Evaluation of Industrial Development Zones in South Africa

Focus on Coega and Richards Bay Industrial Development Zones

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by

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Degree of confidentiality: A 2012

Declaration

Hereby I, Tatenda Zingoni, declare that Evaluation of Industrial Development Zones in South Africa is my own original work and that all sources have been accurately reported and acknowledged, and that this document has not previously in its entirety or in part been submitted at any university in order to obtain an academic qualification.

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Key words

Industrial Development Zones, Special Economic Zones, Industrial Policy Action Plan, New Growth Path

Abstract

Industrial Development Zones (IDZs) are Special Economic Zones which are set aside to facilitate the establishment of export oriented industries which are subjected to custom made policies and incentives. South Africa currently has three functional IDZs which have realised varying levels of success, namely Richards Bay IDZ (RBIDZ), Coega IDZ (CIDZ) and the East London IDZ (ELIDZ).

The South African government's New Growth Path aims at ensuring economic growth and promoting job creation. Investment into the manufacturing sector is expected to contribute to the country's growth and employment imperatives. Industrial Development Zones have been noted as having significant potential of contributing to growth.

Key success factors noted for the operation of development zones include well defined financial and policy incentives, close location to ports or main transport nodes, along with focused marketing of the zones. South Africa's Industrial Development Zones policy framework has some shortcomings which were identified in the research process. Examples of the shortcomings include lack of adequate financial incentives for investors in Industrial Development Zones and absence of a coordinated marketing strategy for the country's zones.

The shifting global economic landscape is seeing an increase in the economic power of developing countries such as the Brazil, Russia, India, China and South Africa (BRICS) bloc. As investors increasingly make steps to establish operations in new regions, development zones are expected to attract growing investment. Revision of the South African IDZ framework is anticipated to make the zones more attractive and competitive.

Opsomming

Industriële Ontwikkelings Sones (IDZs) is spesiale ekonomiese areas wat opsy gesit word om die vestiging van uitvoer-georiënteerde bedrywe te fasilitieer deur middel van unieke vergoedingspakkette. Suid-Afrika het tans drie funksionele IDZs wat wisselende vlakke van sukses bereik het; naamlik Richardsbaai IDZ (RBIDZ), Coega IDZ (CIDZ) en Oos-London IDZ (ELIDZ).

Beleggings in die plaaslike vervaardigingsektor sal 'n aansienlike bydra lewer tot ekonomiese groei en werkskepping; in lyn met die Suid-Afrikaanse regering se Nuwe Groei Pad (NGP). Die spesifieke voordele gekoppel aan Industriële Ontwikkelings Sones sal hierdie beleggings stimuleer.

Kritiese suksesfaktore sluit die volgende in: goed gedefinieerde finansiële voordele soos belastingkortings, goedgunstige beleid, ligging naby hawens of hoof vervoernetwerke, asook gefokusde strategiese bemarking van hierdie sones. Hierdie navorsing het meer as een tekortkominge in Suid-Afrika se huidige IDZ beleid geidentifiseer. Voorbeelde sluit in die gebrek aan voldoende finansiële aansporings vir beleggers in die Industriële Ontwikkelings Sones, en die afwesigheid van 'n goed gekoördineerde bemarkingsstrategie vir die land se sones.

Die skuiwende wereldwye ekonomiese landskap sien 'n toenemende groei in ekonomiese krag in ontwikkelende lande soos Brasilië, Rusland, Indië, China en Suid-Afrika (BRICS blok). Industriële Ontwikkelings Sones in hierdie lande sal na alle verwagting toenemende belegging aanlok. Hersiening van die Suid-Afrikaanse IDZ raamwerk behoort hierdie areas nog meer aantreklik en mededingend te maak.

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ABBREVIATIONS

AGOA	African Growth Opportunity Act
AIS	Automotive Incentive Scheme
APDP	Automotive Production & Development Programme
ASGISA	Accelerated Shared Growth Initiative South Africa
BBSDP	Black Business Supplier Development Program
BLFIZ	Bayan Lepas Free Investment Zone
BPO&O	Business Process Outsourcing & Offshoring
CCA	Customs Control Area
CDC	Coega Development Corporation
CIP	Critical Infrastructure Program
CIS	Co-operative Incentive Scheme
CPFP	Capital Projects Feasibility Program
DTI	Department of Trade and Industry
EC	European Community
ECDC	Eastern Cape Development Corporation
EDD	Economic Development Department
EIP	Enterprise Investment Programme
ELIDZ	East London Industrial Development Zone
EMIA	Export Marketing and Investment Assistance
EPZ	Export Processing Zone
EU	European Union
FDI	Foreign Direct Investment
FTZ	Free Trade Zone
FZ	Free Zone
FPI	Film Production Incentive
GEAR	Growth, Employment and Redistribution
GDP	Gross Domestic Product
GSP	Generalised System of Preferences
IDC	Industrial Development Corporation
IDZ	Industrial Development Zone

IEAT	Industrial Estate Authority of Thailand
IPAP	Industrial Policy Action Plan
ISC	Industrial and Services Corridor
MIP	Manufacturing Investment Program
MDA	Manufacturing Development Act
MBTPS	Medium-Term Budget Policy Statement
MIDA	Malaysian Industrial Development Authority
MFPA	Mauritius Free Port Authority
MFPZ	Mauritius Free Port Zone
NGP	New Growth Path
NIPF	National Industrial Policy Framework
PSDC	Penang Skills Development Centre
RDP	Reconstruction and Development Program
RBIDZ	Richards Bay Industrial Development Zone
SAICA	South Africa Institute of Certified Accountants
SARS	South Africa Revenue Service
SETA	Sector Education Training Authorities
SDI	Spatial Development Initiative
SEZ	Special Economic Zones
SMMEs	Small Medium and Micro Enterprises
SSAS	Sector Specific Assistance Scheme
TIA	Technology Innovation Agency
TEO	The Enterprise Organisation
TSP	Tourism Support Program
UNCTAD	United Nations Conference on Trade and Development
VAT	Value Added Tax

CONTENTS

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CHAPTER 1

1 RESEARCH OUTLINE

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1 NATURE AND SCOPE OF THE STUDY

This first chapter presents the context for this research paper and discusses the research design and literature study.

1.1 RESEARCH TOPIC

The title of this study is: *Evaluation of Industrial Development Zones in South Africa*- with focus on Coega and Richards Bay Industrial Development Zones (IDZs).

Research question

- Determine the critical success factors for operation of South African Industrial Development Zones

1.2 RESEARCH OBJECTIVES

- The main goal of the research paper is to do an evaluation of the South African Industrial Development Zones:
  - Study the factors influencing situation of Coega IDZ and Richards Bay IDZ and, identify the types of industries currently operational in the zones or how the location influences the types of industries investing in the areas
  - Examine the common critical success factors of IDZs in other developing economies

- Analysis of historic and planned investments into the zones and source regions of the historic investing businesses
- Identify ways of increasing the contribution of IDZs to the economic development of South Africa in alignment with the New Growth Path policy document by adjusting the existing IDZs framework in South Africa

1.3 OUTLINE OF THE LITERATURE REVIEW

The literature review provides insight into the Industrial Development Zones and other related concepts. An examination of studies which have been done focusing on the South African economy and other developing economies is provided in order to give context for this research.

The literature study provides background and insights to the research statement and permits an in-depth analysis into the subject area.

The literature study involves:

- A study of the relevant journals, books, newspapers, electronic publications, websites, and all other forms of published material;
- The examination of papers presented at conferences;
- Interactions with local and international experts in the field;
- The use of keyword searches in the full text academic research databases, of Emerald, EBSCO Host and ScienceDirect

The core fields of study encompasses: Industrial Development Zones, Special Economic Zones, regional economic development and spatial development initiatives. Further fields of study are revealed by cross-references or citations. These further fields are followed up and studied for their relevance.

1.4 THE SCOPE AND LIMITATIONS OF THE STUDY

This study is geographically confined to South Africa's Richards Bay and Coega IDZs. The insights from other zones in developing economies are provided in order to enable benchmarking analyses.

1.4.1 Limitations

Selection of the respondents was based on the examination of people who potentially play a significant role in Industrial Development Zones policy formulation, operations and research. However, it should be noted that given the research methodology (semi-structured) the respondents tend to have varying positions regarding critical matters. This resulted in a need to streamline and rationalise the responses provided. In the process of trying to obtain key findings, there is some potentially useful information and insights which might end up being overlooked and excluded from the study.

1.5 RESEARCH METHODOLOGY

The research methodology which was followed is discussed in the following section;

In order to examine the critical success factors for the operation of IDZs in South Africa, there was a need to obtain views from key industry participants in business, government and to an extent in labour. Examination from the perspective of these different stakeholders is necessary because of the differing aims and mandates of these constituencies. A detailed analysis of critical success factors required synthesis of the stand points of these different stakeholders.

Semi structured interviews are used in the research process in order to obtain insights into the key success factors of Industrial Development Zones in South Africa.

1.5.1 Conclusions and recommendations

Results are presented in written, tabular and graphical form and discussed in terms of their correlation with the literature.

The findings, presented in terms of the primary and secondary objectives, enable conclusions to be made regarding factors which can be considered as key success factors for Industrial Development Zones.

This research paper concludes by discussing the implications of the study on government plans to fulfil the mandate of the New Growth Path economic growth policy document. The potential of Industrial Development Zones to contribute to increased labour absorption was examined in the conclusion of the research paper.

1.6 LAYOUT OF THE RESEARCH PAPER

In order to achieve the objectives of the study discussed above the following chapters and content of this research paper are structured as follows:

Chapter one provides the introduction and outline of the research paper. This chapter includes the motivation for interest in the research, the aim of the research as well as the research objectives.

The second chapter contains the literature review. The review examines previous research done on Industrial Development Zones with focus on South African studies. It provides an analysis of the South African Industrial Development Zone incentives. South African economic policies which have a bearing on the establishment and operation of Industrial Development Zones are examined. The chapter further examines the role of government bodies directly involved in the functioning of the development zones. Lastly, this chapter also provides insight into the international experiences for developing economies in the area of Industrial Development Zones and Special Economic Zones.

Chapter three focuses on the methodology which was followed in conducting the study. Variables and data used in the research are explained along with explanations of the concepts and terminology.

Chapter four presents research findings aimed at answering the research question. The fifth chapter then provides conclusions and recommendations derived from findings of the evaluative analysis. The recommendations given in this chapter can be used in the shaping of future policy making decisions. Recommendations for further research have been mentioned in chapter five.

CHAPTER 2

2 LITERATURE REVIEW

2.1 INTRODUCTION

The review was primarily to examine previous research done on Industrial Development Zones and related matters in South Africa. Other relevant research focused on other regions was also drawn upon.

2.2 LITERATURE STUDY

2.2.1 BACKGROUND

South Africa's nine provinces are currently faced with disparities with regard to the level of economic development. The disparities are due to a combination of factors such as presence of natural resources, geographical location and socio-political influences such as historical legacy.
The Gauteng, Western Cape and KwaZulu-Natal provinces contribute approximately 65 percent to the country's total GDP (Gauteng provincial profile 2006; 40).

South Africa's drive to encourage regional industrial development dates back to the 1960's and has been part of government policy initiative. During the apartheid era, the policy initiatives were politically motivated with the aim being to develop the homeland areas in order to reduce the movement of people to the cities (Trudi, 2001). "In the early 1990s, industrial policy was markedly less focused on location. However more recently the Spatial Development Initiatives (SDI) and Industrial Development Zone (IDZ) programmes have both involved the identification of industrial locations and used incentives to encourage firms to locate in these areas" (Trudi, 2001).

Economic activities in South Africa developed and continue to do so primarily due to the physical geographical influences. As an example, the development of the Western Cape as a major fruit and wine farming province was influenced mainly due to the presence of a cool and temperate climate. Coastal towns and cities have their main activities revolving around activities such as being major trade ports for import and exporting of goods.

Although the national government focuses on trying to ensure high rates of economic development for the whole country, the level of disparities in the country are growing (Ramuhashi, 2007). Economic development and growth policies which are formulated by the national government provide the vision and direction which the country is expected to move toward in the medium to long term. Provincial and local governments are the responsible authorities for developing plans to implement the growth plans, in collaboration with national government.

Industrial Development Zones (IDZs) are aimed at stimulating the local economy of the region in which they are located. While national government focuses on providing the necessary enabling environment to drive economic development. “In South Africa, the establishment of IDZs is a recent phenomenon intended to attract investment, increase exports and the competitiveness of South African products” (Tang, 2008). IDZs are part of the global Export Processing Zone (EPZ) strategy. EPZs are established within a particular geographical area with the aim to develop and grow a targeted sector by offering incentives which can be accessed by companies in order to have a competitive advantage in their industrial exports (Tang, 2008).

South Africa’s economy was historically built on the foundation of the mining industry. The services sector which currently contributes approximately 67 percent to the country’s Gross Domestic Product (GDP), overtook the importance of mining and other primary and secondary sector activities. The Department of Trade and Industry’s IDZ program is geared toward “raising the competitiveness of the manufacturing sector through leveraging investment in export-oriented manufacturing industries and the export of value-added manufactured products” (DTI, 2008: 5) .

2.2.2 FOCUS ON DEVELOPMENT ZONES

Establishment of IDZs is with the aim to attract investment into regions which ordinarily would not have been attractive for investors to venture into. In order to ensure attractiveness of the zones, the government needs to have incentives which are specifically targeted at stimulating investors to consider the investment destination.

Due to globalisation, when investors from different parts of the world decide where to invest, they scout for opportunities in all the different continents. Foreign Direct Investment (FDI) is highly dependent on the form and nature of incentives offered by host countries (Sello, 2007). South Africa currently does not have specific incentives which are targeted at Industrial Development Zones. The incentives which are offered in the IDZs are manufacturing specific incentives which are also available to qualifying companies outside the IDZs.

A Special Economic Zones (SEZs) Bill was gazetted in January 2012 by the Minister of Trade and Industry Dr Rob Davies. Under this Bill, IDZs will no longer be classified as a separate entity but will be classified as SEZs (Davies, 2012). Previously, a key requirement for a region to qualify as an IDZ was proximity to either an international sea or airport. The Bill is expected to facilitate spatial development of other regions previously sidelined by the IDZ framework.

In other parts of the world, countries use zones such as Free Trade Zones (FTZs), Export Processing Zones (EPZs) and Special Economic Zones (SEZs) for industrial development purposes. The common factor between all these zones is the focus on providing a competitive investment area able to provide investors access to advantages absent in other parts of the country.

European Community (EC) countries have Free Zones (FZs) whose main function is to "facilitate trading procedures by allowing fewer customs formalities" (Erasmus, 2011). Austria, Belgium, Lithuania, Luxembourg, Slovakia and Sweden are the only EC countries which do not have FZs. Import duties, Value Added Tax (VAT) and other import charges are exempted for goods placed in the FZs (Erasmus, 2011).

According to the Import Administration agency in the United States, there are close to 277 Foreign Trade Zones operating in the country. These zones are "special commercial and industrial areas in or near ports of entry where foreign and domestic merchandise, including raw materials, components and finished goods may be brought in without being subject to the payment of customs duties" (Hinkelman *op.cit*).

2.2.3 PERFORMANCE OF IDZs

The main issues which are raised when there is a discussion about Industrial Development Zones revolves around the ownership model, incentives offered, differentiating factors with other countries and the labour framework.

Coega IDZ is one of the four functioning zones in South Africa which has been under a lot of scrutiny regarding the effectiveness of the zone. Although a lot of money has been spent on the development of the zone, the returns on investment which have been realised in the zones' decade long lifetime have been below expectations. When Coega was established the anchor tenant was the Canadian Alcan steel company. When the steel company reconsidered their initial plan, Coega was left without a main tenant, hence the approach of trying to get different investors to establish operations in the zone.

2.3 ECONOMIC GROWTH POLICIES GOVERNING IDZs- HISTORIC AND PRESENT

The establishment of Industrial Development Zones is primarily "aimed at raising the competitiveness of a country's manufacturing sector through leveraging investment in export-oriented manufacturing industries and the export of value-added manufactured products" (DTI, 2008:5). The National Industrial Policy Framework (NIPF) set out by the South African government identifies the importance of having Industrial Development Zones as catalysts for growth and development of the local economy.

Industrial Development Zones are geographically defined areas intended for major commercial activities and industrial development. IDZs form part of a broader Spatial Development Initiative (SDI) concept by government. Spatial Development Initiatives provide private companies with the opportunity to utilize government resources such as infrastructure, water and electricity for their business activities (Hosking, 2002).

"The IDZ program is intended to encourage international competitiveness of the South African based manufacturing sector. The program consists of purpose-built industrial estates linked to an international port or airport in which quality infrastructure and expedited customs procedures are coupled with unique duty-free operating environments suited to export-oriented production," (the dti, 2011).

As the 1980s were coming to an end and 1990s were being ushered in, the national industrial policy which was in place in the apartheid era had certain aspects which resemble the country's present IDZ policy. Programs under the auspices of spatial development initiatives were specifically set up with the aim to encourage investment in untapped locales of the country. The South African government promoted the potential benefits which would be realized from a rise in the level of industrial investment, performance and exports (Tang, 2008). "South Africa's Industrial Development Zones initiatives and spatial development initiatives have been involved with the identification of industrial locations in specific unfavourable areas and have used incentives to encourage firms to situate themselves in these areas" (Tang, 2008).

2.3.1 ECONOMIC GROWTH POLICIES

In the period after 1994, a number of growth policies have been formulated with the aim of spearheading growth of the economy targeting reduction and possibly eliminating the widespread socio-economic disparities. The Reconstruction and Development Program (RDP) which was formulated and initiated in 1994 had its main focus on fostering growth of local economies through establishment of institutions with the aim of addressing local economic development needs. The needs included job creation and community development (RDP, 2000).

Nevertheless, in South Africa's economic policies there was not much focus on the role that would be played by IDZs in the economic development of the country.

The South African government shifted from the RDP to a new macroeconomic policy framework, called the Growth, Employment and Redistribution (GEAR) strategy. The main focus of GEAR was to establish a high growth and competitive economy. This was to be achieved through, "stringent fiscal and monetary discipline, significant increase in foreign and domestic investment, institution of further steps to open the economy to international competition and re-prioritizing public expenditure," (Harsch, 2001). As with previous macroeconomic policies post-1994, GEAR was aimed towards growing the economy and benefits trickling down to the general populace.

The GEAR policy was established with the aim to "achieve sustainable economic growth coupled with the creation of employment at a rate of 270 000 new jobs by the year 2000. The original growth target was a real GDP growth rate of 6% by the year 2000" (Strydom, 2000). In order to grow the economy, increasing focus by the government on Industrial Development Zones was prioritised. Given the manufacturing industry's potential to absorb more labour than other sectors of the economy, labour intensive industries tend to get special preference in these zones as government aims at tackling the high levels of unemployment.

After the GEAR policy, government developed the Accelerated Shared Growth Initiative South Africa (ASGISA). It has been noted that South Africa's IDZ policy aligns with ASGISA (Tang, 2008).

The framework postulated by ASGISA aimed to have achieved shared growth by 2014 along with halving unemployment and poverty by 2014. The framework highlights that in order to achieve this; there is a need for establishment of South Africa, "into a sustainable, internationally competitive, rapidly growing, labour absorbing economy within an outward-oriented policy framework," (ASGISA, 2007).

South Africa adopted a New Growth Path (NGP) policy framework. The Economic Development Department (EDD) is “focussed on developing the NGP framework, supporting implementation, partnering with other departments and public entities to align the work across government to the over-arching new framework” (Patel, 2011). The NGP continues in the spirit of previous policies such as ASGISA and the National Industrial Policy Framework (NIPF), thus showing necessity of economic restructuring in a bid to guarantee more inclusive and sustainable growth.

IDZs in South Africa are recent phenomena. South Africa’s IDZ program was established in September 2000 with the objective to, “augment the country’s manufacturing sector through encouraging investment in export oriented manufacturing industries, with emphasis on beneficiation or value adding of the country’s natural resources” (RBIDZ, 2011).

The Coega IDZ which covers 11,000 hectares is South Africa’s first IDZ initiative which was established in October 1996 (Driver, 1998). Coega IDZ was gazetted in 2001 (Luiz, 2003) and developments in the zone started in August 2002. It should be noted that the zone is not yet fully functional and there is still scope for new investments.

Coega IDZ is regarded as the largest development zone on the African continent. The government’s expenditure on the zone is currently in excess of R8 billion. The capital expenditure has been used as follows, “R3.1 billion for a new deepwater port, R2 billion for infrastructure in the IDZ, R2.1 billion by the State electricity Eskom to upgrade the power supply and the State rail Transnet’s contribution is estimated at R500 million for the upgrade of the rail facilities,” (Coega, 2008).

Coega and East London IDZs obtained their licenses to operate as IDZs in 2002 while the Richards Bay IDZ obtained its license in 2005. Although Coega has been in operation for close to a decade, the levels of FDI into the IDZ have not reached the expected levels. Hosking and Bond (2000) highlighted the potential lack of viability of the Coega IDZ due to high opportunity costs. As an example it was estimated that the “*ecotourism opportunity cost for the region was around R50 million each year,”* (Hosking, 2000). The research outlined other issues such as potential threats on the environment which could affect local industries such as fishing and citrus.

Historically there haven't been any specific tax incentives directed to IDZs which have been outlined in the national budget. In the 2011 National Budget speech, a R20 billion manufacturing tax allowance provision was announced for businesses making Greenfield or Brownfield investments in the South African economy. Greenfield investments in IDZs qualify for additional relief- this is noted as the first specific tax incentive in South Africa directly targeting IDZs.

"In order to limit the incentive to projects that provide a substantial benefit to the economy, the cost of new and unused manufacturing assets for green-field projects may not be less than R200 million. For brown-field projects the cost of existing manufacturing assets must be increased by at least 25% of the cost of pre-existing assets (but no more than R200 million) or R30 million, whichever is the higher amount (SAICA, 2009).

2.4 THE SOUTH AFRICAN INDUSTRIAL DEVELOPMENT ZONES PROGRAM

South Africa's Industrial Development Zones (IDZs) program falls under the mandate of The Department of Trade and Industry (dti) is the government entity under which the Industrial Development Zones mandate falls. The Enterprise Organisation is a unit of the dti in charge of the IDZ program.

2.4.1 THE ENTERPRISE ORGANISATION

The Enterprise Organisation (TEO), "aims to stimulate and facilitate the development of sustainable and competitive enterprises, through the efficient provision of effective and accessible incentive measures that support national priorities" (the dti, 2011).

One of the aims of TEO is to develop institutions and governance structures for IDZs which seek to enhance the co-ordination between different spheres of government, along with other institutions in the country which are critical for success of the program. TEO is also tasked with developing a financing model for the IDZ program (the dti, 2011).

A problem which had been noted before the establishment of TEO was the fragmentation inherent between different government departments. Lack of clear communication and collaboration in different government spheres has resulted in a lot of duplication of efforts within government. Rationalisation of the way government departments work together is expected to help the dti make the IDZ program more efficient.

2.4.2 THE SOUTH AFRICAN INDUSTRIAL DEVELOPMENT ZONE CONCEPT

South Africa’s Trade and Industry minister can designate an area to be an IDZ if the designation will meet the following criterion;

- “establishment of the zone will facilitate creation of an industrial complex having strategic economic advantage;
- the zone will provide the location for the establishment of strategic investments;
- exploitation of resource-intensive industries will be enabled;
- establishment of the zone will utilise existing industrial capacity in the region, facilitate integration with local industry and also increase value-added production;
- employment creation should be a by-product of establishment of the zone and other economic and social benefits must accrue to the region of location; and
- the designation of the zone must be consistent with any applicable national policies & law, as determined by appropriate environmental, economic and technical analyses.”

(SARS, 2011)

2.5 KEY POLICY DOCUMENTS

South Africa's Industrial Development Zones are governed by four main policy documents; New Growth Path, Manufacturing Development Act, 2010/11 Industrial Policy Action Plan (IPAP2) and the IDZ Policy Review. The aforementioned are the main documents, however the country has other policies such as the 'Economic Development Department's Mid-term Strategic Plan (2010/11- 2012/13) which addresses industrial policy and economic development.

2.5.1 NEW GROWTH PATH (NGP)

The NGP is committed to identifying areas where employment creation is possible on a large scale in line with the government's plan to create decent work. Under the New Growth Path, the focus is for policy development to be facilitated through strategies such as; a drive for social equity and competitiveness, mobilising domestic investment around activities that can create sustainable employment and strong social dialogue to focus all stakeholders.

2.5.2 MANUFACTURING DEVELOPMENT ACT (MDA)

The 2000 Amendment to the MDA established the IDZ Program, and allowed for the appointment of IDZ operators and enterprises. The MDA also clearly defines the Customs Control Area (CCA), the Industrial and Services Corridor (ISC) and the special legislation granted under the South African Revenue Services (SARS).

2.5.3 INDUSTRIAL POLICY ACTION PLAN (IPAP) 2

South Africa's IPAP2 is developed under the National Industrial Policy Framework (NIPF) and identifies key sector clusters particularly in labour-intensive industries. The policy is designed to address declines in industrial and manufacturing capacity, and chronic unemployment in the South African economy. IPAP 2 is a policy and an action plan designed to help build South Africa's industrial base in critical sectors of production and value-added manufacturing.

2.5.4 IDZ POLICY REVIEW

In order to ensure a consistent policy environment for IDZs, there is a constant review of the IDZ policy environment to ensure that IDZs are leveraged as effective industrial policy tools. Such reviews enable aligned of IDZ policy and incentives with the key sector thrusts outlined in other policy documents such as IPAP2. Industrial Development Zones have considerable potential to be able to support the implementation of the NGP, and encourage economic development through infrastructure projects.

2.6 OLD VS NEW POLICY DEVELOPMENT STRUCTURES

Under the old policy development structure, the Department of Trade and Industry was responsible for all policies related to IDZs.

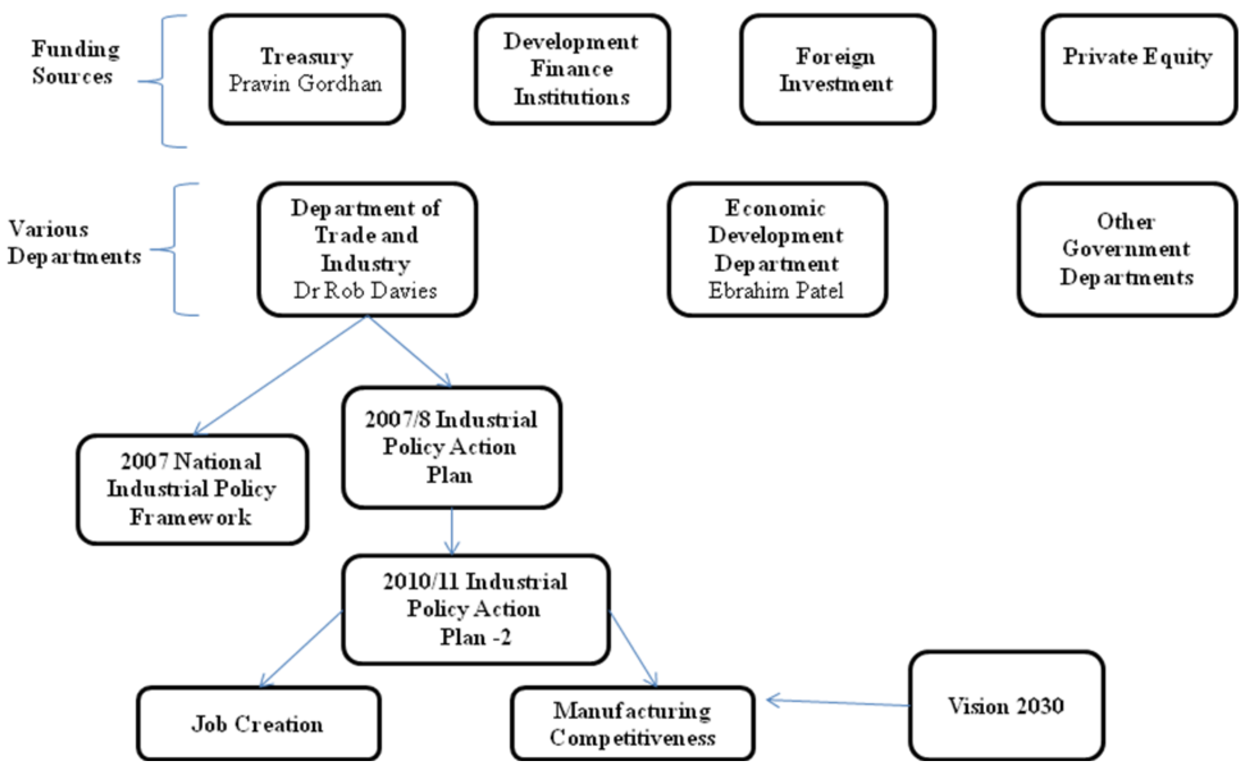

Figure 2.1 Representation of Old Policy Development Structure

Source: Frost & Sullivan, 2010

The old policy development structure did not have specific focus on Industrial Development Zones. IDZs fell under the ambit of the Manufacturing Development Act (MDA) which is part of the National Industrial Policy Framework (NIPF).

South Africa's Economic Development Department (EDD) released the New Growth Path Framework on 23 November 2010 with the core objectives of

- improving performance in terms of labour absorption
- improving composition and rate of growth in the economy

Under the new policy development structure, the New Growth Path is the main framework supported by pillars such as the **dti's** IPAP2, the Medium-Term Budget Policy Statement (MBTPS) and the EDD 2010/11 Medium Term Strategic Plan.

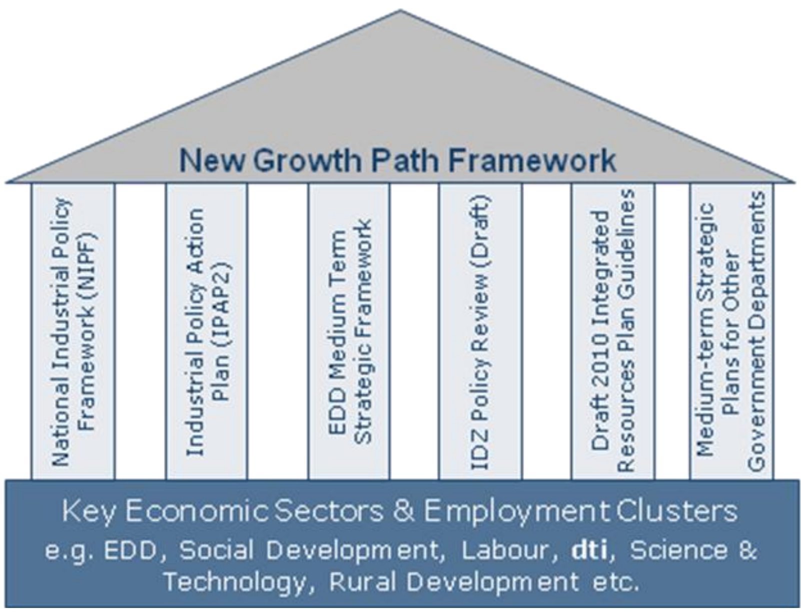

Figure 2.2 New Policy Development Structure aligned with the New Growth Path

Source: South African Government

These policy documents do not have a direct focus on Industrial Development Zones, but the interrelationships between the policies they also share the same objectives such as boosting investor confidence and job creation. Industrial Development Zones have the potential of being used as leverage for the South African government to achieve the growth and employment objectives.

Table 2.1 Linkages between the South African Industrial Development Policies

	New Growth Path	MDA	IPAP2	IDZ Review
Employment	Target: 5 million jobs by 2020 through the use of 'job drivers'	Regulations have a clear emphasis on employment creation and uptake of local content	Each sector has direct job targets – forms the basis of the 5 million jobs target	Ensure that the IDZs are aligned to support the six "job-driver" sectors
Wealth Creation	Focus on sectors that reduce inequality and eradicate poverty	Focus on utilising all inputs e.g. Labour, raw materials, land & technology for industrial development	Promotes uptake of local content in the value chain and therefore supports SMMEs and skills training	Successfully generate investment and generate decent work within the identified locations and regions
Socio-Economic Development	Create decent work and support the growth of a developmental state, not a welfare state	Promotes uptake of local content in the value chain and therefore supports SMMEs and skills training	Creates demand for economic growth through procurement and industrial financing	Incorporates key action plans from other policy documents such as the integrated sustainable rural development program and urban renewal program
Industry-Specific targets	Ipap2 sectors, infrastructure, tourism, agriculture, mining & green economy	Promote value-added manufacturing activities and industrial capacity, as well as utilise resource-intensive industries	Ipap2 has specific action plans in critical sectors of production and value-added manufacturing	Good sector focus, but it will be difficult to meet job targets with some of the key action points – and no mention of the IDZ as a lever for implementation
Summary	IDZs can definitely play a role in supporting the NGP framework, but no defined "implementable" steps or	Overall guidelines are comprehensive, but require a strict governance policy – which is not clearly defined for IDZs	Good sector focus, but it will be difficult to meet job targets with some of the KAPs – and no mention of the IDZ as a lever for implementation	A necessity if the IDZs are ever going to achieve their mandate and address the challenges

2.7 NATIONAL INCENTIVES BENEFICIAL TO IDZ ENTERPRISES

2.7.1 Overview

Investing in South Africa's IDZs has been noted to offer the following benefits for investors; duty free production for exports, VAT-suspension for supplies procured in South Africa and efficient administration characterised by speed and convenience.

Establishment of a single window facility for investors has assisted reduction of the administration and bureaucracy usually associated with establishment of a new enterprise. The 'one-stop-shop' facility is provided for potential investors into IDZs. All the necessary regulatory and documentation services are provided in one place to ensure ease of setup.

2.7.2 12i Tax Allowance

The 12i tax allowance is a R5.6 billion program designed to support Greenfield (new investment in manufacturing) and Brownfield (upgrading existing projects) with additional allocations for training and capital. This incentive offers different allocations based on the type of project, and whether the project qualifies under preferred status qualifying criteria.

Qualifying criteria includes improved energy efficiency; utilising local Small Medium and Micro Enterprises (SMMEs) in the value chain; and whether the company is located within an IDZ. Companies can qualify for allowances of R350 million (Brownfield) to R900 million (Greenfield with preferred status), with an additional R36,000 per employee training allowance. These allowances are capped at an investment allowance of R900 million, and a training allowance of R30 million.

2.7.3 The Automotive Incentive Scheme (AIS)

AIS is a taxable cash grant incentive which is part of the Automotive Production & Development Programme (APDP). The scheme aims at growing and developing the South African automotive industry through encouraging investment in advanced technology.

Qualifying firms are provided with a grant of 20% of the value of qualifying investment in productive assets. An additional 5-10% over and above the 20% is available for projects that meet criteria such as maintaining base year employment levels, and the strengthening of backward and forward linkages.

2.7.4 The Black Business Supplier Development Program (BBSDP)

The purpose of the BBDSP is broader participation of black-owned SMMEs through the provision of business development services. This program targets companies which are majority black-owned entities, with annual turnover of less than R12 million. The offering is a 90:10 cost sharing grant for business development services, with a maximum funding of R100,000 per enterprise.

2.7.5 Business Process Outsourcing & Offshoring (BPO&O)

The purpose of the BPO&O is to encourage employment opportunities in the services sector by targeting enterprises offering BPO&O services. The offering is a training grant worth max. 50% of the qualifying expenditure, as well as an investment grant for investment costs. The maximum funding which can be granted to an enterprise is R60, 000 per seat for investment, and R12, 000 per agent for training costs.

2.7.6 Capital Projects Feasibility Program (CPFP)

CPFP promotes the export of South African capital goods and services, with a focus on capital goods sectors and consulting engineering services. The programme offers a cost-sharing grant (up to a maximum. of 55%) for feasibility study costs, with a cap of R5 million.

2.7.7 The Critical Infrastructure Program (CIP)

The CIP aims at promoting investment through facilitation and provision of critical infrastructure Targets of the program encompasses, local and provincial government, private sector enterprises, private public partnerships, and industrial developments. The program is a cost sharing grant (with a maximum of 30%) of development costs in qualifying infrastructure.

2.7.8 Manufacturing Investment Program (MIP)

The MIP falls under the Enterprise Investment Programme (EIP) with the specific purpose of promoting investment in the manufacturing sector with a target of manufacturing companies, particularly in key sector thrusts that require investments up to R200 million. There is 15-30% grant for qualifying investment in land & buildings, machinery and equipment and customised commercial vehicles, with 15% transportation costs for imported machinery and equipment by Foreign Direct Investment.

2.7.9 Tourism Support Program (TSP)

The TSP falls under the Enterprise Investment Programme (EIP) and is targeted at tourism businesses. The aim is to promote job creation in non-traditional tourism clusters, with a 15-30% grant for qualifying investment in land and buildings, furniture, fittings and equipments, and tourism vehicles.

2.7.10 Export Marketing and Investment Assistance (EMIA)

EMIA targets export-ready manufacturers to assist them to develop an export market for South African goods and services, and encourage Foreign Direct Investment. The EMIA offers a cost-sharing grant for exhibition costs, marketing material and research in foreign markets.

2.7.11 Sector Specific Assistance Scheme (SSAS)

The SSAS has a similar purpose to the EMIA, however it is more specifically focused on non-profit business organisations (e.g. export councils, business associations, joint action groups etc.) in key sector thrusts There is a cost-sharing grant (up to a maximum of 80%) for developmental projects.

2.7.12 Film Production Incentive (FPI)

South Africa has a favourable climate and tourism sector that promotes Film and TV productions. In order to reduce the barriers and encourage investment in film production and exports, the dti offers 15% funding for qualifying expenditure for foreign films and 25-35% funding for local films. The max funding per enterprise is R10 million.

2.7.13 Co-operative Incentive Scheme (CIS)

The CIS targets registered co-operatives that operate in the emerging sectors, as well as manufacturing, retail and services. The incentives offers a 90:10 cost sharing grant for machinery, equipment and business development services, with a max funding of R300,000 per enterprise.

2.8 IPAP AND NGP ALIGNED SECTORS

Industrial policy and the Industrial Policy Action Plan (IPAP) are part of a number of policies which are inter linked to form the base for the New Growth Path (NGP). "IPAP emphasises that sectors have differing characteristics and are important in an economy in their own right, as well as through the impact they have on other sectors, particularly via multiplier effects" (IPAP 2, 2011: 34).

Sectors covered by the NGP and IPAP

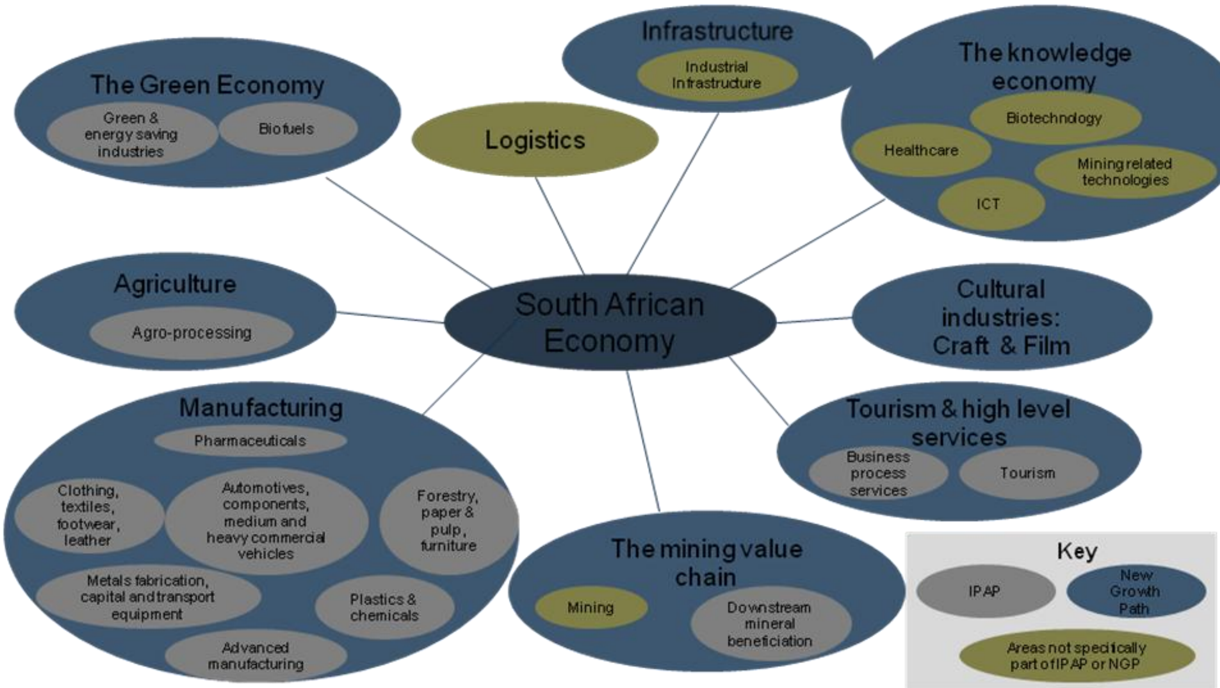

Figure 2.3 IPAP 2 and NGP related sector focuses

Source: Industrial Development Corporation, 2011

2.9 INTERNATIONAL EXPERIENCES WITH INDUSTRIAL DEVELOPMENT ZONES

Use of Industrial Development Zones and/or Special Economic Zones in different countries has for the purpose of driving economic growth has been widespread across the world.

2.9.1 INCENTIVES AND ELEMENTS OF INVESTMENT CLIMATES

Export Processing Zone (EPZ) investment climate involves a three-level hierarchy, with each level having distinct attributes or investment climate elements (Sit, 1988):

- Macro-climate-comparative advantages of the host country.
- Meso-climate-measures aimed at restricting and restraining national policies and practices that would deter the development of export industries.
- Micro-climate-suitable siting, infrastructure, and incentive package.

The presence of the key elements at different levels is expected to coexist with a demand factor in the capital-export source. This enables the EPZ to become an active ground for foreign and joint-venture investment in export-oriented manufacturing. The demand factor may be caused by cost-minimization considerations; a new location requirement promoted by technological change, a new marketing strategy and market expansion, or a combination of all of these.

2.10 CASE STUDIES OF SOME ECONOMIC DEVELOPMENT ZONES

The following case studies are targeted at providing insights into key features of some Industrial Development Zones which are situated in some developing countries. The three examined zones are expected to provide some insight into different best practices and some critical success factors which are characterized by these zones.

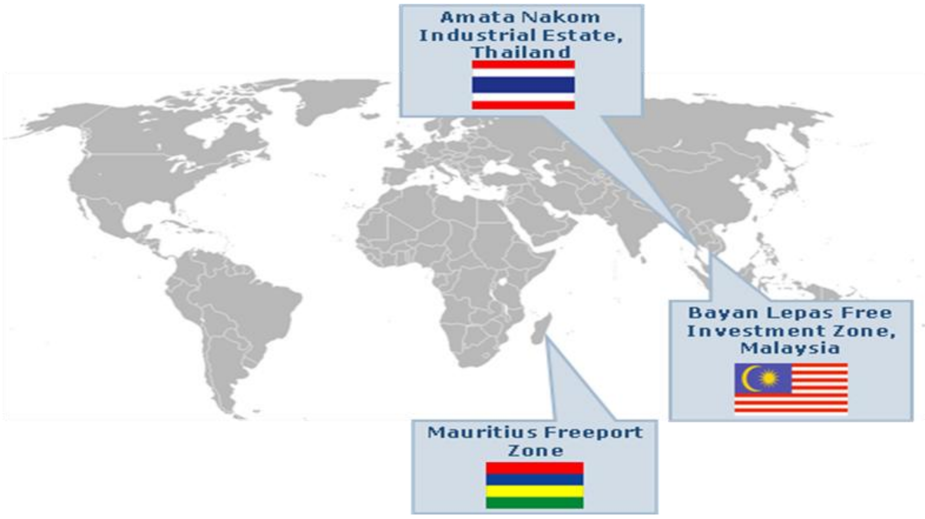

Figure 2.4 Geographic locations of the economic zones examined

Malaysia

Malaysia is an Asian country which experienced rapid growth in the late 1990's. The country's economy changed from focusing on import-substitution which had been used to stimulate domestic employment, to focusing on developing export markets. Although effective to a certain extent, import substitution would have the impact of reducing outflows in the country's current account. Focusing on the export market would contribute to bolstering the inflows to the country. The export markets were used to promote export processing and development of free trade zones.

Regional development plans in Malaysia are structured based on developing particular industries in the different regions. The regions in turn offer investment incentives which are in line with the types of industries which are located in those areas. Success of the free investment zones in Malaysia has been largely premised on the Free Trade Zone Act which was gazetted in 1971 by the Penang State Government.

Table 2.2 Geographic dispersion of free investment zones in Malaysia

Authority	Region	Industries
Iskandar Regional Development Authority	Southern Peninsular Malaysia	Creative industries, Educational services, Financial advisory and consulting services, Healthcare services, Logistics services, Tourism related activities
Northern Corridor Economic Region	Covers the northern states of Kedah, Northern Perak, Perlis and Penang Island	Agriculture, Manufacturing – particularly electrical and electronic products Tourism
East Coast Economic Region	States of Kelantan, Terengganu, Pahang and Mersing district in Johor	Tourism Agriculture, Oil, gas and petrochemicals, Manufacturing Education

Source: Indian High Commission - Doing Business in Malaysia - Handbook for Indian Business

The establishment of the industries in the different zones was based on the strategic location advantages offered by the different regions. The Northern part of Malaysia has better access to the interior of Asia which enables linkages with other manufacturing hubs in countries such as China and Singapore. Focus on manufacturing of electronics is predicated on the presence of easy access to the necessary components to facilitate 'Just In Time' manufacturing.

2.10.1 Bayan Lepas Free Investment Zone (BLFIZ)

BLFIZ is situated in the Penang province in the northern part of Malaysia. The major investors in BLFIZ are Intel, Hitachi, Toshiba, Philips, Bosch and Clarion. The zone was established in 1972 and it covers 5.3 km^2 (1300 acres). Some key success factors for the BLFIZ are discussed in this section.

Infrastructure

Similar to other cases in many of the Special Economic Zones around the world, the Penang Development Corporation reports that investors into Bayan Lepas consider world-class infrastructure to be a minimum requirement for attracting investment.

The combination of world-class infrastructure and attractive import/export incentives originally attracted export-oriented manufacturers, particularly from abroad, to move or expand their operations in the FIZ. The presence of adequate infrastructure enables investors to have a convenient procedure when it comes to setting up operations.

Financial Incentives

Although the Malaysian government provided infrastructure, they understood this was not enough to attract foreign direct investment (FDI). This realisation allowed for the establishment of the Investment Incentives Act of 1968.

The Malaysian government has allowed for continuous revision of these financial incentives in order to attract the types of industries that Malaysia wants to develop.

The scope of the incentives made provision for the Investment Tax Allowance as well as the double deduction of expenses to Promote Exports. In 1971, in a bid to reduce unemployment in the country, the Labour Utilisation Relief program was introduced to attract labour-intensive industries. The program was structured in a way which links the level of corporate tax exemption to the number of local workforce employed.

Policy Incentives

The Malaysian government has also used a number of policy incentives to support the financial incentives which have been used in attracting FDI.

From July 1998, foreign investors were allowed to own 100% equity in their new or expansion driven projects, regardless of the level of exports generated by the operations. The bureaucratic red tape usually associated with making investments in a foreign country hinders some investors from investing. The World Bank's *Ease of Doing Business* measure is a leading indicator for investors as they make decisions to venture into international markets.

In Malaysia, the process for approving a manufacturing licence was reduced from two months to seven days which greatly reduced the turnaround time for potential investors to know the outcome of their applications. Most of the documentation which is required in the registration process would have been adjudicated in the application for a manufacturing license. Upon approval of the license, registration of a business takes approximately an hour.

Support Services

Support services are also considered important for attracting investors into the FIZ. The Penang Skills Development Centre (PSDC) was established to facilitate foreign companies to have access to trained craftsmen and engineers.

The Malaysian Industrial Development Authority (MIDA) hosts the Industrial Support Division. This division assigns a task force to help each company to ensure its projects are implemented smoothly. The task force is involved on a step by step basis for the projects.

Marketing

Although Free Investment Zones might have access to high quality infrastructure, offer incentives and support services, all these elements are likely to go to waste if potential investors are not made aware of these. Marketing of the FIZs is shared between the MIDA and the Penang Development Corporation.

Both organisations have a mandate to promote FDI into the FIZs since these are considered the vehicles for industrial growth in the rest of the country. Collaboration between the country's industrial development authority and the regional development corporation enables the country to align regional development with overall country development objectives.

Globalisation and an ever-increasing level of competitiveness between the Asia Pacific countries has seen the marketing bodies play an important role for attracting FDI. All of these measures have helped Malaysia to move two notches up to 21st out of 181 countries in the World Bank Doing Business Report for 2011 (Doing Business, 2011).

2.10.2 Mauritius Free Port Zone (MFPZ)

Mauritius is an island situated in the Indian Ocean off the southeast coast of Africa, about 900 kilometers east of Madagascar. The MFPZ serves as a transport hub due to the availability of ports which can cater for ocean liners transporting different cargo. A number of factors have been noted which provide advantages which assist investors into the zone.

Infrastructure

The free-port zone is classified as a logistics and distribution hub and therefore the facilities have been made to comply with international shipping standards. Investors can make use of facilities such as container yards for storage and transportation of goods. The zone has 60,000 m^2 of warehousing for dry goods and 60,000 m^2 for warehousing frozen goods. Plug in facilities for refridgerated (reefer) containers are located in the MFPZ. In the event of the harbour at Mer Rouge port being full, cargo transport from the container terminal to the free port zone is provided.

Geographic Location

The location of the Mauritius Free Zone represents the key draw card for investors primarily involved in the export and import of goods to and from Southern and Eastern Africa. The geographic location of the zone has allowed it to act as a bridge for the export and re-distribution of raw materials and products between Southern and Eastern Africa, as well as Middle East and Asian countries such as India. This zone provides access to over 425 million consumers from Southern and Eastern Africa, with an import potential of $100 billion per annum.

Marketing

Marketing of the MFPZ is done as collaboration between the Mauritius Board of Investment and the Mauritius Free Port Authority (MFPA). The Board of Investment is responsible for the marketing of the country to the global market, but places a strong emphasis on the free port zone and its benefits for investors. The MPFA is responsible for the day-to-day running of the zone.

The marketing strategy focuses primarily on countries with a history of high investment in the Southern and Eastern African region. There is a large focus on the development of relationships with national trade organisations.

Policy Incentives

The Mauritius free port zone is a signatory member of key trade agreements that allow preferential tariff rates/ free import duties. The trade agreements include the African Growth Opportunity Act (AGOA) 2000 which provides access to the US market, and the Generalised System of Preferences (GSP) for exports to the European Union (EU).

Key requirements for investors under policy incentives include the following:

- 100% foreign ownership with the free repatriation of 50% of the profits
- The remaining 50% of profits must be used in the local market
- No foreign exchange control
- Reduced port handling charges for goods destined for export
- Access to offshore banking facilities

Financial Incentives

According to the MFPA the financial incentives offered by the free port zone are considered a standard offer for investors. These include:

- Zero corporate tax on trading activities within the free port zone
- 15% corporate tax reduction on goods processing and light manufacturing
- Duty-Free and VAT free for goods and equipment imported into the zone

Support Services

A free-port traditionally offers a broader range of services that are adapted to meet the requirements of the investors. One of the core services includes ship repair and maintenance since there are large shipping volumes, as well as repairs to containers.

The MFPA has also provided an electronic investor support program that allows for online declarations and licensing of companies. International companies are able to license their business in 48 hours. The system also allows companies to access real-time data about the stock levels.

2.10.3 Thailand Amata Nakorn Industrial Estate

Thailand is located in Southeast Asia’s interior. The country has a surface area of approximately 513,000 square kilometres (km). Thailand is classified as the second largest economy in Southeast Asia after Indonesia. Despite this, Thailand ranks midway in terms of wealth spread in the region, since it is the fourth richest nation, based on GDP per capita, after Singapore, Brunei and Malaysia (Economy Watch, 2010).

The country’s economy functions as an anchor economy for the neighboring developing economies of Laos, Burma, and Cambodia. Recovery from the 1997–1998 Asian financial crisis was premised primarily on exports. Thailand ranks high among the world's automotive export industries along with manufacturing of electronic goods.

Infrastructure

Key infrastructure within the industrial estate includes state-of-the-art road infrastructure. Prebuilt factories are developed to the investor’s requirements, and are available for purchase or for rent. Investors are saved from the inconvenience of having to co-ordinate construction activities in a foreign land as the government does this for them.

Geographic Location

The attractive location of the industrial estate is one of the largest driving factors for foreign direct investment into the estate. The zones proximity to major ports and airports limits logistical lead times and its location relative to major eastern manufacturing industries increases its attractiveness for investment. The zone is located 57km from Bangkok, 42km from the new Bangkok international airport and 46 km from the Laem Shabang Deep Sea Port.

Policy and Financial Incentives

Financial incentives further increase the attractiveness of investment in the estate. According to the Industrial Estate Authority of Thailand (IEAT), the labour wages in Thailand are 2 to 3 times higher than other manufacturing bases in Asia (i.e. India, Bangladesh, Malaysia etc). A large emphasis is therefore placed on financial incentives for attracting foreign companies in high-value manufacturing activities such as automotive and electronic components.

Incentives offered include: no tax on importing and exporting companies, no duties on exported and imported goods, free repatriation of profits and 100% ownership of investment and land. Industrial, commercial and service operators are also granted the right to bring skilled labour and professionals, as well as their families and dependents for a time deemed appropriate by the IEAT board.

Marketing

Amata Nakorn relies primarily on the establishment of an investor-friendly environment with particular focus on its favourable location and tax incentives to attract investment. However, any direct marketing initiatives undertaken by Amata Industries are conducted in correlation with government officials from the IEAT and Ministry of Industries in order to coordinate efficient investment into Thailand. Leveraging of the attractiveness of the Amata Nakorn industrial estate is done through coordinated marketing initiatives.

The initiatives encompass regular state and unofficial visits with companies in countries that invest in large-scale FDI projects and usage of tradeshows as an important marketing tool for developing new leads.

Support Services

The majority of industries situated within the industrial estate are medium to heavy industry with substantial energy requirements. The industrial estate guarantees electricity supplies of an 80MW substation and a 277 MW plant, as well as natural gas turbines. Other infrastructure includes telecommunications, water and waste-water facilities.

2.11 CONCLUSION

Governments in the examined countries all utilise Industrial Development Zones (Special Economic Zones) as catalysts for attracting FDI and growing the country’s industrial base. Each country has different factors contributing to establishment of the Industrial Development Zones.

Minimum requirements which are common in the different zones include a favourable geographic location and supporting infrastructure. In order for investors to be attracted into the zones, government has to also have financial and other policy incentives in place. Successful zones provide one stop facilities whereby investors do not have to go through a lot of bureaucratic processes for registering a business entity.

Attracting investment in the development zones is highly related with the presence of clearly targeted financial incentives. Exemptions of import duties and other taxes such as Value Added Tax (VAT) and taxes related to employment are some of the incentives which attract investors to Industrial Development Zones.

Government is expected to provide adequate support services and an enabling environment for investors in the zones, but there should be minimal or no interference with the day to day operations of the zones. Removal of this interference which is characteristic of other regions in the economy increases the ease of doing business and attracts investment into the zones.

Zones which have been noted to also have a high level of success are those which have a specialised focus area. Rather than having a zone where investors from different unrelated industries operate, a specialised zone helps government to provide the right policy framework suited with the type of entities. The marketing of the zones to investors is made easier when there is specific focus by the zones.

Companies establishing their operations within the zones also benefit from the synergies which arise due to the close proximity of related businesses. As an example, car manufacturers will benefit from having component manufacturers close to them in an automotive focused development zone.

CHAPTER 3

3 RESEARCH METHODOLOGY

3.1 INTRODUCTION

The research methodology which was followed is discussed in the following section; in order to examine the critical success factors for the operation of IDZs in South Africa, there was a need to obtain views from key industry participants in business, government and to an extent in labour. Examination from the perspective of these different stakeholders is necessary because of the differing aims and mandates of these constituencies. A detailed analysis of critical success factors required synthesis of the stand points of these different stakeholders.

3.2 QUALITATIVE ANALYSIS

The research methodology employed was the use of semi-structured interviews. A standard questionnaire is drawn up and administered to targeted individuals within the mentioned stakeholder groups. Interviews are semi-structured in order to enable capturing of different perspectives which might be hard to capture using a structured methodology.

3.2.1 The survey instrument

Examination of the critical success factors was done via usage of questionnaires which focused on the following main areas

- Locational factors influencing particular types of activities
- Incentives provided in the different development zones
- Factors affecting access to market
- Impact on employment levels in the region

3.2.2 Data gathering

The data gathering process was undertaken using the questionnaire combining the above mentioned focus areas. The survey was done through face to face interviews, electronic mail and telephonic interviews.

A copy of the research questionnaire used for this research is attached in the appendices.

3.3 CONCLUSION

The research process involved interviews with individuals involved in different areas of operations such as business development for Industrial Development Zones and strategy formulation. Analysis of studies which have previously been conducted on IDZs assisted in the evaluation of key success factors.

CHAPTER 4

4 PRESENTATION OF RESEARCH FINDINGS

4.1 INTRODUCTION

The research question for this study was aimed at determining the critical success factors for the operation of South African Industrial Development Zones. In the process of answering the question, a number of objectives were focused on. A study of the factors influencing the location of the Coega and Richards Bay IDZs along with identification of the types of industries currently operational there was done. To obtain insight into the best practices in other developing economies, critical success factors of development zones in Malaysia, Singapore and Mauritius was provided.

An analysis of historic and planned investments into the developments zones and source regions of the historic investing businesses was conducted in order to evaluate the performance of the zones. This research paper also focused on identifying ways of increasing the contribution of IDZs to the economic development of South Africa in alignment with the New Growth Path policy document.

4.2 COEGA AND RICHARDS BAY IDZs

4.2.1 COEGA IDZ

The IDZ received the designation in 2001 and is fully owned by the provincial government of the Eastern Cape through the Eastern Cape Development Corporation (ECDC) (the dti, 2012). The operating company for the zone is the Coega Development Corporation (Pty) Ltd. Construction of the first factories and warehouses in Coega commenced in a phased programme in the first quarter of 2005.

Coega is located close to Port Elizabeth which is one of the largest automotive manufacturing centres in Africa. The IDZ is also situated close to “reserves of platinum group metals, manganese and chrome ores, titanium minerals, alumino silicates and vanadium, which are required for new automotive technologies, including fuel cells, catalytic converters and lighter components" (CDC, 2005). The presence of an established railway network which connects the Coega IDZ with the main mining regions places the zone in a position of being able to access raw materials which can be used by companies located in the zone. The IDZ has a bulk terminal which has conveyor links to metallurgical clusters thus providing cost effective access to imported feedstock.

Another strategic advantage for the Coega IDZ is the construction of the new deep-water port of Ngqura by the National Ports Authority (NPA) of South Africa. The harbor is fully integrated into the Coega IDZ. Infrastructure is in place to allow direct offloading of ore from the harbor to processors in the Coega IDZ via a system of covered conveyors, and there are direct road and rail links between the IDZ and the port.

Coega was largely marketed as having a cost advantage of electrical power being among the least expensive in the world. On this basis the Canadian Alcan steel company had shown interest in being the anchor tenant at the IDZ. As the power utility Eskom became aware of the looming power shortages in the country, electricity pricing had to be adjusted and the initial cost advantage was done away with.

4.2.2 RICHARDS BAY IDZ (RBIDZ)

The IDZ received the designation in 2002 and is operated by the Richards Bay IDZ (Pty) Ltd company. The uMhlatuze District Municipality owns 40 percent of the company and the KwaZulu-Natal provincial government owns the remaining 60 percent stake. "Priority industrial sectors for the zone include aluminium, furniture, titanium, dry dock (ship repair) and the synthetic wood cluster" (the dti, 2012). The RBIDZ has four investment clusters which are aluminium, renewable energy, heavy metals and agro-processing.

RBIDZ only received its operator permit in November 2009, approximately 8 years after the granting of the industrial development zone designation. The main delay for the granting of the permit was due to the process of defining the different roles and responsibilities of the municipal, provincial and national governments in the zone.

According to the **dti,** at the end of the 2010/11 financial year the zone had received cumulative funding of R294.1 million from the dti and from the provincial government. Tata's R650 million ferrochrome smelter was the only onsite investor at the RBIDZ at the close of the 2010/11 financial year.

The RBIDZ offers a number of investment attraction factors such as the presence of one of South Africa's deepest ports, which is attractive for investors who might require large ships to dock close to the point of delivery or departure. Companies located in the IDZ are allowed to have 100% ownership of the business entity established in the zone, with no requirement for a local stake in the ownership of companies.

The zone has a dedicated electronic customs office which helps to ensure fast inspections and clearance of goods entering or leaving the zone. Presence of a customs controlled area offers investors ease when operating in the zone as there is a reduction in the administration which would have been faced for the investment process in other regions of the country.

4.3 PERFORMANCE OF THE COEGA IDZ

The Coega IDZ and the other zones in South Africa have generally been considered as not performing as anticipated. In order to evaluate this assertion, an analysis of the performance of the Coega IDZ was done which compared the targets set over the five year period 2006 to 2011 with the realised outcomes over this period. Coega started fully functioning in 2005, hence the use of the 2006 to 2011 period.

4.3.1 INVESTORS

One of the measures for evaluating the performance of Industrial Development Zones is the number of investors who set up their operations within the IDZ.

Table 4.1 Analysis of number of investors in the Coega IDZ

		2006/07	2007/08	2008/09	2009/10	2010/11
Investors	Number of investors per year					
	Target	10	6	8	4	4
	Actual	9	***7***	6	***4***	***5***

In three of the five years under review, the Coega IDZ did not manage to attract the number of targeted investors. At the end of the 2010/11 financial year, the IDZ had 12 onsite investors (the dti, 2012).

4.3.2 EMPLOYMENT

One of the main thrusts of the New Growth Path economic policy document is to have 20 million jobs created by 2020. The manufacturing sector is one of the major absorbers of labour and IDZs contribute to this creation of jobs.

Table 4.2 Employment figures for the Coega IDZ

		2006/07	2007/08	2008/09	2009/10	2010/11
Employment	Jobs per year					
	Target	2,960	4,800	4,030	5,798	6,107
	Actual	***3,880***	***5,748***	***7,223***	***7,681***	4,153

The cumulative number of jobs which have been created over the analysed period is 28,685. Given the zone has not yet reached its maximum potential, it is expected that Coega will be able to add more jobs to the tally as more investors are established. When companies establish their operations there is a multiplier effect which results in development of other activities contributing to increased labour absorption.

4.3.3 PROFITABILITY

For any business entity to be considered as being viable, it needs to be able to meet the targets set out for it. One of the main gauges of a business' performance is the profitability of the business entity.

Table 4.3 Review of Coega IDZ revenue generation

		2006/07	**2007/08**	**2008/09**	**2009/10**	**2010/11**
Profitability	Revenue Generated (R m)					
	Target	45.0	30.4	41.23	48.03	94.7
	Actual	42.2	***41.6***	***55.04***	***61.14***	***114.5***

Coega has managed to surpass the revenue targets set over the review period expect for 2006/07. Growth in the number of investors is expected to result in an increased revenue base for the Coega Development Corporation (Pty) Ltd.

4.4 FOREIGN DIRECT INVESTMENT ANALYSIS

In order to contextualise the investment flows into the South African Industrial Development Zones, an analysis of the foreign direct investment (FDI) into the country was done.

Just after the end of apartheid with the economic sanctions which South Africa had been subjected to being lifted by the international community, FDI inflows into the country in 1995 were R62 million. The inflows have been growing ever since the country opened up for business. Although a lot of investment flows into the country, most of the recorded FDI flows have been concentrated in the form of portfolio investments and not investment in physical manufacturing infrastructure.

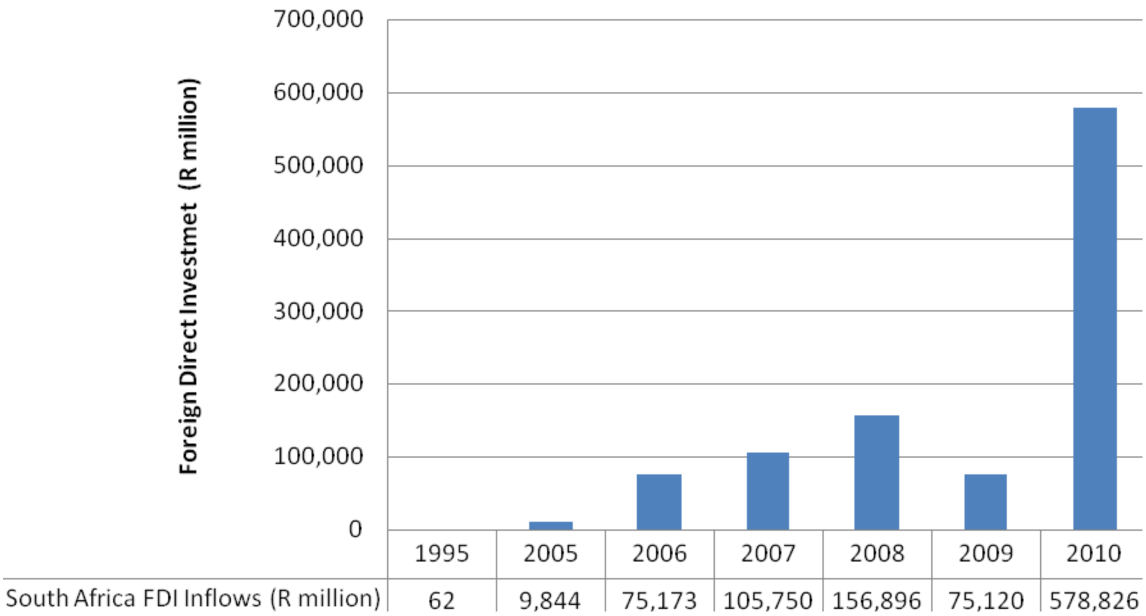

Figure 4.1 South Africa FDI Analysis

NB An average exchange rate of R7.5: $1 was used for the graph

South Africa constitutes a significant share of the FDI destinations on the African continent. Over the period 2005 to 2009, the country experienced a rise in the FDI until 2008. The setting in of the economic downturn led to a slowdown in the global investment flows. FDI inflows to Africa fell by 19 percent between 2008 and 2009 while the inflows to South Africa fell by 52 percent. Whenever there are global economic concerns, the South Africa economy is negatively impacted by the sentiment of the perceived risk of having investments in developing economies. The large drop in the FDI from 2008 to 2009 is due to investors withdrawing their portfolio investments from the country.

Table 4.4 South African and Africa FDI inflows analysis

	2005	2006	2007	2008	2009
South Africa FDI Inflows ($ millions)	1,312	10,023	14,100	20,920	10,016
Africa FDI Inflows ($ millions)	38,197	55,382	63,092	72,178	58,563
SA/Africa	**3.4%**	**18.1%**	**22.3%**	**29.0%**	**17.1%**

Although the Industrial Development Zones aim on attracting a number of investors into the country, a number of global economic forces have a large bearing on investor sentiment.

Another factor to take into consideration with regards to the attractiveness of locating operations in the South African Industrial Development Zones is the proximity to the global markets. South Africa's geographic location places the country at somewhat a disadvantage compared to other developing countries such as Mauritius, Singapore and Thailand which are closer to the major world markets.

Table 4.5 Africa's share of global FDI flows

Year	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Africa ($ millions)	9,829	19,995	16,074	20,418	21,726	38,197	55,382	63,092	72,178	58,563
Share of World's Total FDI	0.70%	2.42%	2.56%	3.61%	2.97%	3.87%	3.80%	3.0%	4.08%	5.24%

Foreign direct investment flows to Africa constitute less than 5.5 percent of the global FDI flows. The share of the global FDI which has been flowing to Africa has been steadily rising over the past decade. A gradual shift toward local beneficiation of resources in African countries is expected to result in an increase in the level of investment in the continent's manufacturing base.

South Africa's second Industrial Policy Action Plan (IPAP2) points toward increased beneficiation of minerals and other resources. Investors seeking to tap into the country's resource base are expected to take the opportunities of locating in the Industrial Development Zones in the country as time progresses.

4.5 RESEARCH FINDINGS FOR IDZ CRITICAL SUCCESS FACTORS

As outlined in the research methodology section, research interviews helped in identifying the key success factors of industrial development zones in South Africa. Case studies of other development zones in Thailand, Malaysia and Mauritius which were provided in the literature review section of the research report provide insight into critical success factors which IDZ frameworks should have.

Respondents outlined four main areas which need to be strengthened in order for the IDZ program to yield better results.

4.5.1 Ownership

The existing Industrial Development Zones are currently mainly owned by government whether municipal, provincial or national. Although a special purpose vehicle with its own board of directors is constituted for the different IDZs, strategic investment decisions might end up not being based on commercial imperatives but on political imperatives.

Richard's Bay IDZ received the designation to be an IDZ in 2002 but only received the operator permit close to the end of 2009. The reason which was cited for the delay in issuance of the permit was the need for delimitation of the functions of the local, provincial and national governments in the running of the IDZ.

Lack of clarity and co-operation between the three levels of government has potential to have tremendous impact on the viability of IDZs, as seen by the approximately 8 year delay in the issuance of a permit. In this period some investors might have already started operations and would have started contributing to economic growth and job creation. There is need to ensure investors are not driven away due to delays in the adjudication process for their investments emanating from lack of adequate coordination amongst the principals.

4.5.2 Labour

International best practice with regards to labour in development zones points to more flexible terms and conditions for dealing with the labour employed in the zones. The South African labour is highly unionised and there is no flexibility which is afforded the companies seeking to be located their operations in the zones.

Respondents to the survey pointed out to the need for a more flexible labour regulatory environment. One of the problems which were highlighted was the shortage of some skills within the country and the lack of flexibility in the employment of foreign labour.

South Africa currently has Sector Education Training Authorities (SETAs) such as the Chemical SETA where people are trained and receive certification in particular job areas. These SETAs are expected to assist in the equipping of artisans and other trades in order to prevent the need to import skills into the Industrial Development Zones.

4.5.3 Incentives

A major problem which was outlined by respondents which South African IDZs currently face is the lack of specifically targeted incentives. There are a number of manufacturing incentives which are available for companies operating in South Africa which are offered by the Department of Trade and Industry. Investors into the IDZs are able to access all the manufacturing related incentives which they qualify for.

International best practice dictates the need for incentives which are specifically designed for the IDZs. The South African government need to establish incentives which will make local IDZs competitive in relation to zones in other regions.

4.5.4 Marketing

Industrial Development Zones have different focus areas which are able to be marketed in order to attract investors. The different zones need to have a focused approach with regards to the type of industries they would like to have established in the zones. Having an area of specialisation helps zones form a Unique Selling Proposition (USP) which can be used to stimulate interest for investors.

South Africa’s IDZs have currently been marketing themselves in an independent manner instead of on a collaborative basis. The lack of a coordinated approach to marketing of the zones results in zones competing with each other rather than leveraging each other’s strengths. Inadequate or unclear definition of the roles and responsibilities of the three tiers of government in the operation of IDZs plays a major role in fragmented marketing of the zones.

Respondents recommended the need for increased co-operation between the three government tiers. When the goals and objectives of the local and provincial governments fit in with the overall aims of the national government, it is anticipated that IDZs will be able to attract investors more easily.

4.6 CONCLUSION

The Industrial Development Zones concept in South Africa has had mixed outcomes. Comparison of the amount of money which has been invested into the establishment of the IDZs with the realised returns has not yet been satisfactory. Although the government has been criticised for the large capital outlays, it might be too early to discard the zones and render them a completely ineffective.

A supportive policy environment is expected to be beneficial to development zones going forward. The second Industrial Policy Action Plan (IPAP) 2 outlines governments aim to increase value addition and mineral beneficiation. Industrial Development Zones are expected to play a major role in harnessing investors who will be focused on value added manufacturing. With the global changes in the economic landscape, the development zones stand a chance of attracting investments as investors seek to be closer to raw material sources as competition for resources rises.

Provision of clear targeted incentives for companies to establish in the development zones is expected to go a long way in attracting investors into South Africa. Proper definition of the roles and responsibilities of the three tiers of government is expected to minimise the bureaucratic red tape faced by potential investors in the IDZs. Establishment of a common ground between the trade unions, government and business is expected to assist in making labour legislation more flexible. Greater flexibility pertaining to labour in the IDZs will act as major pull factor for investors. IDZs in South Africa need to have a co-ordinated approach with regards to marketing their offerings to investors.

CHAPTER 5

5 CONCLUSIONS AND RECOMMENDATIONS

5.1 INTRODUCTION

Industrial Development Zones have been used in different parts of the world with the aim of stimulating economic growth through export oriented industries. South Africa's IDZ Program aims at promoting the same objective, with focus being on establishing the zones in areas with access to a seaport or international airport.

5.2 RESEARCH PROBLEM

South Africa's Industrial Development Zones (IDZs) program is slightly more than a decade and was formulated on the basis of aiming at stimulating economic growth in areas which normally do not attract investment. Although there are currently four designated IDZs, there have been a number of varying reviews regarding the effectiveness of the zones in stimulating economic growth and growing employment.

The study was initiated with the aim of evaluating the existing Industrial Development Zones framework in the South African economy. Research into the critical success factors of different zones in other regions was conducted in order to establish international best practices. These practices can then be incorporated into the existing IDZ framework in order to make it more competitive.

5.3 LITERATURE STUDY

The second chapter gave a comprehensive literature review which drew upon prior studies focused on development zones such as Industrial Development Zones, Special Economic Zones and export processing zones.

Case studies of development zones in Mauritius, Malaysia and Thailand provided insight into best practices in the operation of the zones in other developing countries. Critical success factors such as the need for adequate financial and policy incentives, proper marketing and provision of support services were noted in the case studies.

The literature study also provided an analysis of the major policy documents which have a bearing on economic growth in the country. South Africa's New Growth Path focuses on economic growth and employment creation as the two main focuses of the government. Industrial Development Zones are expected to contribute to the government's imperative.

General manufacturing incentives which are offered by the South African Department of Trade and Industry were also examined in the literature review. The main incentive for companies locating operations in IDZs is the 12i tax incentive. This incentive aims at "stimulating investment in large industrial projects by providing an investment allowance of either 35 or 55 percent of the cost of qualifying investment assets" (Erasmus, 2011).

5.4 CONCLUSIONS AND RECOMMENDATIONS

The South African IDZ program in its current form has been noted to fall short in terms of making the country an attractive investment destination. Lack of a clear consolidated marketing plan for the existing IDZs results in each zone searching for investors on the zones own merits, rather than as a collective. In order to grow the reach and appeal of the country, South African IDZs need to have a collaborative approach in order to enhance the marketing of the country.

Economic development in South Africa is mainly focused on ensuring economic growth and also employment creation. In order to ensure sustainable economic development in the face of globalisation, the South African government needs to foster a favourable environment for investors.

Development zones in different countries around the world aim on having key selling points which will attract investors to these zones. South Africa's present Industrial Development Zones have not been able to market themselves as having Unique Selling Propositions (USP) differentiating with other global zones. This has led to lower than anticipated investment inflows into these zones.

Restructuring of South Africa's IDZs needs to be done in order to ensure each zone has a clear USP which will attract investors into the zone. Current plans for the Saldanha Bay IDZ points toward creation of different clusters within the zone which will be specialised and focused on specific activities such as marine repairs and offshore supply base activities.

Lack of specific incentives which are targeted at IDZs has led to South Africa's zones being less competitive in relation to those in other regions of the world. Incentives which have been available to investors in South African IDZs are the same as those being accessed by other manufacturing companies' investing in other parts of the country.

The only differentiator for companies investing in the zone and those in the rest of the country has been the 'one-stop shop' advantage of the IDZs, where all the incentives can be accessed in one place. South Africa needs to formulate incentives which are able to stimulate interest in the zones.

Apart from tax incentives, a major area which needs to be addressed pertains to labour flexibility. Other IDZs in developing countries have been able to make their zones attractive by having non-unionised labour. This is a contentious issue in South Africa as the main trade unions are sceptical about any suggestions for changes to the existing labour frameworks. Government's aim to create employment through establishment of zones has the potential of being hindered due to the inflexibility of labour laws in the country. A deliberate collaborative approach between the tripartite parties (government, business and labour) with buy-in from the three parties is expected to provide opportunities for increased marketability of the country as a worthwhile investment destination.

Although it is difficult for labour in IDZs to be made to work differently from other workers in the country, the government can change the tax regime for companies employing labour in the zones. As an example, certain contributions which are normally done such as the Unemployment Insurance Fund (UIF) can be waived or lowered. Companies which are able to demonstrate how they will ensure skills transfers can receive special credits which can count toward reduction in the amount of effective tax they will have to pay.

Efficient operations of existing IDZs has been noted to be hindered in some instances due to the overlapping and often conflicting mandates of the three spheres of government, *viz,* national, provincial and local. Differences in terms of national policies and local policies in the country can arise due to different political parties being in charge whose development imperatives and strategies are different. Lack of congruency in mandates has potential to inhibit the potential growth of different provinces. There is need for the relationships between the different spheres of government to be well coordinated by aligning the objectives set out in the mandates of the spheres.

Management of IDZs has to be done with a proper strategic focus to ensure the zones function effectively in attracting investors and ensuring sustainable operation of the zones. Rather than trying to appeal to all types of investors, a focused approach by IDZs in areas of a comparative advantage will enable a better investment destination promotion.

5.5 RECOMMENDATIONS FOR FURTHER STUDY

The South African Department of Trade and Industry gazetted the Special Economic Zones (SEZ) Bill in January 2012. Under this Bill, Industrial Development Zones will be classified as a type of SEZs which will be used to stimulate development within the South African economy. Given the existence of IDZs such as Coega and Richards Bay, it would be of interest for a comparative study to be made between the performances of these zones under the IDZs regime versus the SEZ regime.

The Saldanha Bay Municipality is in the process of applying for the designation of an IDZ. A study can be done to analyse the application process and to also evaluate the zone’s performance in the event that the zone receives the designation.

Another recommended area for further study has to do with how to differentiate South African SEZs from those located in other countries, in order to be more competitive.

6 APPENDICES

6.1 RECONFIGURATION OF IDZs INTO SPECIAL ECONOMIC ZONES

The draft Special Economic Zones (SEZs) bill which was gazetted for public comment on 23 January 2012 (after this research report had been finalised) outlines adjustments which have been made to the IDZ Program. “Special Economic Zones are geographically designated areas of a country set aside for specifically targetted economic activities which are then supported through special arrangements (which may include laws) and support systems that are often different from those that apply in the rest of the country” (the dti, 2012).

IDZs will now be classified as being part of Special Economic Zones under the SEZs bill. Under the IDZ program, regions only qualified to be designated as IDZs if the area to be designated was either adjacent to a seaport or international airport. SEZs are expected to stimulate investment in other parts of the country which previously did not benefit from the IDZ program.

6.2 QUESTIONNAIRE

Evaluation of Critical Success Factors for South African Industrial Development Zones

Respondent's Name	
Job Title	
Telephone number	
Email address	

1. Please provide insights into your understanding of how companies perceive the South African IDZs. *i.e. are they aware of the following services or offerings within the zone, are they interested in investing etc. Please also provide a rating for the perceptions of the outlined factors (Good, Average or Inadequate)*

Investor Perceptions on	**Overview/description of perceptions**	**Good**	**Average**	**Inadequate**
Infrastructure				
Geographic location				
Labour provision				
Local supporting industry				
Intellectual property support				
Marketing				
Management of the IDZ				
Enabling incentive environment				
Others (please specify)				

2. Please indicate the main catalysts for initial investment in the Coega or Richards Bay IDZ (i.e. what attracted the first five companies to invest in the IDZ- please specify which IDZ)

3. What are the main location factors determining the types of companies investing in the Coega or Richards Bay IDZ?

4. Has the Coega or Richards Bay IDZ been able to meet the objectives set for the zone at its initiation? If yes what factors have enabled this, if not- what factors has hindered achievement of these objectives?

5. Can you provide insight into the long-term plans for the continuous successful operation of the Coega or Richards Bay IDZ?

6. Could you please outline ways of increasing the contribution of IDZs to the economic development of South Africa in alignment with the New Growth Path policy document

7. Are there any other insights which you can provide on the IDZs in South Africa (which haven't been addressed above)

Thank you very much for your time and insights

6.3 SUMMARY OF RESPONSES

Responses to the questions posed in the questionnaire were answered in reference to the South African IDZ framework and specific responses were for the Coega and Richards Bay IDZs.

Question 1

Investor Perceptions on	Overview/description of perceptions	Good	Average	Inadequate
Infrastructure	Inconsistent between different IDZs but overall good	X		
Geographic location	South African IDZs to far removed from other IDZs		X	
Labour provision	High costs, low productivity			X
Local supporting industry	In need of further development		X	
Intellectual property support	Development agencies such as Industrial Development Corporation (IDC) and Technology Innovation Agency (TIA) assisting. There is need for more work to be done to make support more robust		X	
Marketing	There is need for enhancement of the marketing of IDZs- a clear strategy and investor marketing guide		X	
Management of the IDZs	Management of the zones has not been able to perform up to expectations			X
Enabling incentive environment	There is need for more incentives such as establishment of			X

	zones as tax-free zones in order to overcome the labour and geographic challenge			
Others (please specify)	South Africa needs to establish a clear proposition and clear point of difference in order to be competitive relative to other zones			

Question 2

Please indicate the main catalysts for initial investment in the Coega or Richards Bay IDZ (i.e. what attracted the first five companies to invest in the IDZ- please specify which IDZ).
Port infrastructure
Infrastructure

Question 3

What are the main location factors determining the types of companies investing in the Coega or Richards Bay IDZ?
Port Infrastructure
Proximity to raw materials
Established rail infrastructure

Question 4

Has the Coega or Richards Bay IDZ been able to meet the objectives set for the zone at its initiation? If yes what factors have enabled this, if not- what factors has hindered achievement of these objectives?
General response was the IDZs have not been able to meet their objectives
the lack of clarity of purpose and direction was given as the main reason
there is need for a clear proposition for the IDZs

Question 5

Can you provide insight into the long-term plans for the continuous successful operation of the Coega or Richards Bay IDZ?
There is need for a clear strategy and investor marketing guide
Appealing incentives must be provided in order for investors to be attracted
An end to end value chain approach should be adopted by IDZs in order to have interlinked industries located in the zone

Question 6

Could you please outline ways of increasing the contribution of IDZs to the economic development of South Africa in alignment with the New Growth Path policy document
South African industry should focus on the country’s strengths
attractive incentives should be provided
value addition should be integrated in the process
ownership of the IDZs should be rationalised to avoid bottlenecks in the system
labour flexibility should be present within the IDZs

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