-Ricardo R&D venture in the West Midlands.

Within this broader context, MGR was the unprofitable rump of a former giant which for years had struggled to generate cash for new models owing in part to a lack of integration across the firm. The firm became reliant on Honda for new models in the 1980s before being acquired by BMW. The latter’s withdrawal from the firm in 2000 left MGR virtually dead on its feet, and by 2002/3 it was clear to many that the firm was running out of time. Also significant in the firm’s demise, however, were a
number of government policy mistakes over the years, including a misguided ‘national champions’ approach, a failure to integrate activities under nationalisation, a mistaken privatisation, and the downside of competition policy which saw the sale to an inappropriate owner in BMW in the 1990s. Add in the considerable volatility of sterling and the scene was set for the firm’s demise. The impact of this collapse and policy responses will be explored in papers in this issue. This will include a comparative analysis, comparing policy responses (see Thomas et al) and labour market outcomes (Armstrong et al) in the case of MGR in Birmingham and Mitsubishi in Adelaide.

REFERENCES

FINANCIAL TIMES (2002) Defiant Carmaker Foresees a Positive Route to the Future. 27/04/02: 3.

1 Birmingham Business School, UK, Graduate School of Business, Nihon University, Tokyo, and Centre for Urban and Regional Studies, University of Birmingham respectively. The authors wish to acknowledge the support of the ESRC under award number RES-000-22-2478. contact: d.g.bailey@bham.ac.uk
3 See Clark (2006) who draws on Abernathy’s work highlighting the unexpected and significant increase in the level of innovation at Ford in the 1960s.

4 A key issue for the future is what effect the anticipated shift to more specialised ‘short-run’ production, including electric/hybrid powered autos, will have on development costs, minimum efficient scales and the players involved.

5 Taking a broad definition of the filiere to include auto-related industries gave a figure of around 120,000 people in 2001, higher than the 100,000 figure given in RTF (2000). More recently, Donnelly et al (2005) put the numbers of workers in the broadly-defined auto industry in the region as low as 65,000. If correct, this would signify as many as 35,000 job losses over 2000-2005.

6 Although in 2007 GM announced that the new model would be assembled there, safeguarding 2,200 direct jobs and more in the supply chain.

7 Bergner (2000) notes that between 1988 and 1998 the global number of direct component suppliers to OEMs and the aftermarket shrank from 30,000 to 8,000. This number is expected to fall considerably in the future. For example, McIvor et al (1998) argue that 50% of European suppliers will cease to exist in their current form owing to pressure from OEMs to reduce costs and innovate.

8 Jaguar was separated and privatised in the 1980s, acquired by Ford in 1989 and sold again to Ford’s US parent in 1991, later being sold to the Indian conglomerate Tata in 2008.

9 For example, in the 1920s BMW had manufactured versions of the Austin 7 under licence.

10 Although BMW was able to access Land Rover’s four wheel drive (4WD) technology and was later able to produce its own 4WD models.