

**THE SOUTH AFRICAN GOVERNMENT'S INITIATIVE TO  
OPTIMISE THE ECONOMY THROUGH THE INDUSTRIAL  
DEVELOPMENT ZONES.**

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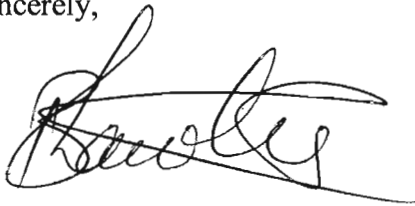
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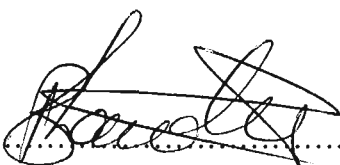
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## DECLARATION

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

Signed

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Date

.....SEPTEMBER 2003.....

## **ACKNOWLEDGEMENTS**

My sincere appreciation to all who have assisted, guided and made this MBA possible.

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To my fellow UND MBA students – thanks for the unforgettable experience.

## **GLOSSARY OF TERMS**

CDC	Coega Development Corporation
DTI	Department of Trade and Industry (South Africa)
EPZ **	Export Processing Zone
GEAR	Growth, Employment and Redistribution – Economic Policy
IDC	Industrial Development Corporation
IDZ **	Industrial Development Zone
IVP	Import Verification Programme
RDP	Reconstruction and Development Programme – Economic Policy
RILS	Regional Industrial Location Studies
SDI	Spatial Development Zone
SGS	Société Générale de Surveillance

*(\*\*) Note: Although referring to the same concept, EPZ is a term used in various other countries, whereas IDZ is term used specifically in the South African context. For the purpose of discussion, these terms may be used interchangeably in this document.*

## **ABSTRACT**

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There is a close relationship between the industrial policies pursued by a government, and the nature and pace of the country's developmental path. The impact of industrial policy is important as it effects the social as well as economic development of the country. The South African government has developed an industrial policy as part of an aggressive strategy to position South Africa within the global economy, and stimulate the national economy through export-led growth for sustainable socio-economic development.

The Industrial Development Zone (IDZ) Programme is a strategic initiative developed by the South African Department of Trade and Industry to encourage economic growth through export-orientated industry. The IDZs will operate as liberalised duty free and multi-sector development areas, and have been designed to have a simplified business environment with streamlined administrative systems to attract investment and maximise private sector participation in all aspects of zone operations and development.

The aim of this study is two-fold. Firstly to examine the extent to which the IDZ initiative can be expected to stimulate economic growth; and secondly to make recommendations to maximise the operations of the IDZs, which will ultimately add value to the resultant effects in the national economy.

An examination of economic industrial location and trade theory has been undertaken and to address the question of whether the location of industry can be a stimulant or an impediment to plans for the involvement of international trade in the strategic development of the national economy.

A second consideration is whether the IDZs are a strategically suitable means to achieve these economic objectives. In order to give perspective to this question, the concept of IDZs as they have been applied in other areas of the world (although termed differently in different areas) has been considered, as well as the IDZs as designed and intended for the South Africa.

An assessment of the suitability of this initiative involves an evaluation of the extent to which it matches the specific needs of the South African economy. Data on the South African economic situation, patterns and predicted trends has been gathered,

The findings of this study, based on the theories and empirical evidence, are:

- 1) The localisation of industry and supply-side features of the IDZs will create the conditions for the concentrated growth of an export-driven economy. Foreign direct investment and increased production in this sector will boost export and increase international competitiveness.
- 2) The IDZs can only be effective in meeting economic objectives if they are run with optimal expertise and service levels. The efficient and effective functioning of the IDZs will ensure concentrated growth in the industrial sector aimed at the export market. Specific recommendations are thus made for a private company with relevant experience and expertise to act in the capacity of an IDZ operator to optimise the level of service and operation of the IDZ.

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# **CHAPTER 1**

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## **INTRODUCTION TO THE STUDY**

### **1.1 INTRODUCTION**

South Africa's economic policy is aimed at levels of sustained growth that will result in a lasting reduction in unemployment and poverty. In the State of the Nation Address, 2001, President Mbeki summed up South Africa's economic objectives in the current period:

*'The objectives we seek to achieve are moving the economy onto a high-growth path, increasing its competitiveness and efficiency, raising employment levels, and reducing poverty and persistent inequalities.'*

The macro-economic policy through which these objectives are to be achieved is known as Growth, Employment and Redistribution (GEAR). GEAR attempts to strike the necessary relationship between accelerating economic growth, on the one hand and social service delivery and job creation, on the other. It emphasises economic stability as a prerequisite for pursuing micro-economic reforms aimed at fostering a faster job-creating economic path.

Industrial policy is a part of the macro-economic policy through which the Government has embarked on an aggressive strategy to position South Africa within the global economy. A key initiative within this strategy is the Department of Trade and Industry's Industrial Development Zone (IDZ) Programme to encourage economic growth through export orientated industry. The IDZ will operate as a liberalised duty-free and multi sector development area. A simplified business environment has been designed with streamlined administrative systems to attract investment and maximise private sector participation in all aspects of zone operations and development.

The Department of Trade and Industry (DTI) has earmarked a number of areas for IDZs. These zones are purpose built industrial estates linked to an international port or airport, and have been specifically designated for new investment in export driven

industries. The establishment of IDZs are provided for in terms of the Manufacturing Development Act No. 187 of 1993 as amended under Regulation Gazette No. 6936, Vol. 426, December 2000, No. 21803 (Eastern Cape Development Corp).

The aim of this research is to assess the suitability of the IDZs in achieving the objectives set by the Government in terms of economic development.

## **1.2 BACKGROUND OF THE RESEARCH**

South Africa's economic policy is aimed at levels of sustained growth that will result in a lasting reduction in unemployment and poverty. The macro-economic policy, known as Growth, Employment and Redistribution (GEAR), emphasises economic stability as a means to the micro-economic reforms aimed at fostering a faster job-creating economic path.

IDZs are special geographic areas where it is intended that particular commercial activities take place. The DTI intends to establish IDZs at a number of locations around the country, in particular, in the Eastern Cape, KwaZulu-Natal and Guateng.

According to the Coega Development Corporation (CDC), South African IDZs will have three key components:

1. A Customs Secured Area with its own South Africa Revenue Services facilities and personnel. This will be deemed to be outside South Africa for customs purposes. It will enable companies to establish themselves in an IDZ Customs Secured Area to import on duty-free basis raw materials required for added value manufacturing of goods for export. Imports from foreign countries will be duty free and those from South Africa will be VAT free.
2. An Industrial and Services Area adjacent to the Customs Secured Area. This is expected to attract mainly service and supply industries supporting large manufacturers in the Customs Secured Area. It will support industries and service providers that require leading edge industrial and office park environments as well as other services offered by zone developers.

3. A One-Stop Centre that will facilitate and expedite regulatory procedures and requirements.

The Coega IDZ was the first IDZ to be promulgated in South Africa. The Coega Project is a development initiative managed by the CDC within the Nelson Mandela Metropolitan Municipality, adjacent to the City of Port Elizabeth. This project comprises of two components: a new deepwater port (Port of Ngqura) and an IDZ. The IDZ covers 12 000 hectares of land adjacent to the port and is intended to attract domestic and foreign investment into the industrial and commercial parks.

The Government's objective for the Coega project is position the Coega IDZ as a viable destination for foreign direct investment, which can act as a springboard to international trade. It is integrally linked to other government programmes aimed at the development of the national economy generally, and the economic regeneration of the Eastern Cape specifically. These projects focus on skills development, tourism initiatives, infrastructure provision and SMME development.

The resultant benefits will be to the economy in terms of GDP, the Eastern Cape in terms of job creation and the development of local business, and to the fiscus in terms of tax and dividends to the shareholder. Government will also enjoy the benefits as a shareholder in the CDC. In the Eastern Cape, all the returns on investments made in the CDC by the Provincial Government will be made available for reinvestment in the socio-economic development in the province.

Job creation forms an essential element of the South African Government's macro-economic policy. The success of the Coega IDZ will be judged by its ability to create sustainable employment in the Eastern Cape and beyond. It has been forecasted that more than 20 000 permanent jobs, and more than 50 000 construction jobs will be created as a result of the development of the initial phase of the Coega project. The construction of infrastructure in the IDZ will result in 8000 jobs in the local building industry; with a further 2500 permanent jobs being created. By far the most jobs created will be as a result of the investments by the private sector in industries located in the IDZ.

The Coega project includes the construction of a new deepwater port. According to a study by Stellenbosch based Maritime Education Research and Information Technology (PTY) LTD (as cited by the National Ports Authority, 2002), the existing ports of Cape Town, Durban and Port Elizabeth will run out of container handling capacity by 2020 – even if billions of Rand are spent on upgrading them during the next 19 years. The report finds that the Net Present Value and the Benefit / Cost Ratio of the investment in the container port and terminal at Coega signify that it is the best option for providing the additional container handling capacity needed in South African ports until 2020, when further port development will be needed. This means that the port is necessary for the continued economic growth of South Africa. Traffic generated out of the adjacent IDZ (Coega) will make it more profitable. The port is an integral part of the IDZ, and will service the industries in the zone.

The Coega Project has been at the forefront of the country's macro-economic development strategy through providing world-class, purpose-built infrastructure as an enabling platform to attract foreign direct investment and increase South Africa's competitiveness. This strategy is aimed at moving the economy from import-substitution to one that is export orientated. Without the basic infrastructure to support the desirable investment levels, South Africa is not able to compete in the global markets. The State, through the R800 million funding of the initial stages of Coega, intends to play a critical role in providing this infrastructural framework, in order to facilitate investments in industrial projects by the private sector.

### **1.3 MOTIVATION OF THE RESEARCH**

The establishment of IDZs is a major development aimed at achieving certain strategic objectives. The South African Government, for example, is investing at least R800 million in the first phase of the construction of the Coega IDZ, and an entirely new port is to be built in Port Elizabeth. The Coega Project is expected to take fifty years to construct.

This is a significant undertaking by the Government in order to move the South African economy toward an economy driven by an export market. Beside the

Government involvement, there will be a massive investment by the private sector in the development of the IDZs. It is imperative that a comprehensive study is undertaken which will assess how suitable this project, and similar initiatives are in achieving economic growth.

Industrial projects such as this will not only have positive effects. There is already resistance from environmental groups, for example, who argue the detrimental long-term effects of these projects. There is also some resistance, to a lesser extent, from some economists who argue that the projects will not produce the results its supporters advocate. An independent study of the suitability of this project is therefore required.

#### **1.4 VALUE OF THE PROJECT**

The South African Government's aim is to encourage foreign direct investment and an export driven market environment, to stimulate both the economies both at a national level, and the economic regeneration of local areas.

The resultant benefits will be to the national economy in terms of GDP, to the local sectors in terms of job creation and to the private sector in the development of local business.

The IDZ projects appear to be well-planned ventures. The value of this research proposal is that it will provide an unbiased report on the suitability of these projects in future economic growth. The researcher is not a stakeholder in the project, or in the export market. This assessment will be made by an independent observer.

#### **1.5 PROBLEM STATEMENT**

To what extent is the development of the IDZ a suitable means to achieve the Government's objectives of creating an export driven economy and encouraging foreign direct investment?



## **1.6 OBJECTIVES OF THE STUDY**

The objectives of this research is to assess the expected extent of the contribution to the economy as a result of the of the IDZ (of creating an export driven economy) against the following Government objectives:

- ⇒ moving the economy onto a high-growth path
- ⇒ increasing its competitiveness
- ⇒ increasing efficiency
- ⇒ raising employment levels
- ⇒ reducing poverty and persistent inequalities

## **1.7 RESEARCH METHODOLOGY**

### **Data Collection**

The method of data collection will be that of literature review. Detailed data of the following will be gathered:

- ⇒ Statistics
- ⇒ Current economic indicators
- ⇒ Current export market mechanisms
- ⇒ Projected economic results (due to the development of the IDZ)
- ⇒ Proposed systems and mechanisms that will exist only in the IDZ, and are therefore expected to encourage export driven growth.
- ⇒ External conditions (i.e. social, political or economic) that could impact on the operations of the IDZ, and its contribution to economic growth.

### **Data analysis and interpretation**

The purpose of this research proposal is to evaluate the suitability of IDZs, such as the Coega project in enabling the achievement of the Government's economic growth objectives. This evaluation will be through aspects of relevant economic theory as well the strategic theoretical model of suitability as outlined by Johnson and Scholes. Suitability is defined as 'a broad assessment of whether the strategy addresses the circumstances in which the organisation is operating'. (Johnson & Scholes, 1999).

As a part of this strategic evaluation framework, a value chain analysis will be undertaken to assess whether the strategy is appropriate. Value chain analysis describes the activities within and around the organisation and relates them to an analysis of the strength of the organisation (Johnson and Scholes, 1999:359). Specifically, the proposed competencies of the IDZ will be evaluated in terms of expected contribution to the South African economy's competitive performance.

Various elements and participants of economic activity will be assessed to evaluate whether the proposed elements specific to the IDZ create an economic environment conducive to sustainable development in an export driven sector.

In essence, a gap analysis will be undertaken. By using the data collected regarding past and current economic conditions, we are able to describe the current economic situation. The literature outlines the goals that these projects are supposed to achieve for the competitiveness and efficiency of the South African economy. The analysis and interpretation of the data collected in the study will be an assessment of the extent to which the IDZs are likely to achieve those goals.

This strategic analysis will assess the extent to which the IDZs can be expected to address areas of macro-economic development as proposed by the Government. The analysis will assess the extent to which this strategy of economic development can avoid the threats and remedy weaknesses imposed by external economic environmental factors. It will also assess how the IDZs can capitalise on the strength of South African resources, and can both create and exploit future opportunities, and how a private company can maximise the features by undertaking the role of an IDZ operator.

## **1.8 LIMITATIONS OF THE PROJECT**

As this is a privately funded project, the researcher is limited in terms of time and financial resources.



The main limitation of this project is that the result will be a report based on an opinion formed from the careful analysis of the information collected. Much of the data gathered will be of a speculative nature of future trends and conditions. The result will not be absolute.

A further limitation is that given the extensive nature of the data available, it will not be possible to conduct an exhaustive study. The study will, however, provide an answer to the research question based on a wealth of credible information, and careful analysis thereof.

A time limit will have to be place on the study. As the focus is on an event in the future, as time draws on, and as the IDZ development becomes more current and topical, the amount of information on the topic will increase. It will not be possible to incorporate all new information on an ongoing basis, and a limit will have to be imposed on the gathering of information stage, so that analysis and interpretation can be conducted.

## **1.9 STRUCTURE OF THE STUDY**

The structure of the study is as follows:

⇒ Chapter 1

Provides a basic introduction to the study, in terms of why this study has been undertaken and the format is shall follow;

⇒ Chapter 2

Review of industrial location and trade theory, strategic theory and an overview of pertinent aspects of the South African economy.

⇒ Chapter 3

This chapter outlines the case study by first looking at industrial development zones in the global and then South African context. The chapter also includes an overview of Scoot General de Surveillance, a company with a recommended role in the industrial development zones.

⇒ Chapter 4

In this chapter, elements of the case discussed in Chapter 3 are evaluated against the theoretical constructs discussed in Chapter 2. This forms the basis for the recommendations made in Chapter 5.

⇒ Chapter 5

Recommendations are made to address both the opportunities and weakness found during the evaluation of the case material.

## **1.10 SUMMARY**

The IDZ initiative is a major development in order to achieve certain strategic objectives. This research has been undertaken in order to examine the extent to which this initiative can be expected to stimulate economic growth; and to make recommendations to maximise the operations of the IDZs, which will ultimately add value to the resultant effects in the national economy.

## **CHAPTER 2**

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### **THEORY**

#### **2.1 INTRODUCTION**

The DTI (2003) states that the Government's objective is to achieve its vision of an adaptive economy characterised by growth, employment and equity by 2014. This vision can only be achieved by careful implementation of a strategy designed to stimulate economic growth.

Various economic theories related to industry and economic growth will be discussed in relation to the question of whether the location of industry in South Africa could be a stimulant or an impediment to the country's plans concerning international trade and competitiveness. This is followed by an overview of strategic theory, in order to establish why the government has chosen this particular growth path. Trade policy in South Africa is based on a relationship between industry, trade liberalisation, and economic growth and development. More specifically, then, South Africa's economy will be examined to highlight features and trends that are pertinent to the later evaluation of the strategic use of an industry-focused drive to stimulate economic growth.

#### **2.2 ECONOMIC THEORY**

The success of the South African Government's Global Economic Strategy (GES), as discussed by Naude and Harmse (2002) depends to a significant extent on the ability of the economy to export in key sectors (e.g. manufacturing), thereby enhancing the country's international trade position and its competitiveness in the global market. However, the formulation of an industrial strategy that facilitates structural change in the South African economy is a prerequisite foundation for that success. The location of industry to maximise the contribution of industry to export competitiveness is also a fundamental component of success for this initiative.

With these linkages in mind, it is significant that the GES contains references to the need for coherence between industrial strategy and international trade, through a number of industry cluster studies for key industries. GES includes a programme of attracting industries into EPZs and IDZs where firms will be able to gain various advantages in terms of reduced tariffs on inputs and export incentives. (Naude and Harmse, 2002).

This section will examine the linkages between industrial strategy and international trade, by examining the connection between trade theory and location theory and then a review of the relevant economic theory. The theoretical review covers Marshall's agglomeration theory, Weber's location theory and the Heckscher-Ohlin theory of international trade. Key government programmes that have a spatial component are examined in terms of their capacity for improving exports and ultimately output and employment. (Naude and Harmse, 2002).

### **2.2.1 Marshall's Agglomeration Theory**

The first major examination of industry concentration and localisation of specialised industries was that of Marshall (1920 as cited in Naude and Harmse, 2002). Having noticed the concentration of certain industries in particular centres, Marshall suggested that the localisation of industries arose through factors such as:

- ⇒ Physical conditions (climate, soil type and resources such as mineral deposits. Industry location followed easy access to water and mineral deposits);
- ⇒ Patronage of courts (the demands of a royal court for certain goods attracted skilled workers who passed on their knowledge and led to the replication of those skills even after the court had moved on);
- ⇒ Deliberate invitation of rulers (rulers often invited skilled artisans to settle in specific centres. These workers often passed on skills to the locals, thereby broadening the overall skill base).

Once industry has become localised, it tends to remain in that locality for a considerable time. The advantages of localisation were put forward by Marshall as:

- ⇒ the hereditary skills nurtured over time,
- ⇒ the growth of subsidiary activities,
- ⇒ use of highly specialised machinery,
- ⇒ benefits from technological spillovers, and
- ⇒ a local market for special skills.

However, disadvantages could also arise:

- ⇒ a heavily localised industry could make extreme demands for one kind of labour, e.g. the dominance of iron industries offered no employment to women, so that wages and labour costs were high while average earning for households were low;
- ⇒ a region dominated by one industry was vulnerable if this industry experienced reduced demand.

The localisation of industries was affected by external factors such as improvements in the means of communication, be it in technical terms or through reduced transportation and freight costs. This would obviate the need for many different industries to concentrate and enable them to rather remain localised some distance from centres of demand.

The issue of agglomeration effects was also examined and deemed important in two respects:

- ⇒ Results in positive externalities on existing firms already located in an area; and
- ⇒ Influences firms' location choice and reinforces positive externalities (positive circle of benefits)

This notion of agglomeration effects is based on the premise that firms in the same industry tend to group together or cluster in certain regions. In economic terms, agglomeration effects arise through financial and technological externalities, which encourage industry localisation. In terms of empirical work on agglomeration effects, Head, et al (1995 as cited in Naude and Harmse,

2002) make the point that much empirical work needs to be done to establish the extent of the effects of these externalities emanating from geographical proximity.

### **2.2.2. Weber's Location Theory**

Weber (1929 as cited in Naude and Harmse, 2002) developed two regional cost factors that are fundamental to the location of industry:

- Transportation costs, and
- Labour costs.

Although it can be argued that transport costs are themselves determined by labour costs (see Weber, 1929 as cited in Naude and Harmse, 2002), they ought to be examined separately to examine their effect on industrial location decisions specifically.

Weber's analysis is extremely important in terms of its treatment of transport and labour costs i.e. whether it held one of the two components constant while allowing the other to vary. Permitting transport costs to vary while holding labour costs constant, Weber formulated his first general rule: that **the location of manufacturing industries would be determined by the ratio between the "weight of localised material and the weight of the product"**. (Naude and Harmse, 2002)

The influence of the variation in labour costs would be determined by the "labour coefficient" or the ratio between the cost of labour per ton of product (labour index) and the total weight of all the goods (raw materials, fuels etc) transported. The aforementioned total weight was termed the "locational weight". This combination led to the second general rule: **"When labour costs are varied, an industry deviates from its transport locations in proportion to the size of its labour coefficient"**. (Naude and Harmse, 2002)



### **2.2.3 Heckscher-Ohlin Theory of International Trade**

The Heckscher-Ohlin contribution to international trade theory is widely documented, however, only a brief account is necessary for the purpose of this discussion.

The principal tenets of this theory are that a country will export the commodity, which intensively uses its relatively abundant production factor. That is, of two countries producing two goods with two factors of production, the country with a relative abundance of labour will export the labour-intensive commodity, while the country with an abundance of capital will export the capital-intensive goods. The implication of this discussion is that labour-intensive industries will locate in the country with an abundance of labour, while capital-intensive industries will locate in the country with an abundance of capital.

### **2.2.4 The Theory of the “Core” and the “Periphery”**

The work undertaken most recently by Krugman and Venables (1998 as cited in Naude and Harmse, 2002) puts forward the notion of a core and a periphery in economic development and international trade, in the context of globalisation. This theory is also applicable in the case of regions within the country.

This model uses a world consisting of two regions, North and South, each producing two goods: agricultural (characterised by constant returns to scale) and manufactured goods (characterised by increasing returns). The latter include intermediate goods used in the production process as well as goods for final demand by consumers. Neither region has a comparative advantage in either of the goods. However, transport costs between the regions are initially extremely high. Each region will be self-sufficient and produce goods for its own consumption.

As transportation costs fall over time, trade between the regions takes place. If there are many different kinds of manufacturers, two-way trade in these occurs between the regions. If transportation costs remain high, no specialisation of activities occurs in the regions. As one region emerges with a stronger manufacturing base, so it will eventually attract more industries involved in

intermediate activities (the production process – leading to backward linkages between industries). If one region produces more intermediate goods, better access to these goods will mean reduced costs of production of final goods (forward linkages). This will result in increased movement of manufacturing to that region. When transportation costs fall below a critical level, the global economy will organise itself into an industrialised core and deindustrialised periphery.

Meanwhile, demand for labour increases in the industrial region or core, through the concentration and growth of industry, and a fall in the demand of labour in the periphery. Real wages then fall in the periphery and increase in the core. *“Global economic integration leads to uneven development”* (Krugman and Venables, 1998 as cited in Naude and Harmse, 2002). If transport costs continue to fall, the advantage of being located closer to markets and suppliers begin to decline. The periphery then emerges with an advantage in the form of a lower wage rate, to the point where this outweighs the disadvantage of distance from markets and suppliers. Manufacturing activities then moves from the core to the periphery, enabling a convergence of wage rates and economic growth between regions. (Naude and Harmse, 2002)

### **2.2.5 Linkages between Trade Theory and Location Theory**

An important concept to examine is the linkage between industry location and agglomeration effects, as first proposed by Weber (1929) and Marshall (1920) respectively, and the Heckscher-Ohlin theory of international trade. The linkages between the theory of international trade and industry location are strong, as even according to Bertil Ohlin (as cited in Naude and Harmse, 2002): *“Trade theory verges on location theory. Instead of asking why certain countries exchange certain goods with one another, one can ask why production is divided between these countries in a certain way”* (Ohlin, 1967: 307) (see also Ohlin, et al, 1977 & Johnson, 1981).

The implication is that if the Heckscher-Ohlin relative factor endowment theory of international trade is considered, this is virtually the same as industry location. Krugman (1993, cited in Naude and Harmse, 2002) examines location



theory and trade theory in terms of their key assumptions, to determine the extent of the common ground between them, while taking his lead from Ohlin: “Ohlin’s *Interregional and International Trade* was in principle written in order to demonstrate that the two branches of economies are essentially the same. If one steps back from the global economy and views it from a distance, it is hard to see why one should draw any sharp distinction between trade theory and location theory” (Krugman, 1993 in Naude and Harmse, 2002).

Krugman then proceeds to identify assumptions of each, and then explore the implications of the linkages between each (Naude and Harmse, 2002):

**Table 2.1: Key characteristics of International Trade Theory and Location Theory**

Trade Theory	Location Theory
General Equilibrium	Partial Equilibrium
Perfect Competition	Imperfect Competition
Constant Returns to Scale	Increasing Returns
Immobile Factors	Mobile Factors
Zero Transportation Costs	Transportation Costs

(Source: Krugman, P.R. 1993. “On the relationship between Trade Theory and Location Theory.” *Review of International Economics* 1(2): 110 – 22) (found in Naude and Harmse, 2002)

In terms of finding common ground between the two theoretical areas, Krugman addresses each of the areas (Naude and Harmse, 2002):

Equilibrium

If trade and location theories are to be linked, the approach ought to be in terms of general equilibrium that takes account of all market interactions.

Competition

Trade theory has moved since 1980 to take account of imperfect competition, so there is no longer conflict in this area.

### Returns to Scale

Increasing returns ought to be part of any trade-location theory approach.

### Factors

The location theory view of mobile factors and immobile land should dominate, although barriers to the movements e.g. borders.

### Transportation costs

Transport costs ought to be included, as it is apparent that the magnitude of trade between countries is a function to a large extent of the distance involved.

Ohlin sets out a number of key domestic components that influence the location of industry within a country (Ohlin, et al, 1977 in Naude and Harmse, 2002):

- ⇒ Total supply and the prices of mobile factors
- ⇒ Quantities. Local spread and prices of natural resources and of other immobile or incompletely mobile factors
- ⇒ Transport conditions – roads, railways, canals, harbours, surface of the earth, etc
- ⇒ Relative transportability of raw materials, semi-manufactured goods, machines and finished goods
- ⇒ External economies from certain forms of agglomeration
- ⇒ Internal economies of scale
- ⇒ Local spread of productive units that are already in existence and either deliver goods that are used by the new factory or buy goods produced by the latter.
- ⇒ Local spread of markets, which among other things depend on the spread of population and other demand conditions, including public purchases, foreign buyers, import duties, etc.
- ⇒ Institutions and cost of living in different parts of the country
- ⇒ Relative height of local taxes
- ⇒ Interregional differences in wage rates and labour qualities.

Oxley and Yeung (1998) make the point that the fundamental changes to the production process and the globalisation trend will have effects on the value chain through the rise of certain industries and the emergence of different centres of production. The restructuring of value chain activities has far-reaching implications for industrial processes and the way that these are examined in the global context. As industries defined in terms of the 3-digit SIC classification become scattered across various locations, the “location pattern of production” might begin to be at odds with the theoretical predictions of the relative factor endowment notion (i.e. Heckscher-Ohlin trade theory). Oxley and Yeung (1998) contend that it may only be through the examination of disaggregated “sub-industries” based more on “value chain activities” than on end products that a location pattern may emerge that corresponds more closely with the traditional relative factor endowment theory. This approach may assist in bridging the gap between Marshall’s agglomeration theory and the relative factor endowment theory of industry location. That is, agglomeration effects would be strongest for upscale value chain activities, whereas lower scale value chain activities could follow the Heckscher-Ohlin approach. The centrepiece of the exercise would then switch from industry location to value chain activity location. (Naude and Harmse, 2002).

### **2.3 THE SOUTH AFRICAN ECONOMY**

According to Beduizenhout (2002), the broad industrial strategy followed since the 1920’s in South Africa, even though not specifically defined in those terms, seemed to display 3 main characteristics:

1. It contained some elements of import substitution industrialisation by means of protecting local industries from competition through import tariffs. The extent to which tariffs protected local industries, however, is subject to debate.
2. The state played a significant role in setting up corporations to drive a programme of industrialisation. During the sanctions era, the state attempted to use corporations to supply key resources, such as fuel extracted from coal through Sasol.

3. A dual labour market was created, where white South Africans were incorporated into a limited welfare state and were accorded labour rights, whereas black South Africans were formally excluded through a repressive labour regime.

During the 1980's, the industrial policy of the apartheid government started to shift toward a position where tariff reform and privatisation were supported. However, decisive steps on economic reform, especially privatisation, could not be taken due to the illegitimacy of the government.

The 1990's saw two significant events that impacted greatly on South African trade relations. The one event was South Africa's first democratic elections, which were held in April 1994, marking the end of years of cultural, political and economic isolation. The other event was the conclusion of the Uruguay Round of GATT negotiations, which created the World Trade Organisation (WTO) in January 1995. According to Wilson (2002), the impact of these two events meant the lifting of trade sanctions and simultaneous accession to all WTO agreements, national reconstruction and development, and integration into the world economy.

When it became clear in the early 1990's that that South Africa would enter a transition process based on a negotiated settlement, industrial policy received renewed attention as a way to address the legacies of apartheid capitalism. According to Beduizenhout (2002), debates on the relationship between the state and market became an area of intense contestation. During these debates, a number of major perspectives emerged, but all agreed that it was important to strengthen manufacturing. In the context of a mineral rich country such as South Africa, policy measures can be aimed at moving up the value chain – focusing on adding more value to commodities through manufacturing before exporting goods or selling to the local market. This form of local restructuring would attempt to strengthen local manufacturing industry.

The new democratic government inherited an economy that had been globally isolated, and where industry was relatively protected. According to Wilson (2002), unemployment was high, and decades of Bantu education had led to chronic underdevelopment of human resources and skills. The economy was highly dependant

on resource-intensive industries, particularly mining and agriculture, although the percentage contribution of mining had already started to decline significantly.

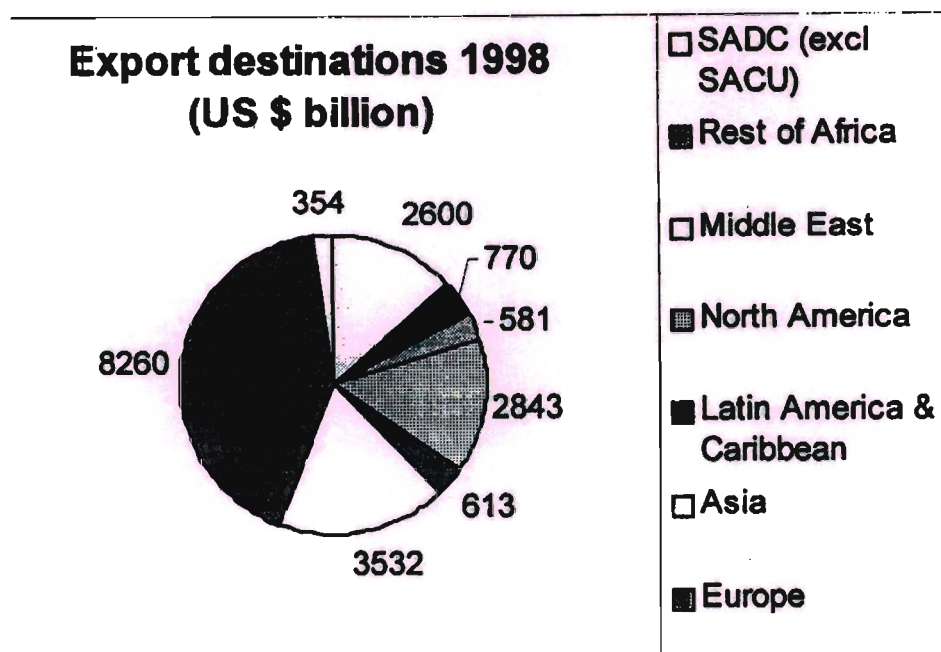
At the heart of the ANC's 1994 election policy was the Reconstruction and Development Programme (RDP), which aimed to build a vibrant democracy that met people's needs and turned back decades of colonial and apartheid rule. Wilson (2002) argues that trade policy was viewed as critically important, given the foreign exchange constraints on growth in South Africa. The key intent of the ANC's trade policy was to:

- ⇒ Enter into agreements with major trading partners that would lead to future development in South Africa.
- ⇒ Restructure South Africa's relationship with neighbouring African countries to enable more balanced and less exploitative trade patterns.
- ⇒ Use tariff reductions on imports, which are a GATT requirement, as a strategic instrument for trade policy and to ensure that reduced protection minimises disruption to employment and sensitive socio-economic areas
- ⇒ Develop better incentive schemes to reduce bias against small and medium sized exporters.

The DTI (2003) views the period since 1994 as seeing the South African economy undergo profound restructuring, with ten years of consistent economic growth been recorded. Furthermore, macroeconomic stabilisation has largely been achieved, providing a platform for accelerating the growth rate. The economy has become increasingly integrated into global markets and has become a successful exporter of manufactured goods and value-added services. South Africa is now able to position itself as an advanced manufacturing economy.

South Africa's major trading partner remains the European Union, which comprised 42.2% of total exports in 1998, a decrease from 46.8% in 1994. Exports to SADC increased slightly between 1994 (12.1%) and 1996 (16.6%), settling down to 13.3 % in 1998. Exports to Africa have increased marginally, but remain low at 3.9% (1998). (Wilson, 2002).





**FIGURE 2.1: South African export destinations (1998).**

(Source: From TIPS 2001, GESS Report as found in Wilson, J. 2002. "Trade, environment and sustainable development". *Department of Environmental Affairs & Tourism – Review of Agenda 21*)

South Africa never had a clear industrial strategy in the 1990's that could have led to a coherent set of industrial policy measures. Hence the role of the DTI, as well as the Industrial Development Corporation (IDC), has generally been used as a yardstick to access current government thinking on industrial policy. Documents such as the section on Industrial Policy in GEAR, as well as the other DTI discussion documents, were used as indicators for the status and direction of industrial policy.

The industrial policy orientation shifted towards what the DTI called a supply-side orientation, where import substitution made way for export-led growth. Alongside a programme of import tariff reduction, the DTI put in place a general set of supply-side measures, including a tax incentive scheme and the provision of low interest loans to companies in industries undergoing rapid tariff reductions. Legislation governing competition was reviewed, and new agencies were created to support the development of small business. It also embarked on Spatial and Industrial

Development Zones in order to attract investment to certain geographic regions. (Beduizenhout, 2002)

It is also important to recognise that the way in which the government's macroeconomic policy was introduced, and the strict adherence to fiscal discipline, closed down some of the space provided in the RDP framework to couple supply-side measures with demand-side measures. Hence, an industrial strategy that could focus on economic growth through infrastructure development and the meeting of basic needs becomes undesirable in the broader policy framework adopted by the government.

South Africa's macro-economic policy, GEAR, outlines an export led growth path where economic growth is seen as the primary way to achieve other development goals (Wilson, 2002). GEAR is conceived within, and orientated towards the global economy, with a strong emphasis on fiscal discipline, investor confidence and macro-stability. In doing so, much of South Africa's trade policy is determined by international trade agreements and actual trade by global supply chains and consumer demands.

*"A decade ago, the South African economy was, by all means, an inward-orientated economy unable to compete globally and saddled with declining growth prospects. Today, its export sector is a key growth driver."* (Abedian, 2003).

As Abedian argues, the structure of the economy generally has been transforming in several interlinked ways. These changes have significance for growth, for the employment and poverty-reducing characteristics of such growth, and for the way in which businesses and its organisations respond to change.

South Africa is much more diversified and competitive than it was 10 years ago. Abedian (2003) points out that the economy's revenue is no longer dominated by the production of primary products or commodities. Even with relatively high platinum and gold prices, the entire primary sector makes up barely 10% of the GDP. By far, the main contributor to the national income is the tertiary, or services, sector that constitutes two-thirds of GDP in 2002. This diversification of income base is vital for the resilience and sustainability of growth. Critically, considerable improvements in

factor productivity, ranging from rising labour productivity to multi-factor productivity, underpin the growing diversification within the economy. Furthermore, Abedian (2003) argues that whereas Government policy has created the enabling environment, the private sector, it is important to note, has been the main driver of investment and capital formation over the past eight years. Rising productivity, together with constructive government policy, have consistently supported the export orientation. In 2003, export intensity is approaching 30% of GDP, leading to a rise in the ability to earn foreign exchange on a sustainable basis and to alleviate the historic balance of payment constraint. (Abedian, 2003). Roughly speaking, commodities constitute only one-third of exports. The other two-thirds are made up of items such as vehicles and agricultural industry products.

The export drive is underpinned by two significant trade regimes with the European union and the US, the latter under the broader umbrella of the African Growth and Opportunities Act.

South Africa achieved this remarkable progress in raising export intensity and diversification during a time when the global economic and financial environment was unfavourable. During this period, a barrage of global financial market crises hit the various economic blocks, covering South East Asia, South America and Russia, as well as South Africa itself. Meanwhile, one of South Africa's key trading partners, Japan, has been gripped by a prolonged economic downturn.

*“Businesses trade to invest and invest to trade”* (Renato Ruggeiro, Former Director of World Trade Organisation in Development Policy Research Unit - UCT, 2001). This view summaries the relationship between investments and exports, and highlights the importance of complementary policies to stimulate investment and promote production of export.

Trade policy in South Africa is based on the assumption that there is a direct causal relationship between trade liberalisation, economic growth, development and sustainable development.



For South African government and business, integration into the global economy, which means opening its borders to increased flow of goods, services and capital, is a pre-requisite for economic growth, which is necessary to meet other developmental objectives, such as job creation.

South Africa's incentive programme is administered by the DTI with Trade and Investment South Africa (TISA) managing the investment side and the National Export Advisory Council (NEAC) the export side. The aim of South Africa's incentive programme is to simultaneously boost fixed investment (with the ultimate objective being increased international competitiveness and thus international trade) and encourage export-enhancing industrialisation. It is consistent with the objectives of GEAR policy, and aims to aid in the transformation of South Africa from a highly protected and inward looking economy to one that is fully integrated into the global economy. (Development Policy Research Unit - UCT, 2001). The main feature of this programme is that incentives are used to target specific high-growth sectors and industries as well as geographic regions. The spatial concentration of infrastructure is deemed to be crucial to South Africa's growth path.

South Africa has several organisations promoting exports and external trade relations. The major government agency is the Chief Directorate: Export and Investment Promotion in the Department of Trade and Industry. (South African Business & Investment Environment, 2003) The main functions of the Chief Directorate are to develop exports and provide assistance and services to South African enterprises wishing to enter global markets.

In recent years, the rate of growth in exports has far exceeded that of GDP growth. (Abedian, 2003) This marks one of the key policy objectives of the 'New South Africa', that is a reorientation towards an export-based economy. Reinforcing the export drive has been the consolidated fiscal position of the government. Sound policies pursued over the past six years have placed South Africa in an enviable position. Abedian argues that very few developed nations and even fewer emerging ones enjoy the same fiscal conditions as South Africa. In an increasingly uncertain global economic environment, it is a great advantage to be in a position to allow for tax breaks, increase social spending, raise government capital expenditure, and still

retain credible macro balances. Macroeconomic conditions remain exceptionally stable despite the current spike in inflationary trend.

The **Regional Industrial Location Study** (RILS) (as outlined in Naude and Harmse, 2002), completed in 1997 by the Industrial Development Corporation, was a comprehensive analysis of the location of South African industry, its performance in terms of exports and competitiveness generally, and an assessment of how it could perform in the future.

Province	Demand for Total Output (%)*				Intermediate Input Demand (%)*		
	Internal Demand		External Demand		Internal Demand		
	Intermediate Demand (%)	Final Demand (%)	Provincial Exports (%)	International Exports (%)	Imports from Other Provinces (%)	International Imports (%)	Local Sources (%)
Eastern Cape	5.1	1.9	84.6	8.4	58.9	18.7	22.4
Free State	3.8	3.3	80.2	12.7	63.5	8.6	27.9
Gauteng	24.5	5.9	56.0	13.6	31.1	15.1	53.8
KwaZulu-Natal	12.1	4.5	64.9	18.5	43.3	16.1	40.6
Mpumalanga	6.4	0.7	78.5	14.4	47.0	16.9	36.1
North West	2.8	1.0	87.8	8.4	55.1	8.4	36.5
Northern Cape	1.7	0.7	89.7	7.9	67.9	8.6	23.5
Northern Province	1.7	1.5	83.7	13.1	59.5	11.0	29.5
Western Cape	9.6	5.1	72.5	12.8	44.1	14.8	41.1

\* Each of Output and Input sum separately to 100% for each province

**Table 2.2: Provincial economic demand for inputs and outputs (%)**

(Source: Naude, CM & Harmse, C. 2002. *“Industrial Strategy and South Africa’s International Trade Position: The Influence of Structural Change and Industrial Location”*)

This table represents the characteristics of the various provinces in terms of their economic relationships with other provinces in South Africa, and the rest of the world. On the output side, data was examined in the RILS regarding the various provinces, i.e. whether the produce for intermediate demand in the province, final demand in the province, exports to other provinces, and international exports. On the input side, the provinces were examined in terms of whether they imported from other provinces, from the rest of the world, or from local (within the province) sources.

The table shows that KwaZulu-Natal province is the most export-oriented province, with 18.5% of output being exported internationally, and a resulting lesser dependence on the other provinces as a market (64.9%).

The province also shows a relatively high proportion of output being taken up by intermediate demand (12.1% of output).

Gauteng exhibits a similar pattern in that it shows the least dependence on other provinces as a market (56% of output). And international exports of 13.6% of output that is supported by a high intermediate demand for output (24.5% of output) and relatively high final demand (5.9%).

It is significant that the provinces of the Western Cape, Northern Province and Mpumalanga, all “border” provinces albeit two inland, show a high proportion of international exports (12.8%, 13.1% and 14.4% respectively) with low levels of final demand in the two inland provinces (1.7% and 0.7% for Northern Province and Mpumulang respectively).

In terms of inputs, Gauteng, KwaZulu-Natal and Western Cape show a strong leaning to local (within province) sources. Gauteng and KwaZulu-Natal also show a reliance on international imports. (Naude and Harmse, 2002).

#### 1.1 Sectoral Concentration and Export Competitiveness

The RILS included the calculation of two ratios aimed at categorising the various sectors in the provinces in terms of their concentration using the location quotient (product specialisation ratio or PSR) and their competitiveness (export specialisation ratio or ESR).

The PSR was calculated as follows:

$$PSR = \frac{(\text{Share of a region's product}) / (\text{Total of all regions})}{(\text{Share of a region's GDP}) / (\text{Total GDP of SA})}$$

The ESR was calculated as:

$$ESR = \frac{(\text{Exports of sector X in province}) / (\text{Output of sector X in province})}{(\text{Exports of sector X in SA}) / (\text{Output of sector X in SA})}$$



The sectors in each province were evaluated in the RILS according to whether they performed well in terms of either ratio, neither or both. Those sectors that had a high PSR and ESR were termed “performers”. The categorisation of the sectors per province is contained in Table 2.3:

RILS Category	KwaZulu Natal	Western Cape	Northern Cape	Free State	Eastern Cape	Mpumalanga	Northern Province	Gauteng	North West
<b>Performers</b> High ESR High PSR	Basic metals Chemicals Paper Wood Fabricated metals	Chemicals Food proc			Non-metallic minerals prod Fabricated metals	Textiles		Textiles Wood	
<b>Small but Export Focus</b> High ESR Low PSR	Food proc	Fabricated metals Basic metals Textiles		Textiles	Textiles Food proc Wood		Basic metals	Non-metallic minerals Chemicals Basic metals	Paper Textiles Fabricated metals
<b>Internal Focus</b> Low ESR High PSR	Textiles Non-metallic minerals	Non-metallic minerals Wood		Chemicals Food proc Wood Paper Non-metallic minerals	Basic metals Paper	Food proc Paper Basic metals Non-metallic minerals	Food proc Chemicals Paper Non-metallic minerals	Fabricated metals	Basic metals Chemicals Food
<b>Weak sectors</b> Low ESR Low PSR		Paper	Wood Basic metals Textiles Chemicals Food proc	Fabricated metals Basic metals	Chemicals	Chemicals Fabricated metals Wood	Wood Textiles Fabricated metals	Food proc Paper	Non-metallic minerals Wood
			Fabricated metals Paper Non-metallic minerals						

**Table 2.3 : Sectoral Performance in terms of PSR and ESR per province**

**Source: Industrial Development Corporation, Regional Industrial Location Study, 1997) (Naude and Harmse, 2002).**

The table shows that only sectors in five provinces managed to attain the status of “performers” (the strongest being KwaZulu-Natal), while the situation was not much different in terms of the category “Small but Export Focused”.

## **2.4 STRATEGIC THEORY**

The move toward an export-driven economy can be described as a grand strategy, which provides basic direction for strategic action. This is the basis of co-ordinated and sustained efforts directed toward achieving long-term objectives. In terms of this

grand strategy, elements of both concentrated growth and market development strategies can be identified:

- ⇒ A Concentrated Growth Strategy would focus on a specific product and market combination. Resources are directed to the profitable growth of a single product, in a single market, with a single dominant technology. Concentrated growth strategies rely on development and exploitation of expertise in a delineated competitive arena, and lead to enhanced performance. By concentrating on a particular area of growth, there is an ability to assess market needs, knowledge of buyer behaviour, customer price sensitivity, and effectiveness of promotion. These core capabilities are a more important determinant of competitive market success than are the environmental forces faced. By concentrating growth on the export sector, economic development will be achieved by building on competencies, and achieving a competitive edge by concentrating on a specialised product-market segment. By employing this strategy, the Government is aiming for the growth that results from increased productivity better coverage of its actual product-market segment, and more efficient use of its technology.
- ⇒ Market Development Strategy allows for a form of concentrated growth by identifying new uses for existing products, and new demographically, psychographically, or geographically defined markets. I.e. incentives to move local products to the export market.

#### **2.4.1 Evaluation of Strategy**

**Suitability** (Johnson & Scholes, 1999) is a broad assessment of whether the strategy addresses the circumstances in which the organisation is operating. This would entail the extent to which the strategy will fit future trends and changes in the environment, or how the strategy might exploit the core competencies of the organisation.

Assessing the suitability can involve two different steps:

- 1 Establishing the rationale or the strategic logic of the strategy in its own right;

- 2 Establishing relative merits of a strategy when a number of choices are available.

The assessment of suitability of a particular strategy is concerned with whether it addresses the circumstances in which the organisation operates or wishes to operate. Simply, it asks the question: “Why is this a good idea?”

The suitability of a strategy assesses the extent to which a strategy:

- Exploits the opportunities in the environment and avoids threats
- Capitalises on the organisation’s strengths and core competencies, and avoids or remedies the weaknesses
- Addresses the political, cultural and socio-economic context

Value Chain analysis is part of the suitability analysis, and describes the activities within and around the organisation and relates them to an analysis of the competitive strength of the organisation. Understanding how cost is controlled and value created within the value system is very important when assessing the strategic capabilities.

## **2.5 SUMMARY**

As South Africa moves away from being a highly protected, inward looking economy towards an internationally competitive economy, fundamental changes are being made to its trade and industrial policy. The trade policy aims to change international terms of trade in order that developing countries might benefit more.

The trade policy is based on a strategy of concentrating growth in the industrial sector to boost exports and thus stimulate the economy with resulting socio-economic spin-offs. The examination of relevant economic theory suggests that this is a strategically suitable means to achieve this goal, albeit with a few reservations. However, the location of industry in South Africa can create the conditions to stimulate the country’s plans concerning international trade and competitiveness. Industrial Development Zones are being implemented in South Africa as a means to create these conditions to further economic growth.

## **CHAPTER 3**

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### **CASE ANALYSIS**

#### **3.1 INTRODUCTION**

There is a close relationship between the industrial policies pursued by a government and the nature and pace of a country's developmental path. It can be argued that no matter how 'free market' a country may now appear to be, it has not developed without an active industrial policy in which the state has played a driving role. But while all countries have pursued some sort of industrial policy, the content of these policies varies tremendously. The impact of industrial policy is important as it effects the social as well as economic development of the country. This can be in relation to the patterns of ownership and control, the demand for different types of labour, and the nature of goods produced for consumption.

A basic strategic requirement for progressive industrial policy measures could be for the state to play the role of planning and co-ordinating a developing industry towards meeting the basic needs for sustainable economic development. While industry policy measures would have a protective component, the more important factor would be a proactive role in identifying and dealing with blockages and opportunities.

An Industrial Development Zone can be, and has been used an important tool in government planning in various countries. In this chapter, the concept of an IDZ is examined in the global context. Various countries have made use of IDZs as part of the industrial policy aimed at shaping the national economy, and this chapter aims to firstly explore and evaluate this on a global scale.

Secondly, this chapter will examine the concept of an IDZ within the South African context. This will cover the intended use of IDZs to meet certain economic strategic objectives.

Finally, this chapter will outline the profile and capabilities of a private company that is proposed to improve the efficiency in the functioning of the IDZ.



### **3.2 INDUSTRIAL DEVELOPMENT ZONES IN THE GLOBAL CONTEXT**

Countries are becoming more economically interconnected as trade barriers between them are dismantled. In the context of trade liberalisation, the way in which goods and services are produced has changed significantly – commodity chains now span across national boundaries, and many products are assembled in several countries. In this context, the role of the state, in particularly in developing countries, has come under renewed scrutiny. According to Beduizenhout (2002), the aim of industrial policy should be to insert the national economy into global commodity chains in a way that reduces vulnerability and risk. Industrial policy, therefore, is not a matter of whether the state has a role to play, but rather what the appropriate role is. The model of the developmental state saw a central role for the state in shaping industrial structure through industrial policy measures such as targeting certain industries for investment or other supportive measures.

Since the 1930's governments have tended to play a central role in their economies through demand-side macroeconomic management. These demand-side measures included various ways of boosting domestic demand, such as minimum wages, coupled with the protection of local industries by import tariffs. The intention was to facilitate the development of local industries, an approach known as Import Substitution (ISI). However, according to Beduizenhout (2002), in the early Seventies, Governments started to abandon these demand-side policies for neoliberal policies, implying a withdrawal from the economy through privatisation, trade liberalisation and flexible labour markets.

Trade liberalisation exposed many developed countries to competition from certain Asian countries, notably Japan and South Korea. This drew attention to the role played by the governments of those countries in facilitating industrial development. Many of these governments had used a combination of supply-side and demand-side measures to stimulate and strengthen their manufacturing industries. Certain industries were targeted for export promotion. They would initially be protected to develop capacity to serve domestic markets while receiving considerable support from



governments through various supply-side measures, including state-funded research and development, financing and tax incentives.

### Export Processing Zones

Given various names in various countries, Export Processing Zones (EPZs) have several qualities in common. According to Khan (2002), EPZs exist to promote export-orientated growth; are usually based near ports of entry (harbours or airports) and are designed to entice investors with low tax rates (even tax holidays), relaxed labour regimes or, in South Africa's case, state investment in infrastructure.

EPZs have been successful in several countries, particularly in the Far East. EPZs also feature in South Africa through the DTI's Global Economic Strategy (GES). Balasubramanyam (1988, as quoted in Naude and Harmse, 2002) defines an EPZ as *"an enclave outside the customs territory of a country"*. Commodities (e.g. inputs) entering the zone can be processed or stored without incurring customs duties (e.g. import tariffs), while exports from the zones are not liable for duties either. Examples of fiscal and financial incentives applied in the South East Asian context have included tax holidays, lenient depreciation allowances and exemption from wage and welfare legislation. According to Balasubramanyam (1988, quoted in Naude and Harmse, 2002), the objectives of these schemes in the context of developing countries include:

- ⇒ Promotion of manufacturing of manufacturing for export;
- ⇒ Creation of employment opportunities;
- ⇒ Importation and subsequent usage of foreign technology in the domestic economy, and
- ⇒ Regional development.

The empirical evidence for the benefits of EPZs as applied seems to be positive both in the Far East and elsewhere. Balasubramanyam (1988) lists studies pointing to the success of EPZs in South Korea, Indonesia, India, Philippines, Singapore, Taiwan and Mauritius. More recently, Joansson and Nilsson (1997) have also argued that EPZs have a substantial role to play as catalysts for economic growth in the areas where

they have been applied. African Business (1999) relates the case of the EPZ in Walvis Bay, Namibia, as one of success.

Khan (2002) examines a report published by the International Labour Resource and Information Group (ILRIG), a South African non-governmental organisation (NGO), which covers EPZs in four countries: South Africa, Zimbabwe, Tanzania and Namibia.

In this report, these 4 have countries enjoyed little benefit from the EPZs. The jobs created amounted to only a fraction of those promised. The report suggests that export orientated industrialisation strategies are wrong for the region. It has provoked in Southern Africa, argues ILRIG (Khan, 2002), a race to the bottom as some countries competed with each other by lowering taxes and relaxing labour laws. And this orientation risked keeping the economies of African countries underdeveloped, by encouraging the export of dominant raw materials.

By following this model, Southern Africa has emulated developing countries in Asia and South America where the zones first gained flavour in the Eighties. Now 850 zones in 70 countries employ a total of 27-million workers, according to the International Labour Organisation (ILO).

In Zimbabwe's EPZ, less than half the 138 opportunities identified were operational by early 2001. Even off this low base, the deteriorating economy meant that EPZs increased their share of exports to 7%, but this was on the back of low wages. In addition, the workers in the zones put in longer hours and get less leave than industrial workers in the rest of the economy. (Khan, 2002)

Despite the African Business review (2002), Khan (2002) argues the EPZs in Namibia are even sketchier, with only nine getting off the ground, and several closed down by the end of 1999. Where the government predicted that 25000 people would be employed in 5 years, only 370 job contracts were recorded, and of that, 150 were temporary. And, Khan (2002) argues, this pattern is repeated in Tanzania, where a slated 7000 jobs has dwindled to only 500 after peaking at 2000 when the Zanzibar Free Economic Zones Authority set up shop.

Despite this patchy record, South Africa is steaming ahead with 3 versions of EPZs. The 3 types include 11 spatial development initiatives meant to draw investment to underdeveloped regions with economic potential, industrial development zones (only one currently legislated) and development corridors – “transport links between one or more production sites and a port”. Khan (2002) is of the opinion that the jury is still out on whether the industrial strategy will succeed, but an early prognosis is ringing warning bells.

### **3.3 INDUSTRIAL DEVELOPMENT ZONES IN THE SOUTH AFRICAN CONTEXT**

Industrial Development Zones (IDZs) are the South African version of ‘Export Processing Zones’ (EPZs), as they are known in other parts of the world. IDZs are part of the broader Spatial Development Initiative Programme (SDI) that aims to encourage private sector participation in providing infrastructure in areas with abundant under-utilised potential. Increasingly, the SDI approach is based on the objective of operationalising South Africa’s commitment to the ‘African Renaissance’. (South African Business & Investment Environment, 2003).

The term SDI is used in South Africa to describe a programme of strategic initiatives by government aimed at unlocking the inherent and under-utilised economic development potential of certain spatial locations in South Africa. In a report by the South African High Commission (2002), this initiative is placed in the context of the new paradigm adopted by the government of South Africa. A key component of which is the move away from the previous protected and isolated approach to economic development, towards one in which international competitiveness, regional co-operation and a much more diversified ownership base is paramount.

The SDI process in South Africa began in 1995 and was the first attempt by, primarily, the DTI and the Department of Transport, to take economic policy into the implementation arena (Naude and Harmse, 2002). It sought to identify key areas of the country that could be the focus for economic development and promote investment in these areas. The areas would be identified on the strength of economic

activities (along sectional lines) which characterised the area and then strategies could be devised focusing on these lead sectors. Anchor projects would then also be identified as being the key projects that could initiate and sustain the SDIs in the future. More often than not, the SDIs encompassed existing or proposed transport infrastructure and took the form of a development corridor. A key component would then be the active promotion by government of investment in the anchor projects in the SDIs by the private sector. The role of government would be to identify projects and to facilitate involvement by interested parties.

Following on from the success of the Maputo Development Corridor, the focus of the SDI concept has broadened to incorporate as a set of initiative concerned with unlocking the inherent un/under-utilised development potential of certain strategically important spatial locations in South Africa. These are at present a number of initiatives being pursued by national, provincial and local government in South Africa. They differ spatially and structurally, depending on the nature of their underlying economic potential and existing economic activity.

The key objectives of SDIs (as outlined by South African High Commission, 2002) are:

1. To generate sustainable economic growth and development in relatively under-developed areas, according to the inherent economic potential of the locality.
2. To generate long term and sustainable employment for the local inhabitants of the SDI area and for the nation in general.
3. To maximise the extent to which private sector investment and lending can be mobilised into the SDI area. This has the added benefit of lessening the already unachievable demands on the government focus for the implementation of much needed development projects.
4. To exploit the spin-off opportunities that arise from this relative crowding-in of private and public sector investments.
5. To exploit the under-utilised locational and economic advantages for export-orientated growth of the SDIs. In terms of this objective, government is giving specific attention to an effective package of supply-side measures, a revamp of the regulatory framework to facilitate export strategy, trade treaties and the restructuring of major import conditions.



The Maputo Development Corridor is the most advanced and best-known programme of strategic initiatives undertaken by the South African government aimed at generating long term, internationally competitive growth and development, and at restructuring the 'apartheid' space economy.

Robert (2000) has examined the performance of various sub-sectors in the manufacturing sector in South Africa between 1990 and 1997 in terms of exports, output and employment. (Naude and Harmse, 2002). Refer to table below. His finding is that even where a number of manufacturing sub-sectors, such as non-ferrous metals and transport equipment, have increased their importance as exporting industries, this has been accompanied by decreases in output and employment in these sectors.

Sub-sector	% manuf. exports 1991	% manuf exports 1997	Avg output growth 1990-97	annual growth	Avg empl. 1990-1997	annual growth
Food & processing*	6.9	3.4	-0.1			-3.5
Beverages*	1.2	1.4	-0.3			-3.1
Tobacco products	0.1	0.2	-1.1			-5.9
Textiles*	3.7	1.9	0.2			-6.4
Clothing*	0.8	0.5	0.8			0.1
Leather products*	0.6	0.7	1.1			-6.0
Footwear*	0.1	0.1	-4.8			-3.6
Wood & products*	0.8	0.3	1.9			1.1
Furniture*	0.6	0.6	1.6			0.0
Paper products*	5.4	2.9	0.6			-0.9
Printing & publishing*	0.2	0.2	0.1			0.5
Industrial chemicals*	8.2	7.5	1.7			
Other chemicals*	1.5	1.7	2.0			-2.4
Petrol & coal products	0.5	4.0	5.7			
Rubber products*	0.4	0.5	-1.3			-1.7
Plastic products*	0.4	0.5	1.2			2.5
Pottery	0.1	0.0	-4.5			
Glass & glass products	0.5	0.2	-1.3			-1.3
Non metallic minerals*	0.7	0.5	-1.0			-3.5
Basic iron & steel*	20.6	11.0	-0.4			-5.4
Non-ferrous metals*	11.8	29.4	7.9			-4.5
Metal products*	3.9	3.4	1.1			-2.6
Mach & equipment*	4.1	5.2	0.9			-3.3
Electrical machinery*	1.4	1.9	-0.2			3.3
Motor vehicles*	3.2	3.4	0.0			-2.6
Transport equipment*	1.0	2.4	-6.2			-9.9
Prof. Equipment*	0.5	0.7	1.2			-2.5
Other Manufacturing*	21.0	15.4	-1.9			-4.0
TOTAL	100.0	100.0	1.0			-2.1

Table 3.1: Summary export, output and employment data doe manufacturing sub-sectors, 1990 – 1997

**Source: Robert, S. “Understanding the Effects of Trade Policy Reform: The case of South Africa”. *South African Journal of Economics*, Volume 68:4. 607 –38).**

This data is also useful in assessing the potential of SDIs as discussed later. Roberts’ key findings that many of those sub-sectors which have increased their share of exports between 1991 and 1997 have seen reductions in output and employment growth (i.e. increases in exports have not gone together with increased output and employment), remains pertinent when considering the potential for the SDI programme to increase employment in South Africa. As can be seen from the list of sectors with an asterisk (\*) indicating inclusion in the SDI programme, the latter is heavily biased towards traditional sub-sectors of manufacturing. With this in mind, Roberts’ finding is all the more crucial for industrial strategy in South Africa. It is apparent that, based on the traditional areas of manufacturing as the SDI programme seems to be, it is largely focused on several sectors which have not increased exports in all cases, and then without fundamental increases in output and employment. This would be a major weakness of the SDI programme if it were looked to as a job creation mechanism.

The IDZ policy is designed to boost exports and jobs (South African Business & Investment Environment, 2003). The DTI (2003) describes IDZs as purpose-built industrial sites linked to an international port or airport, and specifically designed to attract new investment in export-driven industries. The intention is to support these industries with world-class infrastructure, services and logistics networks.

The IDZ initiative is run by the DTI and its ultimate goal will be to boost manufacturer’s international competitiveness within a structured environment. This environment is envisaged to be world-class, complemented by state of the art transport, communication and utility networks. In order to reduce transport costs, IDZs will be situated near an airport or seaport, with efficient customs operations and duty-free incentives stimulating the production of goods for export. (Development Policy Research Unit - UCT, 2001).



Key features of the South African IDZs (DTI, 2003):

- A customs secured area with its own SA Revenue Services (SARS) personnel to provide support on customs and excise requirements. This will be a delimited area with entrance and exit points controlled by customs officials.
- An industrial services area, for service and supply industries supporting large manufacturers in the customs secured area, with top-notch industrial and office park environments.
- A one-stop centre to facilitate regulatory procedures and requirements.

Another important facet of the IDZ programme is the government's commitment to ensuring that all companies comply with the new 'green' standards of production. The Development Policy Research Unit (UCT, 2001) regards this as becoming increasingly important in the global economy, and an area where South Africa cannot afford to be left behind.

In South Africa, the Coega and East London IDZs have received their operator permits; and the Johannesburg International Airport and Richards Bay IDZs have been designated. Other sites earmarked for IDZs include Durban, Saldanha and Richmond. According to the DTI (2003), all companies investing in an IDZ are subject to South Africa's environmental and labour laws and investors in an IDZ will benefit from duty-free imports of capital goods and inputs, plus VAT suspension for supplies procured in South Africa.

According to Dr Mahlape Mohale, CEO of the Enterprise Organisation in the Department of Trade and Industry (cited in Sunday Times, Business Times 2003), the success of South Africa's IDZ programme will depend largely on policies that aim to develop human resources and create the infrastructure necessary to attract foreign direct investment and export-orientated manufacturing.

*"In the comparison of South African incentives and those incentives offered by other free trade zones, studies show that the South Africa's IDZ programme and offerings of incentives, facilities and services are on a par with other world-wide special economic zones, with the notable exception of specific tax incentives."* Mohale (2003)

Investment promotion in the IDZs is estimated to realise approximately R3 billion in 2003 – 2004 alone (Sunday Times, Business Times 2003). According to Mohale (2003), Coega “has proven that with good technical and management capabilities, an IDZ can go a long way as a mechanism for unlocking the economic potential of a country such as South Africa.”

Mohale (2003) argues that major investment interest is present despite one of the major criticisms levelled against South Africa’s IDZ programme – the lack of fiscal or tax-related incentives, which are offered in special economic zones elsewhere in the world. South Africa provides mostly financial and customs incentives.

Regarding the application of the IDZs in South Africa (for the purpose of this argument, the terms ‘IDZ’ as applicable in South Africa, and ‘EPZ’, as applicable elsewhere, will be used interchangeably), their prospects for success in terms of a contribution to output and employment needs to be carefully considered. In several cases, EPZs have involved labour legislation being waived in respect of employers operating in these areas. In the South African case, organised labour has been an extremely important participant in the Nedlac arrangement (involving government, business and organised labour) and has been a key alliance partner of the ruling African National Congress (ANC) party in South Africa together with the South African Communist Party (SACP). According to Naude and Harmse (2002), it seems apparent that labour legislation would not be waived in the case of IDZs in South Africa.

Another important element that arises is whether the firms locating in the IDZs remain in the country only for as long as the advantages of the EPZ exist. To date, South Africa has found it difficult to attract FDI (Schoeman et al, 2000 in Naude and Harmse, 2002), and the possibility arises that it could be limited to IDZs in future, which could be a long-term weakness in the economy in that economic development could be restricted to a few pockets of the country.

Naude and Harmse (2002) pose the question of what will happen when the IDZs are ever dismantled. Is there the possibility that they will simply follow the fate of the industrial parks in the areas of the apartheid-era homeland and Bantustans, which

were deserted as soon as the incentives in the industrial decentralisation programme were removed? Naude and Harmse (2002) are of the opinion that this should not occur if the IDZs are established in areas with locational advantage in terms of linkages with other industries and good access to export routes, which was not the case with the decentralisation programme.

### **3.4 SOCIÉTÉ GÉNÉRALE DE SURVEILLANCE**

Founded in 1878, Société Générale de Surveillance (SGS) is a company with expertise in verification, testing and certification services. SGS operates a network of almost 1200 offices, subsidiaries and laboratories around the world.

The SGS Group offers a range of services with the core competencies of verification and monitoring services for international trade in agriculture, minerals, petroleum and consumer products together with certification and other services to governments and international institutions. SGS also offers strategic services to the industrial, environment, non-destructive testing, project resourcing, logistics and hygiene sectors.

SGS is well established in the international trade sector, and particularly in working in alliance with the customs functions of various countries in developing nations. International trade can only be an effective engine of growth for national economies if the movement of goods is not hindered by delays in the export / import process. To achieve this, SGS has utilised their expertise and experience gained over the years, and have developed a number of services which aim at ensuring that countries and companies can benefit from the freer international trading through rapid clearance of goods and effective interaction with importing countries' administrations.

These services cover the development of national information systems to streamline and accelerate trade processes, the certification of trade entities and products, as well as the introduction of validated customs green lanes.

Besides trade facilitation, it is important that that national security and safety requirements are fully met. SGS has also developed services that serve both the

legitimate needs of governments for effective controls, and those of importers and exporters for speed and efficiency of trade transactions.

A large aspect of SGS's role in international trade takes the form of the Import Verification Programme (IVP). The IVP consists of documentary verification of an export / import transaction to ensure compliance with import regulations, as well as physical inspection to ensure the integrity of the goods. Since 1965, over 40 countries have adopted SGS programmes to protect government finances and/or facilitate trade. Currently SGS holds 23 mandates for IVP programmes that incorporate services both in the country of export and import.

The advantage of the IVP is that it enables the proper identification of goods prior to shipment, with regards to quality and quantity, tariff classification, import eligibility and the provision of valuation information for customs purposes. These programmes allow for the correct assessment of import duties and taxes by Customs to the advantage of both government and trade.

Most governments request SGS import verification services to achieve one or several of the following goals:

- ⇒ Trade Facilitation through simplified customs clearance;
- ⇒ Protection of Revenues;
- ⇒ Promotion of national industry and foreign investment;
- ⇒ Foreign exchange protection;
- ⇒ Physical identification of goods in the country of export/supply;
- ⇒ Review of Compliance with documentary requirements.
- ⇒ Expert opinion on the value of goods for customs purposes;
- ⇒ Contract price verification based on similar exports within market price range;
- ⇒ Accurate classification of goods with appropriate tariff rates.

In addition to IVP, SGS offers to governments and enterprises trade services specifically designed to respond to their international trade needs. SGS aims to become the preferred provider of export "enabling" and "facilitating" services. Of specific interest to the IDZ initiatives, through the export development programme,

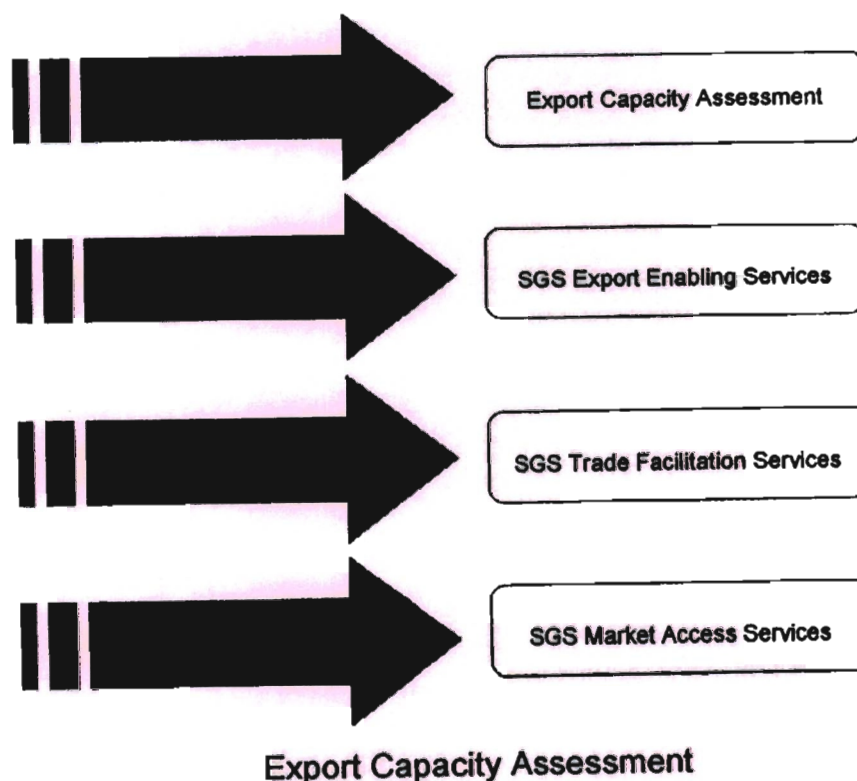
SGS bridges the economic policy issues that are the domain of the government, and the commercial responsibility of enterprises with a complete range of services to improve competitiveness and access to international markets.

The SGS export development services module addresses the needs of emerging as well as existing exporters through a modular service offering. SGS is seeking government support for the services, through co-operation with export promotion agencies and customs administrations.

The SGS export development programme incorporates:

- ⇒ Verifying and validating international trade transactions in terms of their customs and regulatory compliance;
- ⇒ Certifying and assessing products and enterprises against internationally accepted standards;
- ⇒ Knowledge of international trade practices and transactions;
- ⇒ Supporting clients through a unique global network comprising offices and subsidiaries worldwide.

SGS is also positioned to offer export development services within an e-commerce environment, acting as a trust-builder to enable transactions among non-traditional partners.



**FIGURE 3.1: SGS Export Development – Export Capacity Assessment**  
(Available online at [www.sgs.com](http://www.sgs.com))

### **3.5 SUMMARY**

The evidence suggests that EPZs have been the catalyst for economic growth in many countries such as South Korea, Indonesia, India, Philippines, Singapore, Taiwan and Mauritius. There are also arguments, however, that the EPZs have yielded disappointing results in terms of meeting specific objectives. The important question, then, is what will happen in South Africa's case? This chapter has examined the IDZ initiative as it has been developed by South African government, and has introduced a private company that will be recommended as an IDZ operator to maximise the efficiency of the IDZ and thus contribute to the South African IDZs meeting the specified economic objectives.



## **CHAPTER 4**

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### **EVALUATION**

#### **4.1 INTRODUCTION**

There are various conflicting accounts of the success of EPZs in other countries. While there is evidence to suggest that EPZs have contributed to economic growth in many countries, there are arguments as to the extent of this success. A careful consideration of the information at hand is necessary to answer the questions inherent in this discussion.

Will the South African IDZs contribute to export-driven economic growth? More specifically, through the use of IDZs, will the South African economy move to a high-growth path; increase competitiveness, efficiency and employment levels, and reduce poverty and persistent inequalities?

This discussion aims to address these questions by evaluating the case presented against the theoretical constructs discussed in the previous sections.

#### **4.2 EVALUATION**

With the rate of growth in exports far exceeding that of GDP growth; we are already seeing the features of an export-based economy. Reinforcing the export drive has been the consolidated fiscal position of the government. Sound policies pursued over the past six years have placed South Africa in an enviable position. Economist Iraj Abedian (2003) argues that very few developed nations and even fewer emerging ones enjoy the same fiscal conditions as South Africa. In an increasingly uncertain global economic environment, it is a great advantage to be in a position to allow for tax breaks, increase social spending, raise government capital expenditure, and still retain credible macro balances. Macroeconomic conditions remain exceptionally stable despite the current spike in inflationary trend.

IDZs could have great potential for fostering forward and backward linkages between and within industries, particularly in terms of spatial prioritisation, stimulation of local economies and inducing greater integration of related economic activities.

Investments in industries that are highly linked to other up and down-stream industries in the domestic economy will have higher resultant effects on other sectors. These resultant effects could be in the form of investment flows, lower cost inputs, and increased employment. The promotion of sectors exhibiting high linkages to also related to beneficiation. The active cultivation of linkages, however, is more likely to keep production circulating within South Africa rather than have primary products being exported for the next stage in the production process.

Government led infrastructural development can facilitate the crowding in of related industries. The locational targeting of IDZs can be instrumental in development plans for particularly economically depressed areas, and is in accordance with Weber's industrial location theory. If the resultant effects of IDZ production were actively induced, the gains from these activities would have a ripple effect, and stimulate the economic development in the targeted economically depressed areas.

If not properly conceptualised and implemented, however, IDZ initiatives could actually lead to a crowding out of enterprises in the same sector as are targeted in the IDZ elsewhere in the country. Special concessions, such as no import duties, afforded to industries in IDZs could potentially lead to the failure of competing industries that are not in the IDZ. Non-IDZ South African companies will have to unfairly compete with IDZ companies who can average production prices when they export, and supply the local economy. Furthermore it is possible, considering that significant portions of IDZ enterprise output will find its way into the non-IDZ South African economy that there may be other job losses in non-IDZ enterprises.

A particular challenge for industrial development in South Africa and for the IDZ initiative in particular is to move domestic production up the value chain. A situation should be avoided where South African companies are just suppliers to multinationals in the IDZs which then benefit South African goods and repatriate profits to their home country.

The development of IDZs are part of a concentrated growth strategy. Concentrated growth leads to enhanced performance in a particular sector, namely the export market. By concentrating similar and related activities in a location with easy access to, and full utilisation of necessary resources, the growth can be geared towards building and strengthening core competencies, which will lead to further accelerated growth.

The South African economy has been built on the exploitation of renewable and non-renewable natural resources, such as minerals, coal and agricultural produce. For the economy to be sustainable there need to be a shift away from resource intensive industries. Within IDZs, projects on mineral beneficiation, agro-processing and tourism are prioritised in order to earn foreign exchange.

South Africa also markets itself as a provider of cheap electricity, which is an incentive for investment, but also attracts energy intensive industry. If South Africa is to compete in the global economy, it needs to produce to its comparative advantage, as explained in the Hecksher-Ohlin theory of international trade. Given the scarcity of skilled labour and capital, this advantage is found in the natural resources. This entails obvious negative consequences for the environment. Jourdan (2001), however, argues that capitalising on the use of natural resources can launch into other areas of economic activity, through:

- ⇒ Beneficiation, which is the cornerstone of the DTI's industrial strategy,
- ⇒ Developing inputs to the resource extraction sector (for example, in South Africa, this would be moving towards mining machinery and equipment and services),
- ⇒ Lateral migration, where there is a move from a resource industry to a high tech or knowledge industry.

In the long term, therefore, resource intensive industries are used to develop skills and services, acting as the stepping-stone to a service and knowledge intensive economy that is less reliant on resource extraction. However, as Wilson (2002) points out, given apartheid's legacy of minimal education for many South Africans, it is only a

minority if people with high skills who will be able to compete and gain from a knowledge-intensive economy and it will not create employment in the short term.

### **4.3 SUMMARY**

With increasing globalisation, and global trends moving towards opening markets to international trade, gearing the economy towards an export orientation is taking advantage of the opportunities presented in the global arena. The IDZ incentives are designed to attract foreign direct investment to encourage growth and subsequently employment.

According to the various theoretical models, this strategy is suitable in that it addresses the circumstances in which it is operating, within both the South African and global context. Furthermore, according to economic theory, this strategic move has the potential to meet the objectives of high economic growth; increased competitiveness and efficiency, and sustainable development, which entails increased employment levels, a reduction in poverty and eradication of persistent inequalities

It is important to note that this growth strategy is aimed at long-term growth and sustainable development. The re-orientation to an export-driven economy will change the dynamics of the existing economy, which may entail a trade-off in other sectors of the economy in the short-term.

## **CHAPTER 5**

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### **RECOMMENDATIONS**

#### **5.1 INTRODUCTION**

Increasing globalisation and global trends are moving towards opening markets to international trade. Gearing the economy towards an export orientation is a strategic initiative that takes advantage of the opportunities presented in the global arena. The IDZ programme is the tool through which the creation and fostering of an export-orientated industry will create economic growth. The incentives offered to businesses to form part of the IDZs are designed to attract foreign direct investment to encourage growth and subsequently employment.

It is within this context that recommendations are made for a private company, Société Générale de Surveillance (SGS), to be involved in the logistics of the IDZs, and improve the overall performance, thus leading to greater effectiveness of the IDZs.

#### **5.2 IDZ OPERATOR**

As export diversification accelerates, it is critical that appropriate investment is made in the expansion and modernisation of export-orientated infrastructure. Logistical facilities and regulatory and managerial systems within the South African export infrastructure (ports and harbours etc) need urgent attention. The IDZs can only be effective in meeting economic objectives if they are run with optimal expertise and service levels.

It is recommended that SGS can best optimise the efficiency of an IDZ by developing and running the IDZ in the capacity of an IDZ operator.

SGS is well positioned to provide the basic services required of IDZ operator, namely:

- ⇒ Monitoring the movement of goods into and out of the IDZ in order to report this to the South African Receiver of Revenue (SARS).
- ⇒ Establishing a customs secured warehouse and provide guarantees for duties payable on imports
- ⇒ Monitoring the compliance of IDZ enterprises with the applicable regulations, legislation and standards.
- ⇒ Enforcing of internal rules and procedures within the IDZ in compliance with customs, security, environmental and other requirements.

SGS has worked with many governments specifically in the process of import and export for several decades. Within this time, SGS has accumulated vast experience in monitoring mandated processes, regulations and procedures, on governments' behalf.

The South African IDZs will consist of a customs secured area with its own personnel to provide support on customs and excise requirements. This will be a delimited area with entrance and exit points controlled by customs officials. National Customs Administrations are faced with the challenge of maintaining strong controls to protect their national interests while, at the same time, facilitating the flow of goods to improve competitiveness. There are four categories of services for which SGS already has recognised competencies and capacities that will improve the effectiveness of Customs:

#### 5.2.1 Inspection Services:

These are provided across exporting, transshipment or importing locations by means of ad-hoc procedures and manuals; training programmes on inspection techniques; risk-focused pre-shipment inspections; state-of-the-art technology expertise; testing and management of cargo scanning equipment and "second inspection" audit chains.

#### 5.2.2 Valuation Classification and Validation:

SGS will offer operational support to reduce revenue losses related to misdeclared values and origins, thus strengthening institutional capacity. Customs Administration will be able to swiftly implement WTO Agreements'



specific concerns about risk management related to transactions; validation of declared values and classifications through appropriate techniques; compliance with rules of origin.

#### 5.2.3 Monitoring of Special Customs Regimes:

Which are becoming widespread throughout the supply chain, including bonded warehousing, temporary impact regimes, and duty drawback/refund schemes. SGS services cover duty drawback/refund schemes, bonds and guarantees' management, clearance of special export processing zones as well as bonded warehouses supervision.

#### 5.2.4 Trade Facilitation & Certification:

Using SGS worldwide capabilities to validate transactions and identify compliant entities entitled to accelerated clearance at port (green channel status). SGS is capable of performing documentary reviews, certifications and performance audits. Customs will thus optimise deployment of their resources focusing on higher risk transactions, and develop customs-specific compliance requirements.

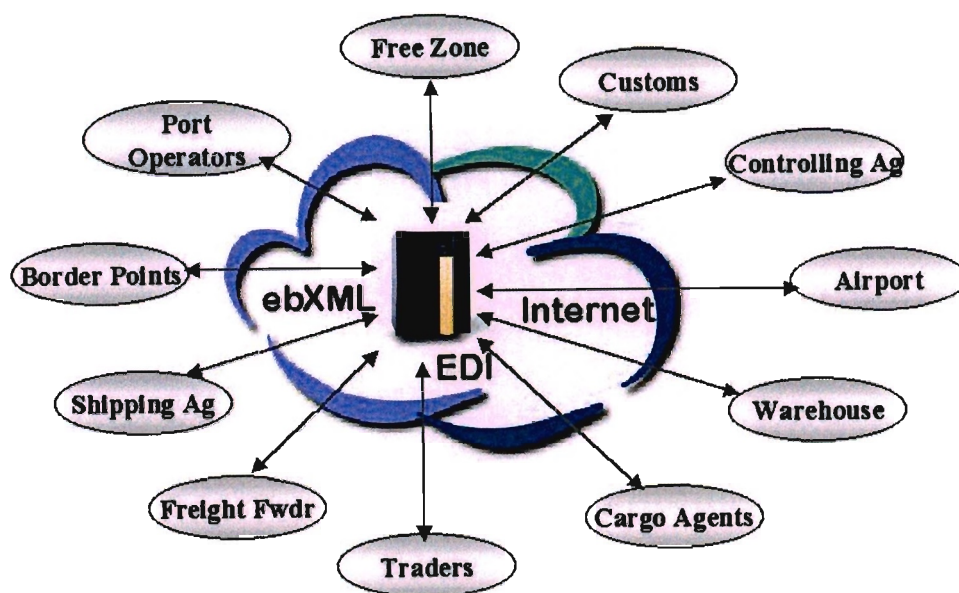
In addition to the experience accumulated over the years, SGS has developed products that, if used in conjunction with the basic services of the IDZ operator, will enhance the level of service and thereby optimise the efficiency of the IDZ.

**SGS Tr@denet** will enhance the customs function of the IDZs, lead to a significant reduction in transaction costs to the trade and improved revenue performance for governments, and assure compliance with national regulations.

It is an international trade management system encompassing the entire integrated trade value chain, including import and transshipment processing procedures. It is an Internet based application that creates a single interface between the trading community and government agencies whose trade control and revenue collection functions will nonetheless remain uncompromised.

As part of the Tr@denet service, SGS can also provide a modern response to customs

administration's needs to adopt a computerised system for the processing of customs' declarations. Such an integrated system can support advanced customs management techniques related to warehousing, financial guarantees, risk management, and interface with treasury systems.



**FIGURE 5.1: SGS Tr@denet** (Available online at [www.sgs.com](http://www.sgs.com))

**SGS PROFILER™** is a unique knowledge-based service developed to assist both Customs and other government agencies in the identification and management of the risks related to trade transactions.

SGS Profiler™ filters transaction data, matching the key attributes against a set of resident risk databases that include both specific trade intelligence information on trade entities and goods, as well as generic information related to valuation and classification risks. These databases incorporate SGS 38 years' trade verification experience, including unique international intelligence and trade knowledge in the areas of valuation, classification, and trade fraud. SGS Profiler™ filters are flexible, expandable and easily customised to the specific needs of a client.

SGS Profiler™ is a sophisticated technological tool that can interface with a wide variety of electronic messaging systems. It can process bulk transaction data at high

speed and transmits an automated risk message to the client for each element of a transaction found to be with risk.

The output from SGS Profiler™ can be used to automatically direct different types of intervention according to the client's requirements. Such intervention might include the identification of high-risk shipments requiring examination either prior to shipment or at destination, as well as low risk shipments entitled to unhindered green lane clearance. SGS Profiler™ is also the ideal tool to manage the effective utilisation of cargo-scanning technology.

### **5.3 SUMMARY**

International trade can only be an effective engine of growth for national economies if the export / import process is unhindered and efficient. To achieve this, SGS has utilised their expertise and experience gained over the years, and have developed a number of services which aim at ensuring that countries and companies can benefit from the freer international trading through various products and services.

SGS's core competencies are embedded in offering strategic services. As a company well-established in the international trade sector, and particularly in working in alliance with the customs functions of various countries in developing nations, SGS is ideally positioned to service the South African government in the capacity of an IDZ operator. The IDZs can only be effective in meeting economic objectives if they are run with optimal expertise and service levels. The efficient and effective functioning of the IDZs will ensure concentrated growth in the industrial sector aimed at the export market. Foreign direct investment and increased production in this sector will boost export and increase international competitiveness, leading to greater revenue and higher economic growth patterns. In the long run, increased economic growth leads to sustainable economic development. Carefully managed, economic development will raise employment levels, and reduce poverty and structural inequalities within the socio-economic arena.

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