


Employment-oriented Industry Studies

KwaZulu-Natal Economic Review

Project Leader:
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HSRC Human Sciences Research Council

employment growth & development initiative
innovative employment strategies

KWAZULU-NATAL ECONOMIC REVIEW

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EXECUTIVE SUMMARY

Background and introduction

The Employment and Economic Policy Research division of the HSRC was appointed by KwaZulu-Natal's (KZN's) Department of Economic Development and Tourism in September 2002 to undertake an economic review of the KZN province with a view towards establishing a provincial industrial strategy.

The terms of reference are to provide a review of the KZN economy, in terms of the following key themes:

- Growth in traditional and non-traditional primary, secondary and tertiary sectors;
- Changes in industrial structure, within and between industries;
- The contribution of nodal developments;
- Firm access to new opportunities such as beneficial trade arrangements (e.g. AGOA);
- Trends in labour absorption within the province;
- Human resource development and take-up of Skills Development Strategy;
- Impact of HIV/Aids on the KZN economy; and
- The contribution of public institutions in KZN in promoting economic development.

With the exception of beneficial trade arrangements, which is the subject of a separate study commissioned by the DEDT and hence was not analysed here in order to avoid duplication, all these themes are addressed in this report.

Following the submission of the phase 1 report, at the request of the DEDT, the HSRC expanded the terms of reference to include:

- The informal sector;
- Small, micro and medium enterprises; and
- Black economic empowerment.

The review comprises 6 main sections. Appendix A, which provides an analysis of industrial policy in the post-1994 period, section 1 (Background and Introduction), section 2 (The KZN economy), section 3 (Labour Markets in KZN: Labour Absorption, Human Resource Development and HIV/Aids), section 4 (The Role of Provincial Government in Economic Development) and Section 5 (Future Growth Prospects for KZN: Challenges and Opportunities).

In order to set the national context for the analysis of the KZN economy, appendix A provides an analysis of industrial policy in the post-1994 period. It has been relegated to the appendix by virtue of its status as a context-setting analytical tool.

In relation to industrial policy, the following key elements of the 1994 regime are pertinent to the performance of the KZN economy:

- South Africa's industrial development trajectory has historically been driven by import-substitution. Many of KZN's manufacturing enterprises were created behind the high tariff barriers that characterise such a development path.
- As a minerals economy, South Africa's future development trajectory is constrained by path dependence. The cost structures associated with a minerals economy rule out the development of labour-intensive export capacity in the manufacturing sector. This limits the options available to KZN in order to alleviate its high and growing rate of unemployment.
- Rapid tariff liberalisation in the post-1994 period has induced structural changes in the manufacturing sector. Such changes have resulted in the contraction of exports from labour-intensive sectors and their expansion in skills, technology and capital-intensive sectors.
- While tariff liberalisation has been far-reaching, anti-export bias remains. This may well inhibit the expansion of exports from sectors located in KZN.
- The buoyant growth of exports has been accompanied by a decline in employment, particularly in the manufacturing sector.
- A range of supply-side measures has been put in place in the post-1994 period to replace demand-side policies. They include incentives to encourage inward investment, competitiveness, innovation, the development of the SMME sector and black economic empowerment. Facilitating access to these incentives is a powerful way to promote industrial development in KZN.
- Measures to promote the SMME sector have been unsuccessful as evidenced by the low survival rate of such enterprises and the miniscule proportion of firm that actually utilise these measures.
- Black Economic Empowerment has similarly failed to foster black ownership of assets at a scale of any significance.
- The only measures created to address the spatial location of industry are spatial development initiatives (SDIs) and Industrial Development Zones (IDZs). They constitute important policy instruments for provincial-level industrial development.
- The restructuring of state-owned enterprises has not commenced at the anticipated pace. The inefficiencies of state-owned enterprises in the transport and communications sectors continue to undermine South Africa's competitiveness. Notwithstanding initiatives to fast track the concessioning of the Durban Container Terminal to a private operator, the decision to suspend further restructuring until after the 1994 elections will continue to act as a constraint to competitiveness.

- Recent policy initiatives – in the form of the microeconomic reform strategy and associated integrated manufacturing strategy – propose to follow a knowledge, capital and technology intensive development path. Such a development path appears unattainable in the context of a labour force that is predominantly semi-skilled and unskilled.

This national context both explains the structural changes that are emerging within the KZN economy and creates the parameters within which a provincial-level industrial strategy can be framed.

The KZN economy

The KZN economy is home to 21% of South Africa's population but contributes a mere 15% to its GDP. It is the fourth poorest province in South Africa with a GGP per capita of R9,713. This is just over a third of Gauteng's per capita GGP and less than half of that of the Western Cape. Despite its relatively weak position, KZN has been the fastest growing province during the 1995 to 2000 period, with an annual average growth rate of 4.3%.

The structure of KZN's economy differs from the structure of the national economy in that it has a much larger manufacturing sector (25% of GGP compared to 19% of GDP for SA) and a mining sector that is one-sixth of the size of its national contribution to GGP (1% for KZN, compared to 6% for SA). In addition, KZN's transport and communications sector is larger than at the national level (15% for KZN, compared to 10% for SA), as is the agriculture and forestry sector (4% for KZN, compared to 3% for SA).

Between 1995 and 2001 signs of structural change in the KZN economy began to emerge. They took the form of a reduction in the contribution of the primary and secondary sectors and an increase in the contribution of the tertiary sector to GDP. Despite these structural shifts, KZN retained a production base characterised by a much smaller primary sector (just over one-quarter) and a much larger (more than double) secondary sector than the national average.

Growth rates in excess of the national average have been driven by high growth in the services sector, in particular, financial and business services and transport and communication. The latter is explained by the growth of logistics services, in a context of a significant expansion in both exports and imports.

In the manufacturing sector, growth has been driven by three industries: paper and paper products, ferro-alloys (i.e. aluminium) and other chemicals (i.e. petroleum). Sectors of less significance (in terms of their contribution to GGP) that have experienced growth include: motor vehicles and parts, printing & publishing, beverages, non-electrical machinery, iron & steel and wood furniture.

Declining industries that are important to the KZN economy include food & food products and textile. Although the quantitative data indicated a contraction in the clothing sector, qualitative analysis revealed that it is growing in a context of casualisation, informalisation and outsourcing. Less significant industries (in terms of scale) that have experienced decline include fabricated metal products, footwear, plastic products, leather & leather products, rubber products, electrical machinery and transport equipment.

These structural changes have been induced by the exposure to global competition brought about by trade liberalisation. They are positive insofar as they signal the positioning of the KZN economy within the global arena. Moreover, despite the decline of some industries, the manufacturing sector has been growing in aggregate, suggesting that deindustrialisation has not taken place.

As regards investment, the proportion of national investment flowing to KZN is commensurate with its contribution to South Africa's GDP and accounted for 15% of aggregate national investment in the 1995 to 2001 period. It flowed to the high growth sectors. The scale of investment in KZN is, however, insufficient to drive higher growth rates.

In terms of the spatial distribution of economic activity, as is the case in the broader South African economy, in KZN economic activity is concentrated in three centres: Durban, Pietermaritzburg and Richards Bay. In the long term, policy-makers may wish to see a more equitable distribution of economic activity across space.

In terms of nodal developments, the following initiatives are currently at various stages of implementation in KZN:

- The Lubombo SDI;
- The Richards Bay SDI;
- The Pietermaritzburg-Msunduzi SDI;
- The Dube Trade Port IDZ; and
- The Richards Bay IDZ.

Responsibility for the implementation of the SDIs has recently been transferred from national to provincial and local governments. In the case of IDZs, their designation and creation is the responsibility of provincial and local government. Consequently, SDIs and IDZs are central policy instruments of the KZN government for promoting nodal developments.

Initiatives to restructure the Port of Durban will unlock a range of opportunities for economic development. While measures to enhance its capacity will increase the volume of cargo flowing through the port, the concessioning of the Port of Durban to a private operator will act as a catalyst for the development of 'back of port' manufacturing capacity.

The imperatives of BEE and SMME development loom large in KZN. While the framework within which they will be promoted is set by national government, the DEDT has an important role in facilitating the entry of such firms into the provincial economy. The impact of policy measures that are currently in place to achieve this must regularly be evaluated.

As regards the informal sector, while it is a significant source of employment in KZN, its activities are concentrated in the low-productivity, low-wage end of the economy. The imperative is therefore to facilitate the movement of its participants up the value chain in order to increase their income and contribution to the economy.

The KZN labour market: employment, human resource development and HIV/Aids

The structural weaknesses of the KZN economy come to the fore in this section. The province has the highest unemployment rate in South Africa and a high prevalence of HIV/Aids. Moreover, skill formation is slow and tertiary education institutions appear to be unresponsive to the demand for skills emanating from growth sectors within the KZN economy.

Labour absorption

South Africa's high and growing unemployment problem is the most important economic challenge currently facing policy-makers as it poses a certain brake on long-term growth and human development. Within this context, KZN has significantly higher levels of unemployment than the national average, in terms of both the strict (33%, compared to a national average of 29%) and expanded (46%, compared to a national average of 41%) definition of unemployment. The latter definition includes discouraged workers. KZN accounts for 17.9% of employment in South Africa. This is disproportionate to the province's share of the country's population, which is 21%.

This amounts to in excess of 1.6 million unemployed people for whom jobs must be created. In fact, entrants to the labour market (net of those who exit) averaged 155 000 per annum during the 1996 to 2001 period, in terms of the expanded definition of unemployment. This means that merely to maintain the status quo of a 45% unemployment rate, 150,000 jobs have to be created each year. To make any inroads into the unemployment rate, far more than 150,000 jobs must be created.

KZN's unemployment problem is exacerbated by the structural shifts that are emerging within the economy. As is the case in the national economy, as a consequence of trade liberalisation labour-intensive industries (for example, clothing and footwear) are declining, while capital, technology and skills intensive industries and sectors are expanding. In such a context, unemployment among the semi-skilled and unskilled mushrooms, while the economy's ability to grow is constrained by skill shortages.

Strategies to create employment should be guided by the reality that the potential for mass employment expansion in South Africa through labour intensive exports is quite limited. The most likely avenue for creating more employment is by increasing effective domestic demand for more employment-absorbing, low labour productivity non-traded goods and services. 'Non-traded' is distinct from non-tradable: most goods and services can practically be traded, but some are more oriented toward the local market, such as construction, or social services.

In the context of a relatively small productive base, and a large un- and under-productive sector, the balance between high productivity, income generating sides of the economy and sustainable transfers to socially useful lower productivity activities is quite critical, particularly if sustained for a lengthy period of say 10 to 15 years. Over this period, it is expected that the higher value sectors would expand, and that net new entry to the labour force would diminish due to falling birth rates and to HIV/Aids.

Human resource development

In terms of human resource development, its centrality in broader economic development strategies has become imperative in a context of globalisation where skills rather than the resource base of regions determine their competitiveness. As is the case in the broader South Africa, KZN has a small proportion of skilled workers within its labour force, as evidenced by the fact that 14.5% have tertiary qualifications, while 28.5% have completed matric.

The relationship between educational attainment and employment in KZN is highlighted by the fact that a high proportion of people with post matric qualifications (83.2%) are employed. Of those with *matric more than half (57.3%) are employed. In contrast, 52% of people with less than matric and 45.7% with no education at all are unemployed in KZN.*

Of concern is the fact that of the 96 423 candidates who sat for the matric examination certificate in 2000 only 57% passed. This is a significant decline from the pass rate of 68% attained in 1994. Moreover, the number of university exemptions granted to candidates that passed matric has also declined by 10 percentage points, from 26% in 1994 to 16% in 2000. This suggests that the supply of skilled labour is declining in a context where demand is growing rapidly.

While KZN has the highest proportion of tertiary education institutions, it has the lowest participation rates. Moreover, these institutions appear to be operating in isolation from the patterns of skill demand emerging from growing sectors and industries within the KZN economy. The alignment of the supply and demand for skill is therefore an imperative of industrial policy.

The take-up of the national skills development strategy within KZN represents an important instrument for rapid skill formation. The programme for the unemployed has been well supported in KZN. Secondary information was not, however, available to analyse the take-up of this strategy for employed workers under the auspices of the SETAs.

HIV/Aids

From the perspective of labour markets, while the HIV/Aids epidemic will not only reduce unemployment it will also negatively impact on productivity as workers become symptomatic and will add to skill shortages when skilled workers afflicted by HIV/Aids exit the labour force. Of course, it will also reduce the unemployment problem.

While the treatment of affected people remains the responsibility of the KZN Department of Health, the DEDT must be cognisant of its negative economic impact and develop a strategic framework for mitigating such impacts. In addition, prevalence of HIV/Aids in KZN will create a growing demand for health services, which will provide an avenue for employment creation.

The role of provincial government in economic development

The survey of international literature, analysis of the role and functions of the three tiers of government in South Africa and examination of the institutions tasked with promoting economic development in KZN, provides a framework within which economic development can most effectively be promoted in KZN.

The international literature highlights the shift from central determination of regional policy to the decentralisation of decision-making with respect to local and regional development. This development has been underpinned by the devolution of power to provincial and local governments and fiscal decentralisation. Consequently, a development model in which provincial and local governments wield greater discretion over infrastructure provision and economic development incentives is currently in vogue the world over.

In terms of the interventions made by provincial-level institutions, the creation of clusters (in order to realise agglomeration economies) and investment promotion are the most commonly utilised instruments across the world. Harnessing agglomeration economies in order to reduce costs and enhance the competitiveness of particular industries is deemed to fall within the realm of provincial government because decentralised policy may be more efficient in determining industrial location, as it is difficult for central government to gauge scale and agglomeration economies and diseconomies in specific regions.

In terms of investment promotion, the decentralisation of the role of the state in economic development to second and third tier government has been accompanied by increasingly higher levels of competition among provinces and localities for investment. Hence the promotion of inward investment has become a key policy objective of provincial governments the world over. From a policy perspective, the determinants of the attractiveness of a location may conceptually be divided into four areas: public capital, factor markets, social factors and governance factors. Provincial governments should endeavour to influence the factors over which they hold sway in order to maximise investment flows to their regions.

In South Africa, the devolution of power from national to provincial government in the post-1994 period has been significant, as evidenced by larger proportions of the national budget being allocated to second tier government. As regards economic development, central government sets the parameters within which provincial and local strategies are framed.

In terms of promoting regional economic development, provincial governments have concurrent legislative and executive power with national government over matters such as agriculture, public transport, tourism, urban and rural development and trade and industrial promotion. In practice, their knowledge of the provincial economy places them in a strong position to provide strategic direction to its development in cooperation with national and local government.

In the case of industrial policy, national government's powers to alter customs duties (within the framework of the regulations of the World Trade Organisation) and design and administer supply-side measures means that the DTI effectively determines the parameters within which growth and development takes place. The translation of national-level industrial policy into concrete developments on the ground is, however, driven by provincial and local governments (especially those of the scale of Durban and Richards Bay).

The relatively recent devolution of power in South Africa away from the centre and towards the second and third tiers of government has meant that the institutional framework for cooperation between the three tiers is not well developed and the relevant role of each tier is not well understood. This represents a major challenge with respect to the implementation of a provincial industrial strategy.

A number of key institutions – including the DEDT, Ithala, Trade & Investment KZN (TIK), Tourism KZN and the Dube Trade Port Special Purpose Vehicle - are tasked with promoting economic development in the KZN province. Their powers and functions and the mechanisms at their disposal to execute their respective mandates represent the instruments for achieving KZN's economic development objectives.

The successful implementation of a provincial industrial strategy that prioritises employment creation and skill formation, while being cognisant of the deleterious economic impact of HIV/Aids, is dependent on the efficacy of the instruments utilised in its implementation. The range of instruments at the disposal of provincial government is spread over many institutions, including national and local government.

In addition to the provincial-level institutions identified above, the resources and programmes of the DTI, IDC, DBSA and National Treasury will play an important role in promoting industrial expansion in KZN. Hence a key challenge is to mobilise the resources of these institutions in support of KZN's industrial strategy.

The overarching priority for DEDT is to develop a detailed policy framework for the province's economic development that prioritises particular sectors and geographic areas. This will focus the resources and programmes of the public entities that are mandated by DEDT on defined outcomes. The absence of an overarching policy framework is clearly inimical to sustainable economic development.

Future economic prospects for KZN: challenges and opportunities

KZN is the most populous province in South Africa, with the highest level of unemployment and the most severe incidence of HIV/Aids. Moreover, it has a disproportionately high share of South Africa's manufacturing sector and is home to the most important logistics platform for South Africa's trade. The province's economic fortunes will therefore clearly have a significant impact on the broader South African economy.

The key opportunities within the provincial economy include:

- The buoyant growth of a number of industries in the secondary and tertiary sectors in a context of trade liberalisation, suggests that they have made the necessary adjustments to their cost structures to become players in the global arena;
- Initiatives currently underway to restructure South Africa's port system, and the decision to fast-track the process of concessioning the Durban Container Terminal will increase the volume of cargo flowing through the port and act as a catalyst for the development of 'back of port' manufacturing capacity;
- The three spatial development initiatives (Lubombo, Richards Bay and Pietermaritzburg-Msunduzi) and two industrial development zones (Richards Bay and Dube Trade Port) present an opportunity to greatly enhance the growth rate of the provincial economy, while at the same time enhancing its ability within the global economy; and
- In a context where the skill of the labour force is becoming a more important determinant of competitiveness than resource endowments, KZN has significant institutional capacity to develop a skilled labour force.

The following challenges currently confront provincial policy-makers:

- The highest rate of unemployment in South Africa, in a context where structural changes in the economy are creating a contraction in labour-intensive sectors and an expansion in skill, capital and technology intensive sectors;
- Tertiary education institutions that remain unresponsive to the demand for skills emanating from industry;
- A decline in skills formation as evidenced by a decline in the matric pass rate and number of university exemptions attained;
- The high incidence of HIV/Aids. From the perspective of labour markets, while it will reduce unemployment it will also negatively impact on productivity as workers become symptomatic and will add to skill shortages when skilled workers afflicted by HIV/Aids exit the labour force;

- In the context of structural in response to trade liberalisation, the decline of food & food products, textiles, clothing, fabricated metal products, footwear, plastic products, leather & leather products, rubber products, electrical machinery and transport equipment;
- The need to develop the economic logic underpinning the Dube Trade Port more clearly, particularly the identification of industrial clusters to populate it;
- Developing an overarching economic development policy to focus the efforts of the public entities mandated by DEDT; and
- Building functional relationships with national government in order to effectively drive KZN's economic development agenda.

MAIN REPORT

1. Background and introduction

The Employment and Economic Policy Research division of the HSRC was appointed by KZN's Department of Economic Development and Tourism in September 2002 to undertake an economic review of the KZN province with a view towards establishing a provincial industrial strategy.

The review comprised two phases:

- A summary briefing document, based on secondary information, completed in November 2002, which included:
  - A presentation of broad trends;
  - Availability and quality of accessed information; and
  - The approach towards producing a more in-depth review.
- A more in-depth economic review in the form of an annual report.

This report is the deliverable of the second phase of the economic review. The terms of reference was to provide a review of the KZN economy, in terms of the following key themes:

- Growth in traditional and non-traditional primary, secondary and tertiary sectors;
- Changes in industrial structure, within and between industries;
- The contribution of nodal developments;
- Firm access to new opportunities such as beneficial trade arrangements (e.g. AGOA);
- Trends in labour absorption within the province;
- Human resource development and take-up of the national skills development strategy;
- Impact of HIV/Aids on the KZN economy; and
- The contribution of public institutions in KZN to promoting economic development.

With the exception of beneficial trade arrangements, which is the subject of a separate study commissioned by the DEDT and hence was not analysed here in order to avoid duplication, all these themes are addressed in this report.

Following the submission of the phase 1 report, at the request of the DEDT, the HSRC expanded the terms of reference to include:

- The informal sector;
- Small, micro and medium enterprises; and
- Black economic empowerment.

The review comprises four sections. Appendix A, which provides an analysis of industrial policy in South Africa in the post-1994 period, sets the context for the analysis of the performance of the KZN economy. It has been placed in the appendix as a convenient point of reference.

Section 2: The Performance of the KZN Economy, commences by locating the KZN economy within the national economy by examining its contribution to, and contrasting its performance with, that of the national economy. Structural change within the KZN economy during the 1995 to 2001 period is then analysed. This yields a clear picture of the sectors that have been driving KZN's growth, as well as those that are declining. These sectors (in particular, aluminium, petroleum, paper and paper products, food and beverages, automotives, clothing and textile) are subjected to further analysis in order to identify the dynamics driving their growth and decline. The spatial distribution of economic activity is subsequently analysed to demonstrate the concentration of such activity in KZN's three metropoles. The status of the SMME sector, the informal sector and black economic empowerment are then surveyed. Finally, the role of nodal developments (in particular, spatial development initiatives and industrial development zones) and KZN's logistics platform (i.e. the Ports of Durban and Richards Bay) in KZN's economic development are examined.

Section 3, Labour Markets in KZN: Labour Absorption, Human Resource Development and HIV/Aids addresses the critical issues of unemployment, skills formation and the economic impact of HIV/Aids. It commences with an overview of the unemployment situation in KZN and provides an analysis of employment trends across sectors, occupational categories, age groups, racial and gender groups and the formal and informal sectors. The analysis of human resource development in KZN highlights the educational attainment of the labour force and provides an analysis of the province's educational institutions, with respect to their responsiveness to the demand for skills emanating from industry. It also examines the extent to which there has been take-up of the national skills development strategy (NSDS) within KZN. The sub-section on HIV/Aids provides an analysis of the prevalence of HIV/Aids in KZN and its impact on labour markets and the broader economy.

Section 4: The Role of Provincial Government in Economic Development provides a context for the identification of policy instruments to drive economic development at the provincial level. To that end, it commences with a survey of international trends with respect to regional development and highlights agglomeration economies and investment promotion as key policy instruments. The roles and powers of the three tiers of government in South Africa are then surveyed. Finally, an analysis of the role of the various provincial institutions responsible for promoting economic development in KZN is provided.

Section 5, Future Economic Prospects for KZN: Challenges and Opportunities, summarises and synthesises the key challenges for the KZN economy that emerge from the analysis in sections 2, 3 and 4.

2. The KZN economy

2.1 Introduction

In order to set the national context within which the KZN economy is located, an analysis of industrial policy is provided in Appendix A. While the structure of the KZN economy differs from that of the broader national economy – particularly with respect to the dominance of the manufacturing sector and the limited role of mining – its development trajectory will take place within the framework of national industrial policy and the positioning of specific sectors within global supply chains. This is an important point of departure in the formulation of a provincial industrial strategy.

The objective of this overview of the KZN economy is to identify the sectors and dynamics that are currently driving economic growth. To that end, the KZN economy is contrasted with national economic trends, structural changes are surveyed and the dynamics underpinning them are analysed for particular industries. In addition, given their prominence in KZN's future economic development trajectory, nodal developments and the role of KZN's logistics platform (in particular, the Port of Durban) are examined.

Promoting small, micro and medium enterprises to enhance linkages and employment multipliers in the provincial economy is a central preoccupation of the DEDT. Measures that are being undertaken to promote this sector are therefore surveyed. A related issue is the role of the informal sector. The magnitude and role of this sector are analysed to provide an indication of its contribution to employment and output. Finally, the status of black economic empowerment in KZN is examines as its promotion is an imperative of both first and second-tier government.

A note on the provincial database

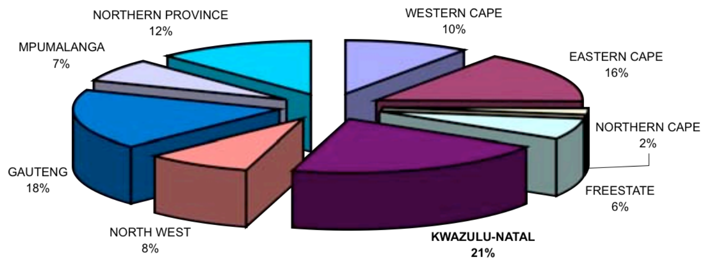
The database used in this analysis was sourced from Econometrix. It provides estimates based on the 1994 census carried out by the (then) Central Statistical Services. Microanalysis and qualitative work have demonstrated that the trends captured by this database across South Africa's 9 provinces are extremely reliable.

A week before the submission of the interim KZN economic review (on 30 November 2002) Statistics South Africa (SSA) released a Discussion Paper entitled "Gross Domestic Product Per Region: Annual Estimates 1995 to 2001". The data presented for KZN has been thoroughly scrutinised by the project team and compared to the Econometrix database. In addition, Econometrix and other firms that construct databases were consulted about the accuracy of the SSA provincial database. There is consensus that it is not very accurate, hence its status as a "discussion document" rather than a definitive source of provincial data. For this reason, the economic analysis presented in this section is based on the Econometrix database. The qualitative analysis of different economic sectors has confirmed its accuracy.

2.2 KZN in a national context

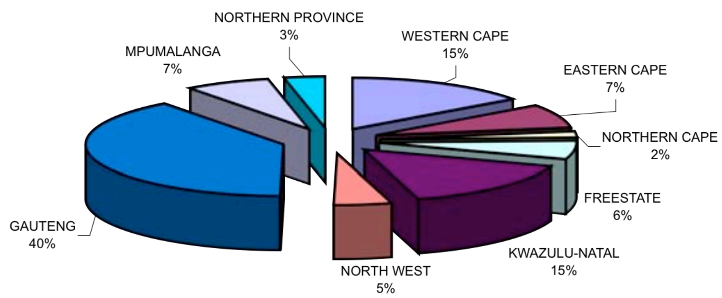
KZN is the most populous province in South Africa. It is home to over 9 million people, accounting for 21% of South Africa's population. In terms of South Africa's GDP, however, KZN generated a mere 15% of total output in 2001, as illustrated in Figure 2.1.

Figure 2.1 – % population by province, 2001



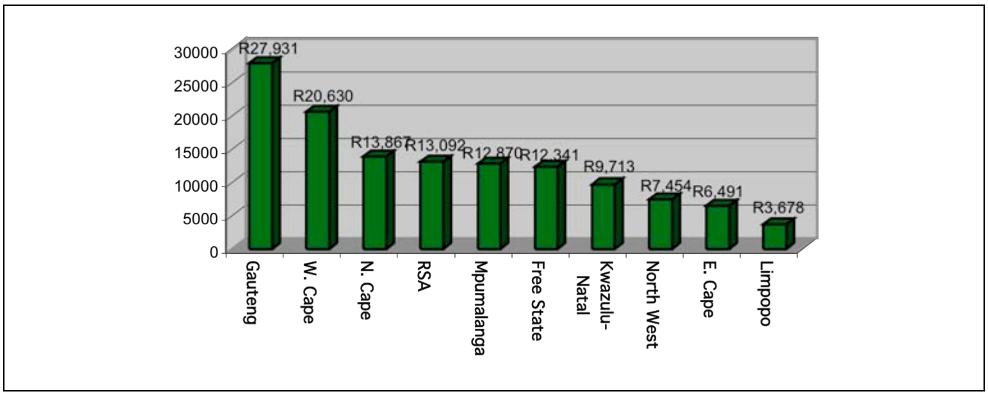
KZN is the second largest contributor to South Africa's GDP (together with the Western Cape), but is well below the leading province, Gauteng, which accounts for 40% of South Africa's GDP. This reflects South Africa's unorthodox development trajectory, as in the absence of mineral extracting activities in Gauteng, economic activity would tend to be concentrated in a coastal region with a large port such as KZN, rather than an interior hinterland.

Figure 2.2 – % GDP per province, 2001



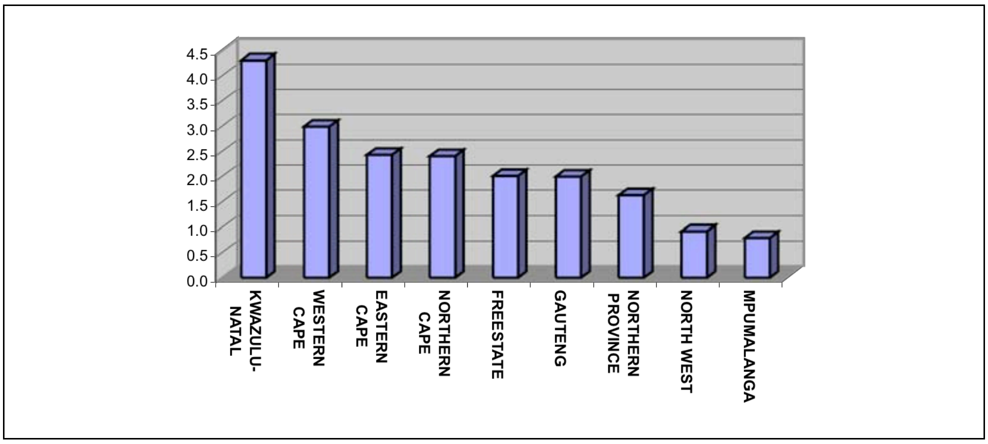
A calculation of Gross Geographic Product (GGP) per capita reveals that KZN is the fourth-poorest province in South Africa, with an annual income of R9, 713 per person living in the province in 2001. This is just over a third of Gauteng's per capita GGP of R27, 931 per annum and less than half of that of the Western Cape at R20, 630. The Northern Cape, Mpumalanga and the Free State all have higher per capita incomes than KZN (see Figure 2.3).

Figure 2.3 – Per capita GGP by province, 2001



The relatively poor status of the KZN economy is more marked in a context where it has been the fastest growing province during the 1995 to 2000 period. Figure 2.4 illustrates that at an average rate of growth of 4.3% per annum, KZN has outperformed all the other provinces in terms of growth in the post-apartheid period.

Figure 2.4 – Average annual % real GGP growth, 1995 - 2000



The structure of KZN's economy differs from the structure of the national economy, as illustrated in figures 2.5 and 2.6. The most striking difference is that KZN has a much larger manufacturing sector (25% of GGP compared to 19% of GDP for SA) and a mining sector that is one-sixth of the size of its national contribution to GGP (1% for KZN, compared to 6% for SA). In addition, KZN's transport and communications sector is larger than at the national level (15% for KZN, compared to 10% for SA), as is the agriculture and forestry sector (4% for KZN, compared to 3% for SA).

Figure 2.5 – KZN contribution to GGP by sector, 2001

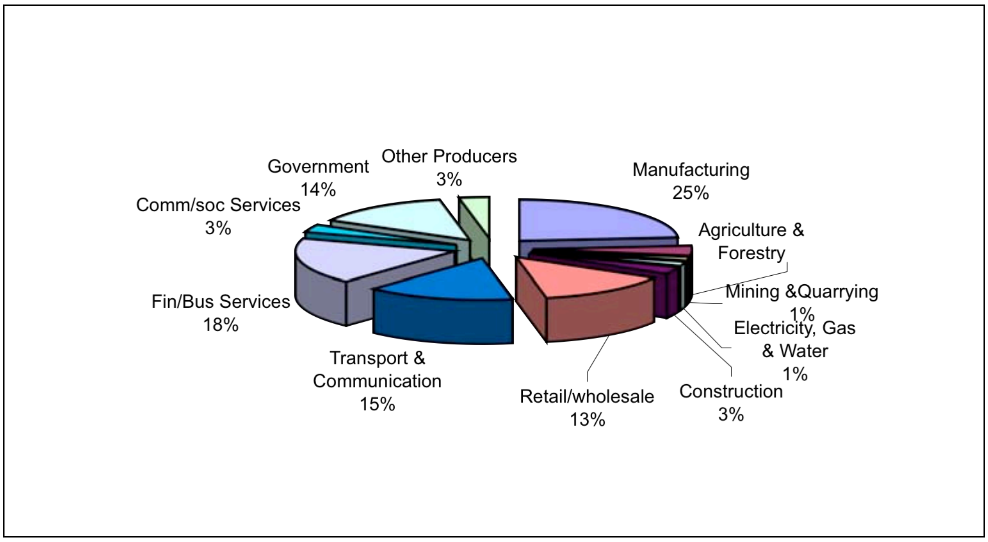
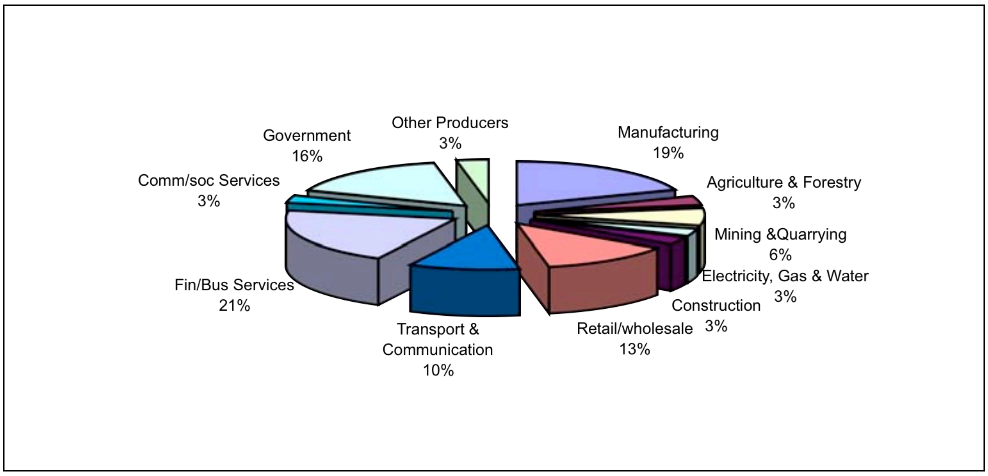


Figure 2.6 – SA: sectoral contribution to GDP, 2001



In summary, while KZN's economic performance has been impressive in the post-1994 period, with growth rates above the national level, it remains the fourth poorest province in South Africa. Given its coastal location, resource endowments and the fact that it is home to South Africa's most important logistics platform for trade, the province's poor position within the South African economy is surprising.

2.3 Structural change

The structure of the KZN economy is related to the province's competitive advantage in the production of certain agricultural products (in particular, forestry and sugar), which feeds into the supply chain for agro-processing in the food, beverages and paper sectors. The logistics platform provided by the Ports of Durban and Richards Bay, both generates economic activity in the form of logistics services, and was a key determinant of the location of import-dependent (for example, petroleum and industrial chemicals) and export-oriented (for example, aluminium) sectors.

Between 1995 and 2001 signs of structural change in the KZN economy began to emerge. Table 2.1 illustrates that in 1995, the KZN economy had a much smaller primary sector and a much larger secondary sector than the national economy. The tertiary sector was slightly larger than for the national economy (due to the predominance of logistics services in KZN), while government's contribution to GGP was smaller than for the national economy.

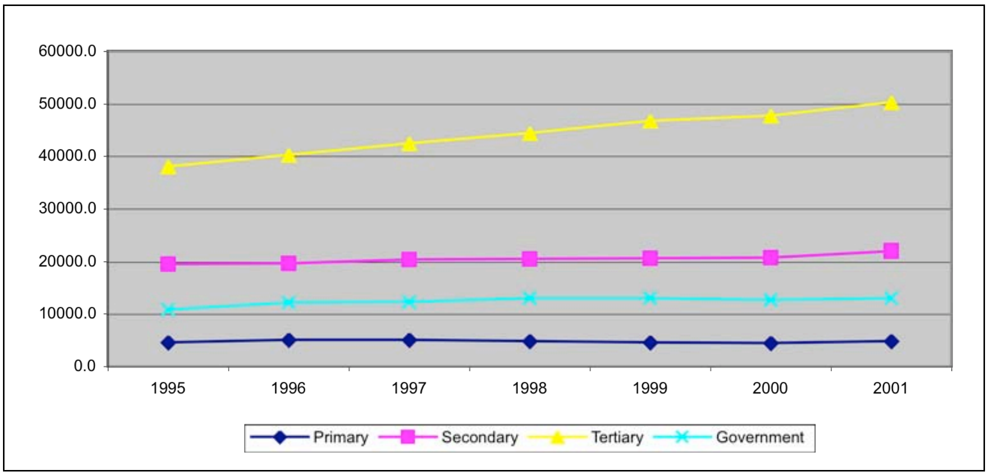
Structural change in the national economy between 1995 and 2001 has been characterised by a reduction in the contribution of the primary and secondary sectors and an increase in the contribution of the tertiary sector to GDP. KZN mirrored these trends but retained a production base with a much smaller primary sector (just over one-quarter) and a much larger (more than double) secondary sector than the national average. Of note is the fact that in 2001 the contribution of 'government' to the KZN economy was 2 percentage points below the national average of 16.5%

Table 2.1 – Structural features of the KZN and SA economies, 1995 & 2001

Sector	KZN - % of GGP		RSA - % of GDP	
	1995	2001	1995	2001
Primary (agriculture & mining)	6.3	5.4	21.8	19.7
Secondary (manufacturing)	26.8	24.4	11.2	10.0
Tertiary (services).	52.1	55.6	50.4	53.7
Government	14.9	14.5	16.6	16.5

Figure 2.7 illustrates growth trends in KZN for the primary (mining and agriculture), secondary (manufacturing), tertiary (services) and government sectors in the 1995 to 2001 period.

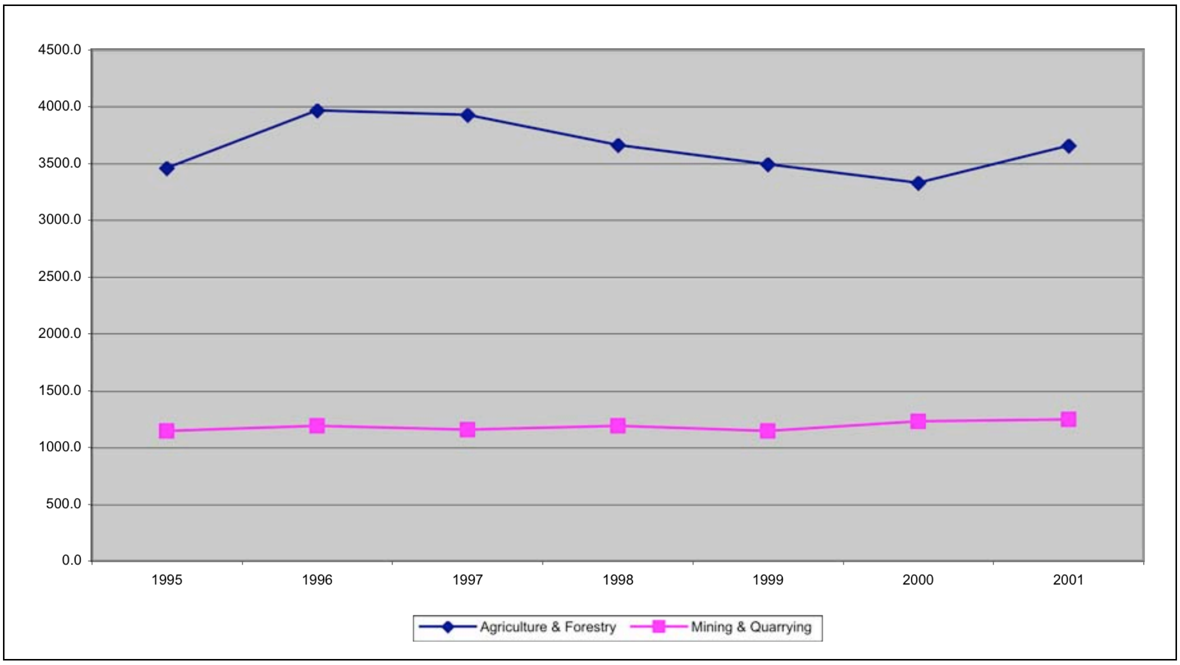
Figure 2.7 – KZN sector growth, 1995 - 2001



The most marked structural change has been in the growth of the services sector (from 52.1% of GGP in 1995 to 55.6% in 2001), which is the most important contributor to GGP. The contribution of the government and manufacturing sectors grew in real terms, but at a slower rate than the tertiary sector. The primary sector demonstrated extremely modest growth.

As illustrated in figure 2.8, within the primary sector, agriculture and forestry grew impressively between 1995 and 1996 (by 14.7%), but experienced negative growth between 1997 and 2000, rebounding in 2001 with a real growth rate of 9.8%. The output of the mining and quarrying sector fluctuated over this period, with an average annual growth rate of 1.5%.

Figure 2.8 – KZN growth of primary sector, 1995 - 2001



Although agriculture and forestry's contribution to KZN's GGP is insignificant, it accounts for nearly 17% of the sector's national output. Although it is relatively unimportant in its own terms, it provides valuable industrial inputs into sectors that play a substantial role in the manufacturing sector (for example, food and food products, paper and pulp and beverages). The agriculture and forestry sector is experiencing extreme difficulties on a national level as evidenced by a miniscule increase of 0.2% in real gross value-added for the period 1996-2001, considerably below a 0.7% increase in output. This reflects the removal of subsidies and import protection in the sector.

In the services sector (figure 2.9), the retail and wholesale sector was the largest contributor to GGP in 1995, but was overtaken by finance and business services in 1997 and transport and communication in 1999. Indeed, the latter two sectors grew spectacularly over this period, with finance and business services recording an average annual growth rate of 7.3% and transport and communication of 6.2%.

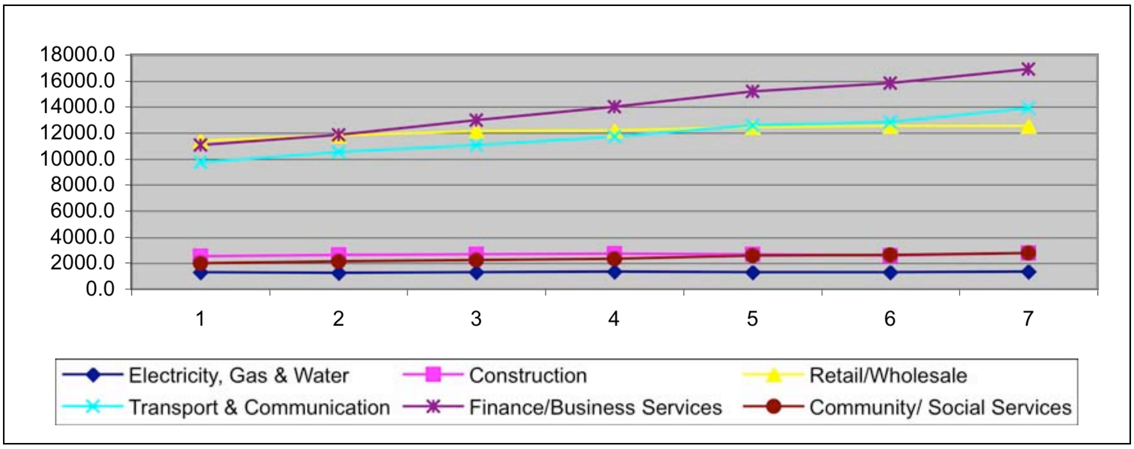
The growth in transport and communication services is related to the dominance of logistics services in KZN, particularly around the ports of Durban and Richards Bay. Higher volumes of trade as a consequence of trade liberalisation, have underpinned the growth of this sector. For example, exports from the manufacturing sector have increased from approximately R20-billion in 1993 to nearly R45-billion in 2001 in constant 2000 prices (DTI, 2002). KZN's increasing strength in this sector bodes well for the future performance of the provincial economy, as the sector is predicted to grow considerably quicker than the national average. Indeed, transport and communications in SA is predicted to outperform the global growth rate in this sector. However, it is important to note that this sector is sensitive to downturns in the economy as this may trigger declines in both imports and exports. In this respect the growth of the KZN economy is strongly linked to economic performance in the SA economy.

As regards the financial and business services sector, its strong growth does not alter the fact that it is still relatively less important to the KZN economy than the national economy, where it accounts for 20.5% of GDP (compared to 18.1% of GGP in KZN). This is related to the presence of most major financial institutions in the Johannesburg and Cape Town centres with very little financial market related undertaking being situated within KZN. Nevertheless the provincial growth in this sector is positive, as predictions are that the sector's growth will continue to outstrip national output over the next four years.

However, neither the transport and communication or the finance and business services sectors hold much promise in absorbing the loss in employment that the province has experienced. Both sectors have high skill requirements while the transport and communications sector tends towards capital intensity and is likely to shed jobs as re-capitalisation of the ports occurs.

In terms of the other tertiary sectors, construction and electricity, gas & water grew moderately (at an annual average rate of 0.6% and 1.6% respectively) from a relatively low base. Community & social services also started from a low base but grew impressively at an average annual rate of 5.3% between 1995 and 2001.

Figure 2. 9 – KZN growth trends of the tertiary sector, 1995 - 2001



2.3.1 The manufacturing sector

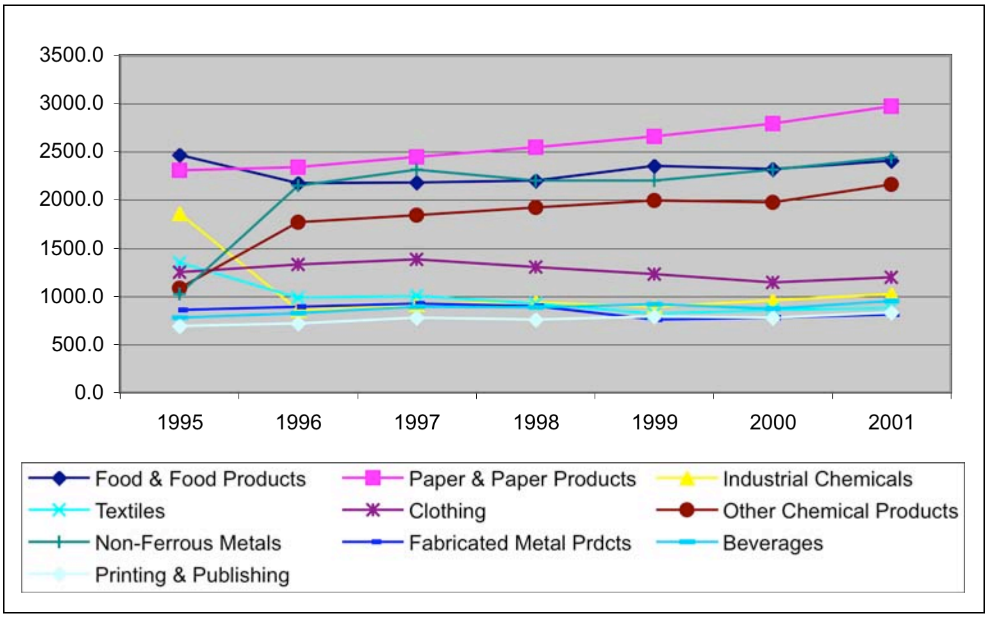
Historically, KZN's forest and sugar plantations provided the inputs for the development of agro-processing and paper product manufacturing sectors that benefited from their proximity to these resources. Simultaneously the presence of the

Durban port laid the basis for the emergence of manufacturing sectors dependent on imported inputs. KZN also benefited from a lower manufacturing wage rate than held sway in South Africa's interior. This laid the basis for the emergence of labour intensive industries, such as clothing and footwear in the province.

The relatively higher contribution of manufacturing to the KZN economy than the national economy, suggests that the process of trade liberalisation (outlined in Appendix A) has had a more profound impact on KZN.

Given the large number of sub-sectors within the manufacturing sector, utilising a SIC 3-digit classification, the analysis proceeds by isolating the top 10 sectors (by contribution to GGP in 1995). Figure 2.10 illustrates that food & food products, which was the largest contributor to GGP within the manufacturing sector in 1995, declined to third position over the period as a consequence of a real average annual growth rate of -0.2%. In contrast, paper & paper products grew at an average rate of 4.3% to become the largest contributor to GGP in 2001. The non-ferrous metals sector grew spectacularly over this period, with real growth rates averaging 20.6% per annum, largely as a consequence of enhanced capacity in aluminium smelting in Richards Bay.

Figure 2.10 – KZN growth trends in top 10 manufacturing sectors, 1995 - 2006



The petroleum industry (falling under the sector 'other chemicals'), which is concentrated in Durban and engages in petroleum refining (for the entire country) and some down-stream petrochemical activities, grew at an average rate of 20.6% per annum in real terms during this period. The beverages and printing & publishing sectors grew modestly at 3.6% and 3.2% per annum in real terms.

In terms of the food and food products sectors - South Africa's largest manufacturing sector - growth both nationally and provincially has been marginal since 1996, largely due to the relatively weak performance of the agricultural sector (ABSA 2001:7). This highlights the fact that the performance of the agricultural sector should be viewed as a source of strategic importance for the province as it feeds into a significant value-chain.

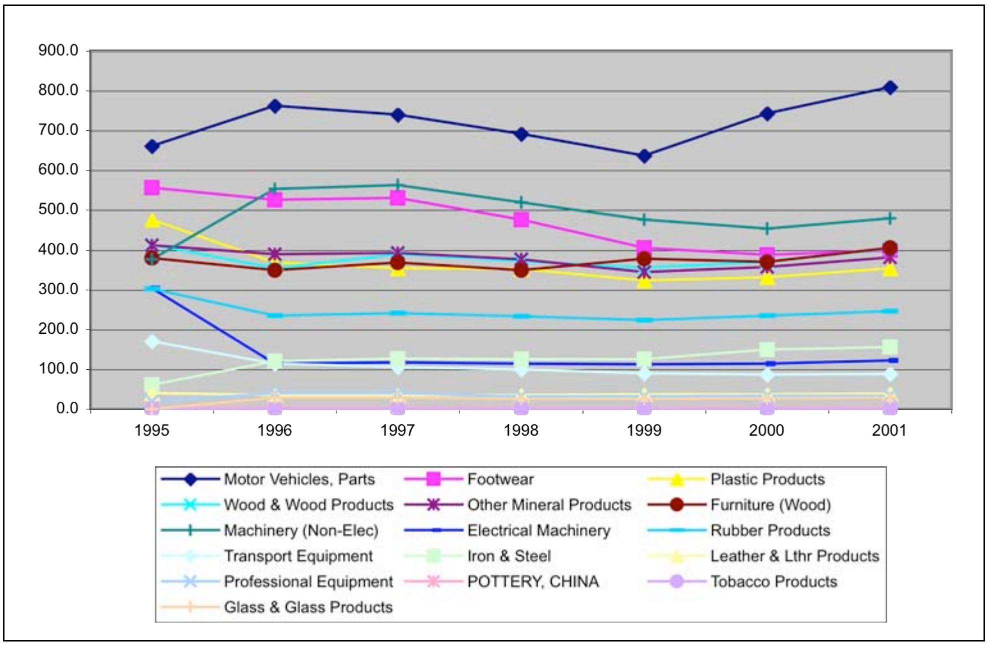
As regards the largest contributor to manufactured outputs – paper and paper products – its export propensity has increased from R1.3-billion in 1993 to just over R2-billion (in constant 2000 prices) in 2001. While the sector's labour productivity has improved dramatically, it appears to still be shedding jobs with employment levels dropping by 4.14% between the September quarter of 2001 and the same quarter of 2000 (DTI, 2002).

The Non-Ferrous Metals sector has also experienced increasing exports and productivity growth. While the sector lost large numbers of jobs during the 1990s, it appears that there may be a slight turnaround, with employment increasing by just below 1% between the September quarter of 2001 and the same quarter in 2000 (DTI, 2002).

In addition to food & food products, declining sectors (in terms of average annual growth rates) include textiles (-6.2%), clothing (-0.6%) and fabricated metal products (-0.6%). Tariff liberalisation in the clothing and textile sector accounts for its decline, particularly as there is evidence of import-penetration in the low end of the market, which is concentrated in KZN.

At a second level of analysis, figure 2.11 provides growth trends for the remaining 15 manufacturing sub-sectors. Motor vehicles and parts emerge as the largest contributor within this category, demonstrating an erratic growth performance over this period, with growth rates ranging from 15.4% in 1996 to -7.8% in 1999, but averaging an impressive 8.8% real annual growth rate. The recent restructuring of Toyota, the dominant player in this industry in KZN, is likely to see this industry expanding further in the future as it gears up to produce for export markets.

Figure 2.11 – KZN growth trends, other sectors (mfg), 1995 - 2001



In contrast, the footwear, plastic products (-5.2%), leather & leather products (-0.4%), rubber products (-2.9%), electrical machinery (-9.4%) and transport equipment (-9.2%) sub-sectors declined in terms of real average annual growth rates over the 1995 to 2001 period. Notably, the iron and steel sector grew at an average rate of 21.3% over this period, albeit from a low base. The top performers in KZN's manufacturing sector (in terms of contribution to GGP) in 2001 are summarised in table 2.2.

Table 2.2 – Top performers: contribution to GGP, 2001

Sector	R-million (constant 1995)	% of total manufacturing output	Ave annual growth (1995-2001)
Paper & Paper Products	2977.2	13.5	4.3%
Non-Ferrous Metals	2444.9	11.1	20.6%
Food & Food Products	2410.8	10.9	-0.2%
Other Chemical Products	2160.6	9.8	13.9%
Clothing	1198.5	5.4	-0.6%
Industrial Chemicals	1024.2	4.6	-5.9%
Beverages	952.7	4.3	3.6%
Textiles	878.3	4.0	-6.2%
Printing & Publishing	832.1	3.8	3.2%
Fabricated Metal Products	814.4	3.7	-0.6%
Motor Vehicles, Parts	809.8	3.7	3.9%

Growth trends within these sectors reveal that the following industries are expanding: paper and paper products, non-ferrous metals, other chemical products (i.e. petroleum), beverages, printing & publishing and motor vehicles and parts. Declining sectors include food & food products, retail & wholesale, clothing & textile, industrial chemicals and fabricated metal products. The factors contributing to the growth and decline of these sectors warrant further investigation.

All sectors that have been experiencing growth in the 1995 to 2001 period are captured in table 2.3. Apart from glass and glass products, which grew spectacularly from a miniscule base, the sectors that are growing rapidly and are of a scale to impact on the KZN economy (as measured by their contribution to the output of the manufacturing sector) are non-ferrous metals, other chemical products (petroleum), paper & paper products, beverages, motor vehicles, printing and publishing, non-electrical machinery and wood furniture.

Table 2.3 – Manufacturing sectors undergoing growth, 1995 - 2001

Sector	% manufacturing	Ave annual growth (1995-2001)
Glass & Glass Products	0.1	3519.5
Iron & Steel	0.7	21.3
Non-Ferrous Metals	11.1	20.6
Tobacco Products	0.0	17.2
Professional Equipment	0.2	16.5
Other Chemical Products	9.8	13.9
Machinery (Non-Elec)	2.2	5.6
Paper & Paper Products	13.5	4.3
Motor Vehicles, Parts	3.7	3.9
Beverages	4.3	3.6
Printing & Publishing	3.8	3.2
Furniture (Wood)	1.8	1.3

As outlined in Appendix A, a key factor underpinning structural change in the manufacturing sector is trade liberalisation. The DEDT recently commissioned the School of Development Studies at the University of Natal, to undertake an analysis of trade patterns in KZN in the post-1994 period. Of note is the finding that over the 1993-2001 period, the most important export sectors were paper, chemical & allied, minerals, metals and wood. Imports dominated the chemical & allied, machinery & equipment, mineral and textile sectors.

The data is not strictly comparable as this study has utilised the 3-digit SIC classification while the trade study utilises the Harmonised System as this is the classification used by Customs and Excise for the collection of trade data.

2.3.2 Tourism

Tourism is captured statistically in the tertiary sector, under the wholesale/retail sub-sector, where catering and accommodation services are recorded. As it is a prominent sector in KZN, which has one of the highest employment multipliers, trends in this sector are discussed separately.

Tourism is one of KZN's most important sectors. It contributes approximately 10% to GGP, amounting to $1.3-billion in 2002. The province hosts approximately 445,765 international visitors per annum. In addition, approximately 18% of all domestic tourist visits are to KZN, making it one of South Africa's leading domestic tourism destinations (see Figure 2.12).

The industry makes a substantial contribution to job creation in KZN, providing approximately 110,000 jobs. A review of research conducted at the national and provincial levels[1] confirms that the economic multiplier for tourism in KZN is in the order of 1:1.42 and the employment multiplier is estimated to be 15.6 jobs for every R1-million of direct tourism expenditure in 2001. The sector contributes substantially to sectors reliant on consumer spending – the average tourist spend is approximately R1,000, and the average visit 11.4 nights.[2]

The Province has many and varied attractions to offer. Natural resources include beaches, wildlife, and the mountains. A rich and varied cultural tradition of both city and rural life provides for a range of tourism experiences. This is evident in the wide range of tourism product and services on offer (see Table 2.4).

Table 2.4 – KZN tourism supply statistics

Facilities	No.
Hotels	208
Guest Houses	165
Bed & Breakfasts	555
Caravan & Camp Sites	130
Conference Venues	243
Tour Guides	529
Tour Operators	236

[Source: TKZN 2002]

The varied product range enables the province to cater for a wide tourism market. In a recent survey conducted by TKZN, it was found that the psychographic characteristics of people who made a holiday or leisure trip to a KZN destination

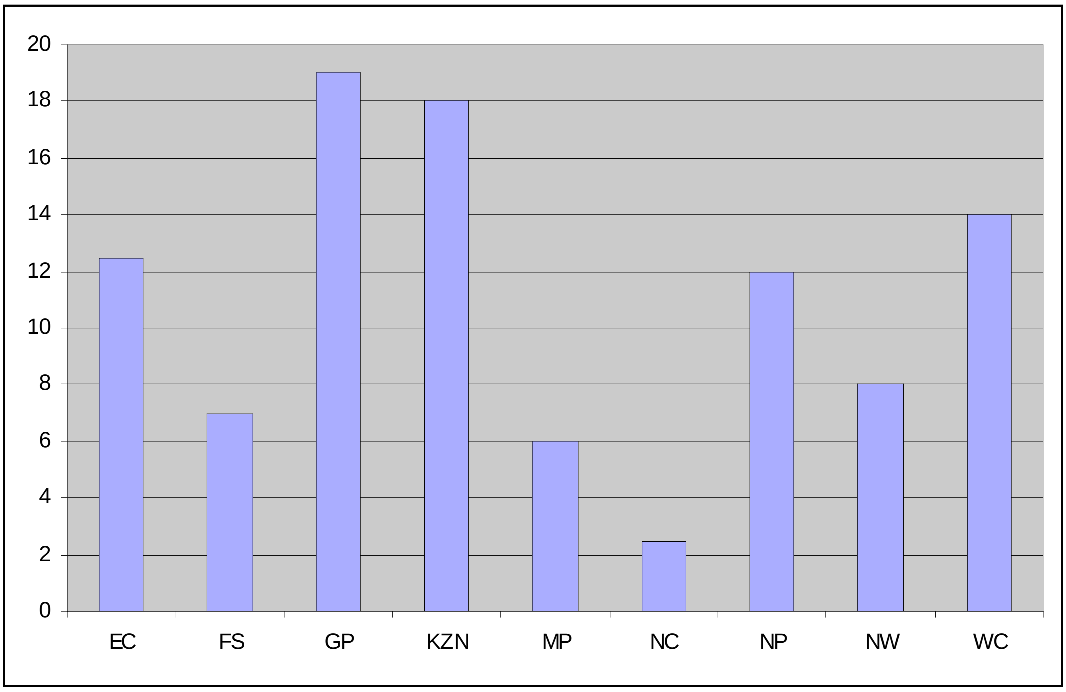
[1] S A Tourism, TKZN

[2] TKZN, 2002

included 43% who could be classified as upmarket campers, 30,2% as beach lovers, 25,2% as game and bush lovers and 8,3% as economy trippers. While 34% did not fit clearly into any of the four categories, many people fitted into more than one category.

2.3.2.1 KZN: domestic tourism trends

Figure 2.12 – SA domestic tourism: share of provincial destinations



[Source: SA Tourism 2001 Domestic Tourism Survey]

Gauteng if the only province that surpasses KZN in terms of the number of domestic visitors. It is, however, the leading domestic destination for leisure visitors and domestic tourism spend. Indeed, KZN continues to maintain and grow its share of the domestic tourism market with an estimated 5.8 million urban adult domestic tourists visiting destinations within KZN in 2002, 1 million up on the same period in 2001. This indicates a recovery in tourism flows to the peak years of 1997 and 1998. The average adult domestic tourist to KZN spends approximately R616 to R1,300 per trip[3], and stays for an average 7.4 nights. At current visitor numbers, this represents approximately R4-billion per annum.

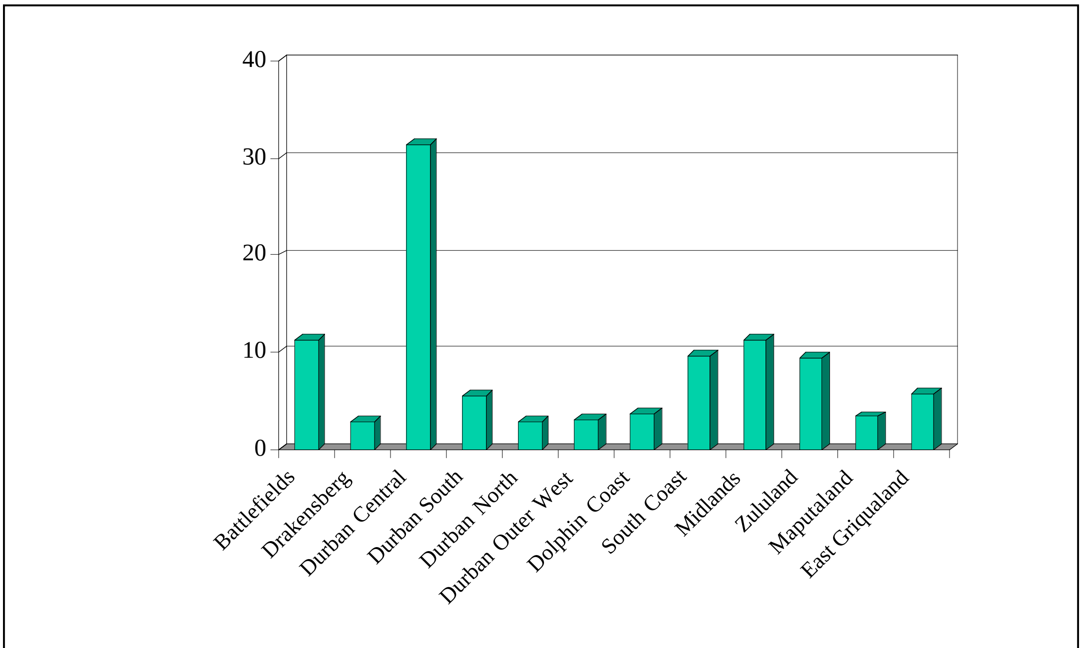
Tourism patterns are typically cyclical with visitor numbers increasing in particular periods such as school holidays and large sporting and cultural events. Statistics South Africa notes that in Easter 2001, a 71% occupancy rate was experienced by hotels in

[3] TKZN, 2001

Umhlanga and on the Beach Front, representing just under 1 million tourists. A similar pattern is experienced over the Christmas break.

The main source markets for domestic tourism include KZN residents and visitors from Gauteng and the Eastern Cape. The main purpose of visiting KZN for domestic visitors includes visiting friends and relatives (53%), holiday (25%), business (9%), with other purposes accounting for 13%.[4] The main activities undertaken in KZN by domestic visitors include Beach activities (45%), watching live sports events (23%), visiting a nature reserve (13%), Arts / Crafts Centre (12%), Museum / Art Gallery (8%), and hiking / mountain climbing (8%).[5] Key domestic tourism destinations are the Durban Central area, the South Coast, the Midlands, the North Coast, and the Drakensberg Mountains.

Figure 2.13 – KZN dominant regional destinations



2.3.2.2 KZN: international visitor trends

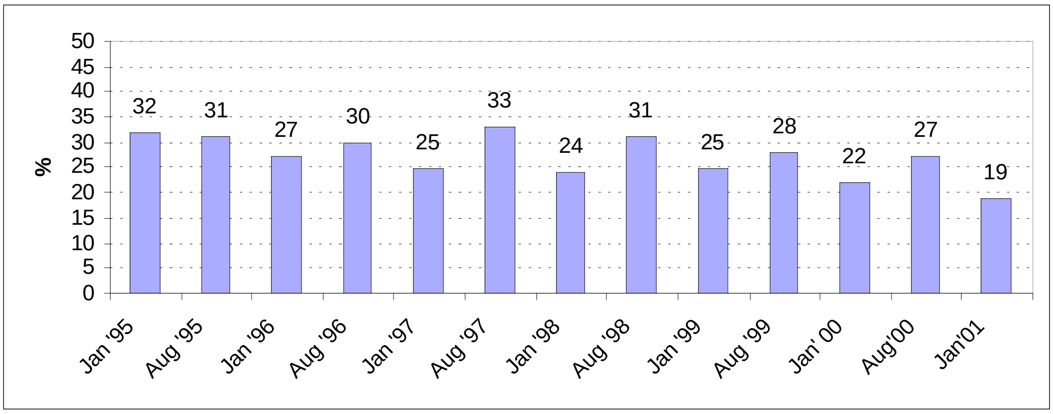
The number of international tourists (based on all RSA air arrivals in 2002) visiting KZN annually is approximately 445,765. Despite the fact that the absolute number of international tourists to KZN has been increasing, relative to other provinces the percentage share has declined in recent years. Between 1997 and 2001, the percentage

[4] TKZN, 2002

[5] TKZN, 2001

of international visitors to South Africa that visited KZN declined from 30% to 25%. This decline was first noted in 1998 when SAA and BA eliminated all foreign tag flights from Durban International Airport (DIA). This reduced share of foreign visitors is compounded by an overall decline in foreign visitors experienced by the nation in that time frame – 2001 visits from foreigners to South Africa declined marginally due to September 11th, lack of air seat capacity to South Africa and concern about the political situation in Zimbabwe. In spite of the difficulties in sustaining share of foreign arrivals KZN has been benefiting from the 19% growth in overseas arrivals during the first nine months of 2002 (see Figure 2.14).

Figure 2.14 – Proportion of foreign SA air arrivals that visited KZN



Foreigners visit the province for a range of reasons: 54% come for holiday purposes, 16% to visit friends and relatives, 17% for business purposes and 13% for other reasons.[6] Activities undertaken by foreign visitors include beach activities (44%), visiting a nature reserve (39%), Arts / Craft Centre (25%), Cultural Village (25%), Museum or Art Gallery (19%), and Hiking / Mountain Climbing (17%).[7]

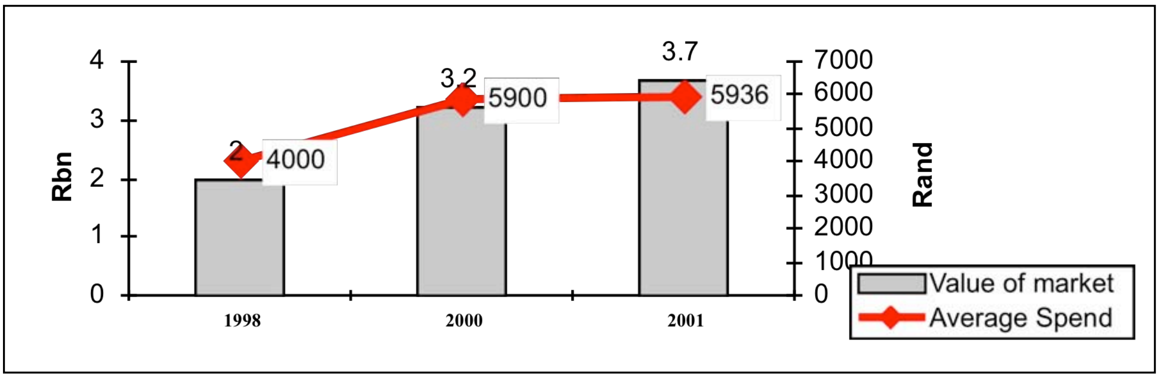
KZN's foreign airborne tourists originate predominantly from the United Kingdom (17%), USA & Canada (15%), Germany 12%, Africa (9%), Australia (6%), the Netherlands (5%) and France (4%). The top Foreign tourist spenders based on average spend per trip include Australia (R11 928), USA (R6 440), France (R4 642), Germany (R4 528), Holland (R4 120) and UK (R3 870). Foreign tourists make an important economic contribution to the province - they spend an average of R5,936 per person with the average length of stay in KZN of 5 to 6 nights. At current levels, this generates revenues estimated at R 3.7-billion per annum[8] (see Figure 2.15).

[6] TKZN, 2002

[7] TKZN, 2002

[8] TKZN, 2002

Figure 2.15 – Value of KZN foreign market



2.3.2.3 Tourism investment potential

The natural tourism resource base, combined with the large Gauteng market on the doorstep, and a highly efficient tourism infrastructure, suggest excellent long-term investment potential for tourism in the Province. This is acknowledged by the market - 2002 saw substantial progress in a number of new tourism related investments including casinos in Empangeni, Pietermaritzburg and Newcastle, the Village Green, Durban, and Umhlali, as well as the Point Marine Park, an R800-million investment.

2.3.2.4 Challenges facing the tourism industry

Tourism flows to KZN are substantially affected by the levels of disposable income available to its target markets, and perceptions regarding the safety of the Province as a destination. Domestic tourists also are wary of the "crime and grime" image of Durban. For international tourists, additional considerations are fears linked to safety in the air, fears related to war in the northern hemisphere, and fears regarding the instability of Zimbabwe.

Recent research conducted by the province notes that perceptions of domestic tourists around personal safety and security are improving. Challenges remaining for the Province include improved hygiene, tired and insufficient product, lack of marketing/awareness, and overpricing. When tourism businesses do relocate to other areas, a key driver is the perception of massive bureaucratic red tape hampering development, resulting in businesses relocating to Cape Town and Johannesburg.

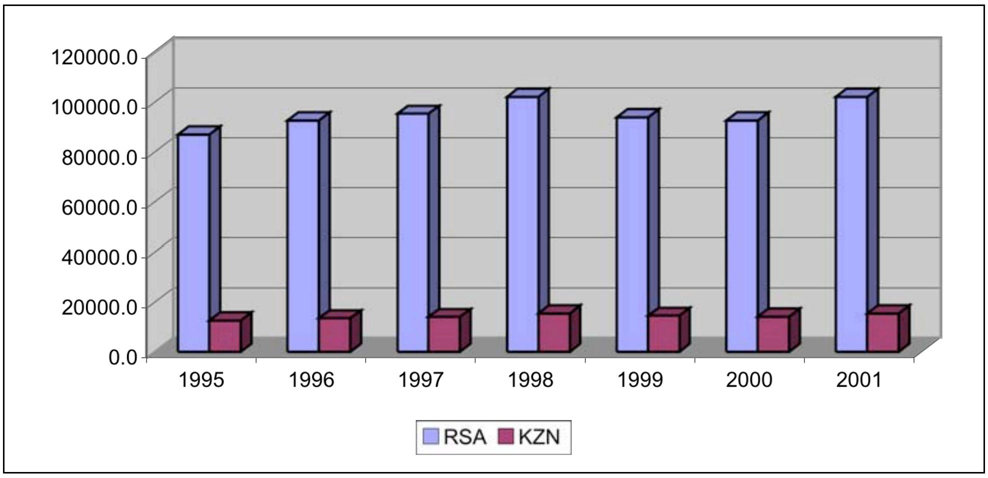
From a marketing point of view, there is a need to create a greater awareness of KZN's diverse tourism product by increasing advertising both nationally and internationally. Additional priorities are to undertake far-reaching anti-crime and city clean-up campaigns and to commit government resources to opening up new regions through improved logistics infrastructure.

A further challenge is to address the lack of effective participation of previously disadvantaged individuals and companies at an ownership level in tourism products and services. This will require that a range of programmes be implemented which ensure effective black and community involvement in tourism in KZN. Finally, a major opportunity exists in increasing the number of foreign tourists to the province.

2.3.3 Investment trends

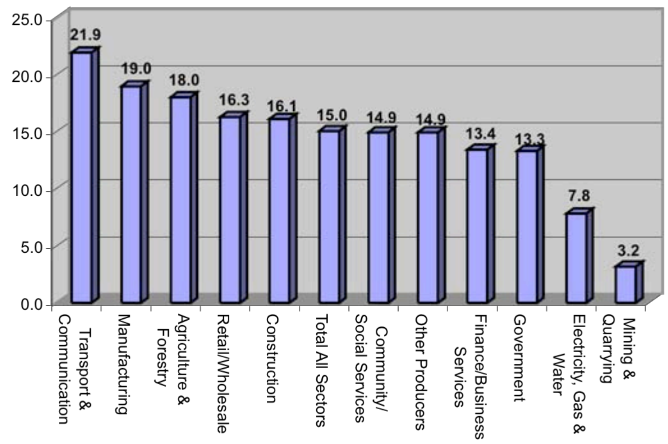
The proportion of aggregate investment flowing to KZN is commensurate with its contribution to South Africa's GDP. In aggregate, KZN accounted for 15% of South Africa' investment in the 1995 to 2001 period, although it fluctuated between 14.6% in 1995 and 15.5% in 1999, as depicted in figure 2.16.

Figure 2.16 – Investment: 1995 - 2001 (at 1995 constant prices)



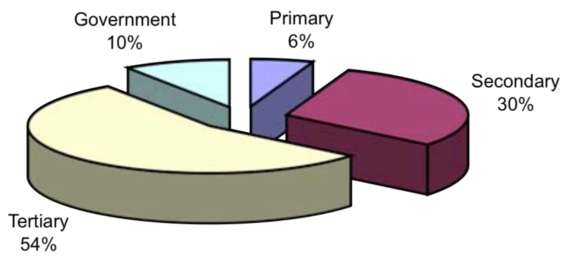
As a share of national investment, the highest proportion has gone to transport and communication, manufacturing, agriculture & forestry, retail & wholesale and construction. The latter three do not correspond to the growth sectors in the KZN economy, but the data must be interpreted in the context of low investment in these sectors at the national level (see Figure 2.17).

Figure 2.17 – Investment in KZN as % of SA, 1995 - 2001



In terms of the 15% of national investment accounted for by KZN, figure 2.18 illustrates its distribution across the different sectors for the 1995 to 2001 period. These investment trends broadly reflect the structural changes within the KZN economy.

Figure 2.18 – KZN investment by sector (constant 1995 prices), 1995 - 2001



The dominance of the finance and business services in KZN's economy is underpinned by the fact that 22.4% of total investment flowed to that sector. The transport and communication sector also performed impressively, accounting for 19.5% of total investment. In the primary sector, the majority of investment flowed to the agriculture and forestry sector, accounting for its modest growth.

In the manufacturing sector, investment patterns do not cohere with growth trends. For example, food and food products accounted for 12.3% of total manufacturing investment, textile 4% and industrial chemicals 7.3% although they have been declining in terms of output. Paper and paper products (the largest growth sector within manufacturing), accounted for 12% of total manufacturing investment, other chemical products (petroleum) for 1.5% and non-ferrous metals for 1.5%. Notably, motor vehicles and parts accounted for 3.4% of investment in the manufacturing sector.

In terms of the spatial distribution of specific investments, the Durban Pinetown Region – commensurate with its status as the leading economic region in the province – received the lion's share of investment, totalling R13,912.5-million during the 1997 to 2001 period.

Investment projects in the Pietermaritzburg statistical region accounted for R7,278-million. In the non-ferrous metals sector this included the R2,400-million investment in the Hulett Aluminium Plant, completed in Pietermaritzburg in 1999 and Hulamin's aluminium roll expansion of R3,000-million completed in 2000. Two shopping centres, the Brookside Garden shopping centre, and the Pietermaritzburg shopping and entertainment centre saw respective investments of R350-million and R250-million in Pietermaritzburg. The Akani Msunduzi Golden Horse Casino & Entertainment Centre, completed in 2001, gave a boost to the local tourism and leisure industry with a R220-million investment. Government investment in the area included the R42-million Edendale housing project, R230-million Midmar Waterworks, and R125-million infrastructure Development projects undertaken by the Indlovu Regional Council (now District Municipality).

The Lower Tugela Statistical Region, comprising the Industrial node of Richards Bay benefited from investment in a range of projects totalling R28,460-million. Investment projects related to the upgrading of the Richards Bay Harbour and various terminals, and various investments from industry benefiting form close proximity to the port such as the granular fertilizer plant, AECI lysine expansion, Hillside Aluminium smelter.

Investment in rural areas was negligible in comparison to that recorded in the major economic metropoles of the province. The only investment in the Mapumulu Ndedwe statistical region was a R65-million investment in the electrical machinery sub-sector, comprising the Tridelta Magnet production plant in Mandini where the project completion date was set for 2002.

Investment in the Mahlabatini Nongoma area included a R73-million investment in the Hluhluwe community water project by Mahlatuze water, with the project set to for completion in 2000. No investment has been recorded in the Umlazi Umbumbulu statistical region.

Recorded investment in the Camperdown Ixopo statistical region included the R150-million investment in the Bayhead-Umlaas gas pipeline located at Umlaas, by project investor Sasol and completed in December 1999.

The major investment in the Mount Currie Underberg region was an investment of R60-million by Investec Properties in the Kokstad retail centre, completed in 2001.

Four major investments were recorded in the Port Shepstone Alfred statistical region. Collectively the investments amounted to R264-million and were located in the water, transport, communication and community social services sectors. The projects included the Port Shepstone /Baboyi Housing Development comprising an R80-million investment which was completed in December 2000, a R90-million rehabilitation of the Harding-Izingolweni N2 by the SA National Roads Agency completed in 2001, a R5.2-million upgrade to roads & sanitation services in Margate completed in 2001, and the implementation of three rural water schemes in Port Shepstone and Margate to a value of R3-million.

The economically depressed Mooi River Umvoti statistical region benefited from investment in the transport and communication sector. Road Surface repairs undertaken by the Provincial Department of Transport in 1999 in Mooi River saw some R20-million invested in Mooi River.

Two major investments were recorded in the Escourt Klipriver statistical region. The local food and food products sector was given a major boost with the location of a Starch and glucose factory, in Klip River in 1999. The Tongaat-Hulett project involved a R600-million investment in the area. The manufacturing sector of Ladysmith benefited from a R3.3-million computer upgrade, completed in 2001.

Investment in the Newcastle Dundee Statistical region was undertaken in the iron and steel sector between 1999 and 2000. This involved an investment of R730-million in Chrome plants in Newcastle.

The Vryheid Paulpietersburg region benefited from investment in four projects in the water, food and food products and manufacturing sectors totalling R1,106-million. The projects included a R900-million investment in a Glycol manufacturing plant in Pongola, the R185-million Illovo Sugar expansion in 2000 in Pongola, the establishment of the Ingle Game Reserve, in Vryheid in 2000, which involved a R126-million investment, and the R75-million investment in the Paris Dam in Vryheid in 2000.

Investment in the Ingwavuma Hlabisa statistical region was concentrated in the food and food products sector and involving the Illovo Sugar plant expansions in Ubombo and Umfolozi.

Critically, as argued in section 2, the quantum of investment in South Africa (and KZN, which accounts for a mere 15% of the total) is simply too small to underpin higher levels of growth. Hence the challenge is to utilise policy instruments in order to enhance investment flows to targeted sectors in the KZN province.

2.4 The dynamics of structural change

In order to develop a deeper understanding of the dynamics driving structural change in KZN, a qualitative methodology – in the form of interviews with key players in select sectors – was utilised. The findings are extremely pertinent to the development of a provincial industrial strategy as they highlight the factors that both enhance and undermine the competitiveness of industries as they reposition themselves for global competition.

The analysis of structural change in the KZN economy during the 1995 to 2001 period reveals that growth has been concentrated in the services sector. The primary sector has been relatively stagnant, while the manufacturing sector has enjoyed moderate growth. Hence the higher than average growth experienced by KZN during the 1995 to 2001 period is largely driven by the growth of the services sector.

A disaggregation of these sectors reveals that in terms of scale, finance and business services, transport and communication, paper and paper products, non-ferrous metals (i.e. aluminium) and other chemical products (i.e. petroleum) are driving the province's growth.

Smaller sectors that are performing well include community and social services, beverages, motor vehicles & parts, printing & publishing, non-electrical machinery, wood, iron and steel and professional equipment. Declining sectors include (in order of their weight in the KZN economy): food & food products, clothing, industrial chemicals, clothing, textiles and fabricated metal products.

Qualitative research revealed that the growth of the tertiary sector – in particular, financial and business services and transport and communications – is related to KZN's economic growth and substantial increases in the volume of exports. This is because the demand for financial and business services is a *derived* demand – i.e. it is derived from the growth of other economic activities. Hence there are no specific dynamics that underpin the growth of this sector. In the case of transport and communications, substantial increases in the volumes of exports going through the Ports of Durban and Richards Bay underpin this trend. The dynamics underpinning growth and decline in the aluminium, paper and pulp, petrochemicals, automotives, clothing, textile and food and beverages sectors are elaborated upon below.

2.4.1 Aluminium

Aluminium is the world's largest metal commodity market with an annual turnover exceeding R1,000-billion. It is traded in US dollars through the London Metals Exchange (LME) and is has only been produced on an industrial scale since 1886. In 1900, yearly output of aluminium was a thousand tons and by the end of the twentieth century, yearly production had reached 32 million tons, comprising 24 million tons of primary aluminium and eight million tons from recycled material.

Availability of Bauxite and/or Alumina, cheap energy and up to date technology determine competitive capability in upstream Aluminium. Energy represents a large part (some 25%) of the costs associated with primary aluminium production. This means that producers have always had a vested interest in minimising electricity consumption. Smelters in the 1990s used a third less electricity per ton than the equivalent plant in the 1950s.

Aluminium is considered an 'energy bank', that is, the original energy input can be recovered every time the product is recycled. Consequently, there is substantial economic activity in the recovery and recycling of scrap Aluminium, which can be recycled repeatedly and profitably without loss in quality. Many products, such as automotive castings, are made mainly from recycled metal, otherwise known as secondary aluminium.

Excluding demand from China, the global aluminium market is projected to grow at 2% to 3% per annum. 2% of the world market represents approximately 400,000 tons of aluminium per year of new capacity.

Aluminium is used as the material of choice where light weight, increased power to weight ratio, recyclability and decreased rolling resistance are important. It finds major application in the Automotive Industry worldwide – in 1990, autos used 34kg of aluminium per car, today, and 120kg per vehicle is used on average. Globally, 33 million auto components are sold annually and 20% of all aluminium is consumed by the automotive industry.

The metal is used extensively by the Aerospace industry, the building and construction industry and the packaging industry, as well as in electrical cabling and in electronic equipment.

Trend analysis of the data tabled by the International Aluminium Institute (1990 to 2002) indicates a long-term growth rate of approximately 2% per annum in demand for the metal. Consumer demand for electronics, vehicles, packaging, and construction demand (including electrical cabling) are key drivers of overall demand.

2.4.1.1 Aluminium sector in KZN

Massive shifts in investment focus have changed the nature of the Aluminium Industry in South Africa and in KZN. Southern Africa will soon boast a primary capacity of some 1,35 million t/y, (including Mozal) from 34,000 tons of capacity when the first aluminium smelter in the region, Alusaf, was commissioned in 1971. In KZN, the proximity of appropriate ports, (for raw material imports as well as for exports), reliable supplies of cheap energy and labour and logistics capability are the key drivers behind the upstream expansion growth rate. A negotiated pricing arrangement for electricity, whereby energy costs fluctuate in line with the LME, has been a crucial factor in decisions to invest in the region.

2.4.1.2 Upstream

South Africa's upstream Aluminium manufacturing capacity is entirely located in KZN, although Mozal is located in Mozambique. The sector is very important to

KZN – non-ferrous metals is the second-largest manufacturing sector in the Province and was the fastest growing between 1995 and 2001 – real growth rates averaged 20.6% per annum (contribution to GGP) over the period. This growth was driven by extensive investments upstream in smelting capacity expansion and upgrades in the Richards Bay area, which resulted in substantial increases in upstream (primary) exports. These investments are capital intensive in nature, and hence have limited impact on the levels of job retention or sustainable (long term) job creation in the sector. Upstream investment in KZN has far outstripped investments at the semi-fabricated level (one level downstream) or at the conversion level where components and finished items are produced.

KZN is home to global resources group BHP Billiton's 100%-owned Hillside and Bayside aluminium smelters, both based in Richards Bay. The group's $449-million expansion of the Hillside aluminium smelter, known as Hillside Three, was launched in April 2002 with the start of construction. The Hillside smelter is to be expanded by a further 130,000 t/y, and the Bayside capacity is to increase to 200,000 t/y. This expansion will make Hillside the largest primary aluminium smelter in the Southern Hemisphere and in the western world and will increase BHP Billiton's global primary aluminium production to 1,4 million tons a year, or about 8% of the western world's total production.

The Hillside smelter users French-based Aluminium Pechiney AP30 technology and is deemed to be one of the world's cleanest and most efficient smelters. The reduction pots are the largest in commercial production worldwide. The 576 pots operate at about 320,000 amps and consume less than 13,7MWh of electric energy per ton of aluminium produced.

The bulk of the aluminium produced at Hillside is exported to the Far East, Northern Europe and the USA. (84%) The balance is sold in South Africa and neighbouring countries. The remelt ingots destined for export are transported by truck to the Strang Rennies Metal Terminal (SRMT) at the Port of Richards Bay where they are loaded onto the ships. BHP Billiton Marketing BV, based at The Hague in the Netherlands, sells them.

The aluminium destined for the regional market (16%) - Southern Africa -is sold in liquid and ingot form. Bayside buys liquid aluminium to be sold on to South African customers for the manufacture of aluminium alloy wheels. The ingots for the regional market are delivered by road and rail. They are used by rolling mills (such as Hulett Aluminium in Pietermaritzburg), extrusion plants and cable plants to make a variety of products such as aluminium foil, pots and pans, roof cladding, windows, doors, cables and conductors. It seems likely that investment upstream in KZN may have reached its natural limit – Hillside is constrained by space regarding future expansions, and plans for Aluminium investment in Coega , close to the Automotive industry of the Eastern Cape, may shift the focus of upstream investment in the future. This trend is underpinned by the absence of a container terminal in Richards Bay.

There are four secondary smelters in South Africa. All four extrude aluminium but rolling takes place only in Pietermaritzburg and in Cape Town. Three of the four firms are located outside the Province. However, the largest of the four is the Aluminium division of Tongaat-Hulett, located in Pietermaritzburg and this firm is expanding production facilities. Hulett Rolled Aluminium Products has commissioned a new multipurpose hot-mill, tripling its rolling capacity. Hulett Aluminium is the country's major producer of rolled and extruded aluminium and its main plant is located in Pietermaritzburg, with additional capability in Gauteng, and in Cape Town.

Scrap is typically bought by the secondary smelters, and converted into ingot for castings. Approximately 68,000 Tonnes per annum of scrap is generated in South Africa, of which approximately 34,000 Tonnes is exported with the remainder recycled and re-sold to fabricators and converters.

2.4.1.3 Downstream

In contrast to Billiton and Hulett Aluminium, which are capital-intensive, driven by factor conditions and are cost sensitive, downstream aluminium companies are demand driven. Downstream conversion in South Africa, but especially in KZN, has not kept pace with expansion upstream. The local market is considered close to saturation in terms of how much Aluminium per capita can be consumed domestically, (consumption per capita is 4.5 kg on average per person per annum in South Africa) but there are large opportunities in exports, both direct and indirect. KZN has not historically been well represented in downstream conversion, and there is little activity in the province relative to that in Gauteng and in the Cape.

Recent increases in value added conversion and export have been driven in large part by the devaluation of the Rand against the major currencies. This rendered many South African producers competitive. Major export opportunities may lie in indirect exports – the supply of aluminium components to the automotive industry for example.

Value added aluminium manufacturing in South Africa has increased by a factor of some three-and-a-half times over the last 10 years, but from a low base. South Africa today exports only 20,000 Tonnes of value added products per annum, mostly wheels (South Africa's largest value added export is aluminium alloy wheels, with 80% of production exported) and building products[9].

Most exports are to the SADC and are in relatively low value-added products. Although sustainable exports of primary and secondary aluminium ingots and semi-fabricated products have increased substantially, the downstream value-added product contribution remains small.

Little of this activity has taken place in KZN. This is difficult to understand – since KZN is ideally positioned, in terms of proximity to input material supply as well as to coastal logistics capability, to take advantage of the export opportunity. Yet value

[9] (T Paterson, AFSA)

added conversion in KZN represents less than 15% of the total value added conversion activity of South Africa[10].

To maximise potential for downstream conversion requires researching and understanding the markets and customers, training, technology transfer, and capital upgrades. Much of South Africa's conversion technology is out of date, and general purpose in nature, rather than focused on specific products.

Key constraints to improved downstream capability in KZN are the age of the capital stock and the level of skills available. The capital stock is 8 to 9 generations old, (70's and 80's) and training of people in necessary skills is poor. There is very limited use of the SETA system because it is so expensive to access for smaller firms, and many conversion firms are small to medium enterprises.

2.4.1.4 Policy measures

Support to improve access to SETA training funds combined with support for Capital Stock upgrade over a five to six year period are seen by Industry as the key areas which are likely to stimulate export led value added production growth. Although value added production has historically been located in Gauteng, there is sound economic logic in locating new investment in downstream Aluminium production in KZN, given proximity to supply of upstream and semi fabricated products combined with proximity to ports for export.

KZN institutions such as TIK, in recognising the potential for growth in the local downstream cluster, could consider assigning the Aluminium sector downstream special status, and developing a focused inward investment (FDI) drive to attract investors to the Richards Bay and Pietermaritzburg areas.

This suggests sustainable opportunities for BEE in the value added sector. Possible linkages could be structured with the existing Billiton value added project at Richards Bay, which, although currently small, may offer a starting point for a stronger value added cluster, if supported in a PPP by the Province. The imminent development of Dube, wherein aluminium will be used, can be structured to leverage a starting point for aluminium fabrication in the building products markets.

Detailed economic feasibility studies may be required and could be commissioned thought KZN government agencies to determine the ideal export product focus for the province, which will ensure that investment in new Capital stock is relevant and useful.

Discussions involving the Sector charters with Billiton and Huletts Aluminium might include discussion around assistance to support an export focused conversion initiative, and linkages could be made into the Industrial Offsets program.

[10] (R Linnell, Billiton)

2.4.2 *Paper and paper products*

In KZN, the paper and paper products sector has undergone strong average annual growth of 4.3% between 1995 and 2001. Nationally, the pulp and paper industry contributes 14,4% to manufacturing GDP and 2,7% to national GDP. The bulk of industrial production in South Africa is located in KZN.

In 2000, South Africa was ranked the sixteenth largest producer of pulp in the world and the twenty-fourth of paper and board production. The value of paper and pulp produced in SA in 2001 was in excess of R12-billion and paper production was running at 85% of capacity.[11]

The local industry produces a range of pulp paper and board products and supplies the bulk of local demand. The packaging sector consumes 55% of domestic production, followed by printing and publishing at 24%, newsprint 14% and tissue and disposable products accounting for 7% of domestic production. Local production accounts for 87% of local consumption[12]. A notable paper and pulp export is that of dissolving pulp used in the manufacture of viscose fibre.

Imports are mostly in the specialty papers and board products -domestic demand is insufficient for economic local manufacture. Certain types of pulp for which SA lacks the necessary raw materials are also imported. Large volumes of converted paper and board products are indirectly exported through the packaging of export products, particularly corrugated boxes for export fruit and wine.

The SA pulp and paper industry is supplied exclusively from plantation forests. The forestry industry has enjoyed an annual 8% annual growth in contribution to foreign trade during the last 10 years[13].

Table 2.5 – Summary of SA trade in wood, pulp, paper & paper products

R-million	Imports 2000	2001	% change	Exports 2000	2001	% change
Wood	1,012	1,095	8.2	2,269	2,723	20.0
Pulp	280	216	-22.7	3,429	2,615	-23.7
Paper	2,010	2,227	10.8	2,264	3,098	36.8
Paper products	430	490	13.7	611	860	40.7

[Source: SARS]

[11] PAMSA, 2002

[12] PAMSA, 2002

[13] PAMSA, 2002

The five largest manufacturers of pulp and paper products are SAPPI, Mondi, Nampak Kimberley Clarke and Unicell, together producing almost 99% of national pulp paper and board production. Production is concentrated in 18 pulp, paper and board mills in SA. SAPPI and Mondi are exclusively responsible for pulp production undertaken in nine mills. A Saiccor mill is the only mill that produces only pulp almost exclusively for the export market. Sappi and Mondi are both fully integrated, with involvement in the forestry industry as well as pulp and paper production.

The industry has a strong export capacity with expansion by SAPPI and Mondi resulting in SAPPI ranked as 14th and Mondi 39th by turnover on the list of the largest pulp and paper companies in the world. Nampak and Kimberley Clarke produce tissue, which is converted into consumer and industrial paper products. Nampak also make linerboard and fluting which is converted into corrugated boxes and makes packaging products. Unicell has the capacity to manufacture 80 000 tonnes of packaging papers a year. In recent years a number of smaller producers, focusing on the production of tissue and test liner have emerged.

The lion's share of South Africa's paper and pulp industry is located in KZN. This is due to a number of factors relating to climate, logistics and resources. The climatic conditions of the province are ideal for growing plantations with its high rainfall (afforestation is only possible in areas where rainfall exceeds 800mm per annum) and river access – for example, eucalyptus grown in Northern KZN can be felled from 7 years onwards as opposed to 11 years in cooler high-lying areas. Where bagasse is utilised, it is also necessary to locate pulp mills in close proximity to sugar mills in order to reduce bagasse logistics costs. Furthermore, the high cost of capital intensity of the industry makes operation close to mill capacities imperative.

The close proximity of ports (Durban for paper & pulp, Richards Bay for chips), road and rail networks is a further contributing factor, enabling access to markets, both local and international. The University of Natal and Steve Biko Technikon provide a research and skills support base for the industry.

The major production processes in South Africa are listed below. Those marked with an * are to be found in KZN. Furthermore, recent years have seen the move by various support industries to be located to the province. For example the University of Natal Durban offers extensive research capacity for the industry (see Table 2.6).

Table 2.6 – SA pulp mill capabilities in KZN

Company	Mill	Products	2001 Capacity (1000 t/a)
Mondi	Richards Bay Mill*	Hardwood and soft wood kraft pulp	576
	Piet Retief Mill*	Hardwood and softwood NSSC pulp	60
	Felixton Mill*	Unbleached bagasse pulp	70
	Merebank Mill*	Thermomechanical pulp	220
		Groundwood pulp	66
SAPPI	Ngodwana Mill*	Hardwood and soft wood kraft pulp	410
		Groundwood pulp	100
	Tugela Mill*	Unbleached softwood pulp	230
		Hardwood NSSC pulp	120
	Stanger Mill*	Bleached bagasse pulp	60
	Enstra Mill	Bleached hardwood pulp	90
	Saiccor Mill*	Dissolving pulp	600
Total			2,602

Sappi is the leading producer of coated fine paper in North America, Europe and Africa. The company produces a range of uncoated graphic and business paper, coated and uncoated specialty paper and casting release paper used in the manufacture of artificial leather and textured polyurethane applications. Its Southern African operations include a Corporate head office located in Johannesburg, 3 fine paper mills, 5 forest products mills 4 fine paper sales offices, 3 SAPPI trading offices and a forest products sales office. (SAPPI Annual Report, 2002).

Table 2.7 – Mondi: Anglo Forests production (ton)

Pulp	290,400
Graphic papers	509,800
Packaging papers	527,600
Corrugated board	275,000
Lumber	137,000
Wood chips	1,284,300
Mining timber	131,800

Mondi's involvement in the paper industry is extensive ranging from carton board, packaging, pulp and linerboard to recycling and forests. Mondi controls 563 000 ha, of which 200 000 managed for conservation, and the remaining 344 000 comprise 33% planted to pine, 58% planted to eucalyptus, and 9% to wattle. It has recently undertaken an extensive Durban Southern Industrial basin environmental management problems delayed the extension of the Merebank plant.

Direct employment in the industry is currently estimated at approximately 14 800 people in various pulp and paper mills. Approximately 60 000 forestry workers and transport contractors are employed directly for the growing and supply of raw materials. The sector has in recent years been adopting a number of measures to reduce people costs by shedding jobs (nationally and in KZN) largely due to the imperatives of globalisation, and related restructuring and rationalization to improve competitiveness. People related business costs have been further exacerbated by the skills levy, and impact of HIV on staff turnover. A national and KZN trend is that of outsourcing non-core activities such as maintenance, services, transportation, cleaning and catering. Opportunities for Black Economic Empowerment and SMME development have largely emerged through outsourcing of non-core operations and various programmes such as that of the small grower schemes.

2.4.2.1 Investment trends

The sector is extremely capital intensive with major investment in plant required every 10 years. Recent major investments in the sector underpin its expansion. Mondi Paper is in the process of upgrading the Merebank mill in Durban which houses five paper machines with output reaching over 500 000 per annum. The overhaul of the mills 80 000 tonne a year uncoated wood free PM2 and the expected increase in capacity of another 40 000 tonnes a year is intended to service both local and export markets. In addition, the plant is to see the installation of the 13 pocket A4 cutter, the third largest in the world, which will, once operational, double the mill's existing capacity. A key motivation of the project is the focus on low cost production near relevant markets.

A planned increase of the Richards Bay mills pulp capacity to a total of 720 000 tonnes a year, with present capacity at 575 000 tonnes, is also on the cards. The Richards bay investment will represent an investment of some R3-billion. In 2002, Mondi together with empowerment partner IL acquired the lease of 22,000 hectares previously part of SAFCOL to be used for eucalyptus plantations to supply the Richards Bay operations. The recent JV between Nampak and Norwegian firm has doubled plant capacity.

Further industry growth will be influenced by:

- The availability of fibre to be converted into value added paper products by increased afforestation, increased yields for research and development and increased recycling of used paper, availability of bagasse as a fibre source.
- The low specific consumption of paper and paper products in South Africa and Africa, which will grow as the per capita GDP of the continent, grows. In this context, initiatives such as NEPAD are a factor aiding growth of the sector. The demand for particular paper products will be dependent on the related growth of the sector in question (for example improvement in demand for coated fine paper depends on a sustained increase in advertising in the print media)
- South Africa's geographical location creates a window to maximize opportunity in Asia Europe and South America.

2.4.2.2 Factors constraining growth

Factors constraining growth of the sector includes high transport costs, declining infrastructure, drought in the 1990s, the slow granting of water permits, and a slowdown in plantings in recent years. Forestry's classification as a Stream Flow Reduction Activity under the National Water Act has resulted in a Water Resource Management Charge and an additional business cost incurred by the industry. In terms of the Act, new plantings necessitate a water licence and applying for one has cost implications. To address this constraining factor, industry has adopted a partnership approach to working with the national DWAF on detailing regulations.

In KZN, insecurity arising from communal land tenure is in part ameliorated by the ability of a local Inkosi to grant use of land to individuals, thereby giving the individual some security of tenure to plant trees and reap the harvest.

Business costs are negatively impacted by the power outages and poor quality of supply received by Eskom affecting production output. The high cost of capital investment, interest rates and depreciation constrain ability to invest in new plant and equipment.

2.4.2.3 Possible policy measures for government to support expansion of the sector

The paper and pulp industry is highly capital intensive. To attract the necessary investment, risk factors need to be ameliorated with appropriate investment incentives. A prerequisite is ensuring long-term security of supply of raw material and related security of tenure.

To increase levels of direct employment in the industry, new investment in forests and mills is needed. The Department of Public Enterprises has made land available for afforestation, with the intention of increasing opportunities for new entrants. This provides further opportunities for broadening the ownership base of the industry and promoting black economic empowerment.

Three specific areas of intervention are critical in this sector. First, government support for research focusing on tree breeding to improve yields will further give impetus to growing the industry. Second, the implementation of policy measures designed to trade savings in carbon emissions with those countries required to reduce their carbon emissions in terms of the Kyoto Protocol. Third, an integrated and partnership based approach by a range of public, private and civic bodies to address the environmental management problems arising from the Southern Industrial Basin in Durban

2.4.3 Petroleum

Petroleum refining accounts for 9.8% of KZN's manufacturing sector and has been growing at an average annual rate of 13.9% during the 1995 to 2001 period. This growth has largely been driven by the increase in petrol consumption associated with national economic growth and higher volumes of trade.

SAPREF (comprising BP and Shell) and Engen (Petronas) are the refineries located in Durban and jointly account for 42% of South Africa's production of liquid fuels. An issue that currently looms large for this industry is an initiative to reduce environmental pollution in the Durban South Industrial Basin (DSIB), where the refineries are located. The issue in the DSIB is that there is a mix of heavy industrial activity interspersed with dense community settlements. Hence the health of the 200 000 people residing in the area is compromised by the emissions from industries located there. The refineries are located in close proximity to the single buoy mooring (SBM), which facilitates the transmission of crude oil from ships through a pipeline to the refineries. Hence they are not able to relocate.

The initiative to curb pollution in the DSIB is termed the "South Basin Multi-point Plan" and is being driven by an intergovernmental coordinating committee comprising national, provincial and metropolitan government under the leadership of the Department of Environmental Affairs and Tourism (DEAT). The issue is, naturally, highly emotional. Moreover, it is difficult to solve because the output of the industries located there accounts for some 8% of South Africa's GDP. Measures to reduce pollution will be costly and may compromise the competitiveness of industries located in the DSIB

One aspect of the initiative that has a direct impact on the petrol refineries is the adoption of EU standards for vehicle emissions – including the phasing out of lead in petrol and the reduction of sulphur in diesel – which the DTI has estimated will cost the industry R18-billion. The DTI, together with DME and DEAT are currently engaged in discussions with fuel manufacturers to find ways of meeting these standards economically.

2.4.4 Automotives and components

The modest average annual growth rate of 3.9% of this sector between 1995 and 2001 is linked to the performance of Toyota Motor Corporation (TMC), the only car manufacturing plant located in KZN. While motor vehicles and parts currently account for a mere 3.7% of KZN's manufacturing sector (or 0.9% of GGP), the current re-orientation of TMC's production to export markets – as it positions itself within global supply chains – suggests that it is likely to be a significant driver of GGP growth in KZN in future.

Until recently, TMC has had little exposure to export markets. In contrast to other motor vehicle manufacturers in South Africa, Toyota was not able to position itself to export to other markets, as the majority of its equity was held by South Africans, effectively preventing the parent company from allocating market share beyond the African continent. In 2002, however, the Japan-based parent company increased its equity in the KZN plant to 75%, making it the majority shareholder. This facilitated a re-orientation of production to export markets.

The KZN plant has targeted the Australian (right-hand drive) market as the initial destination of its exports. It currently has an order for 10,000 corollas, but aims to supply that market with 30,000 vehicles per annum. The European market will be TMC's next targeted export market as it expands its productive capacity.

In Appendix A, it is argued that the single most successful policy intervention by the DTI since 1994 has been the motor industry development programme (MIDP). Its success is attributed to its ability to position South Africa's automotive industry within global supply chains. TMC's recent export orientation makes it eligible for the incentives provided by the MIDP. The credits earned by exporting can be offset against import duties to enhance the competitiveness of vehicles produced for both domestic consumption and export.

The potential for job creation within TMC is limited, given the capital-intensive nature of motor vehicle manufacturing. The total staff complement at the KZN plant is 7,000. Of note is the fact that 350 new jobs were created to facilitate the expansion of production into export markets. TMC plans to establish a Toyota Academy of Learning in order to ensure that its staff has world-class skills.

In contrast to other local motor manufacturers, TMC's operations include ancillary production facilities for the manufacture of components. This has an important impact on employment creation as evidenced by the fact that 1425 of TMC's employees are involved in component manufacture. A new facility – Cataler SA – was established in 2001 to manufacture catalytic converters. TMC's objective is to produce in excess of a million catalytic converters a year, most of which are destined for export markets. In addition, firms that supply components to TMC have invested in KZN in order to be in close proximity to their market. TMC has cooperated with these suppliers to enhance the skills of their employees and the quality of their products in order to meet TMC's extremely stringent quality criteria.

From the perspective of growth - and employment creation in particular – the key issue with respect to the automotives sector in KZN is the potential for the formation of an automotives and components cluster. At present, local content accounts for approximately 50% of the value of the final product. The intention is to increase local content to 70% by sourcing components domestically, rather than from Japan. In addition, TMC is exploring the opportunities for exporting components to Turkey, Thailand and Brazil.

In terms of provincial-level government interventions, the priority for this sector is to support the development of an automotives cluster, as this will enhance the competitiveness of both the car (OEMS) and components manufacturers. Moreover, it will generate employment and may lure other OEMs to KZN.

2.4.5 Food and beverages

The food and beverages sectors jointly account for approximately 15.2% of KZN's manufacturing capability. The food sector has contracted marginally at an average annual rate of -0.2% between 1995 and 2001, while the beverages sector has grown at an average annual rate of 3.6% over the same period. They are well-established sectors, located within well-developed supply chains in respect of both domestic agriculture and international markets. Despite large price increases (as high as 20% for some brands), attributed to exchange rate fluctuations, better than expected results were recorded for the industry in 2002. Traditionally, the industry experiences slow and steady growth in established brands. In contrast, rapid growth is driven by investment in innovation and the introduction of new products into the market.

The food processing industry is highly competitive. Historically, it has focused on servicing the domestic market by processing the domestically produced agricultural goods. The industry has, however, increasingly extended its product range to include high quality processed foods targeted at both the volume and niche sectors of the market. An important characteristic of the industry is that it is relatively employment intensive.

Demand is determined by population growth and changes in real per capita income. Growth in the food sector is thus very dependent on disposable income. In terms of government's impact on the industry, stimulatory budgets play a major role in strengthening the industry, as do provision of water and electricity because higher disposable income and access to basic services expands the range of products accessible to consumers.

The food sectors in which KZN has significant agricultural primary product available include livestock, poultry, dairy produce, sugar, maize and some sub-tropical fruits. The sugar industry, with a strong base of coastal sugarcane production in KZN, is an important contributor to the local food industry. Maize is also produced in KZN. The most developed area of tropical fruit production in KZN is bananas. Escourt, Pietermaritzburg, Hammersdale and Kokstad are the centres for the processing of meat and dairy products. Processing is carried out as near as possible to the production source because of the high cost of transporting unprocessed milk and animals. In the case of refined sugar cane production, five of the fifteen sugar mills carry out their own refining, close to where the sugar cane is grown, and the other ten mills send their raw sugar directly to the Tongaat Hulett refinery in Durban.

Meat processing is the largest sub-sector in food processing representing nearly 25% of total national output of the sector. It includes smoking, salting, sausage making, pickling, soup production, meat extracts, meat pies, canned meats and edible animal fats. Dominant KZN based brands include the Escourt brand, which processes mainly pork and a range of meat products, and the Rainbow Chicken Group, which is a world-class producer. Additionally, high quality beef and mutton is produced in the Midlands, Drakensberg region and East Griqualand.

The dairy products sub sector contributes approximately 7% to total local processed food output. It includes the manufacture of condensed, powered and evaporated milk, cream, butter, cheese, ice-cream and baby foods with a milk base. The quality of local products compares favourably with international standards. KZN is a major dairy producer with several established brands operating in the province (for example, NCD which is based in Pietermaritzburg).

Major food processing companies operational in KZN include the multinational Unilever, whose food division in Africa concentrates on spreads and culinary cooking products. Its South African division is located in Durban. Some of the group's leading brands in Africa include Rama, Flora, Blue Band, Royco, Knorr, Magnum ice cream, Hellmann's mayonnaise, and Liptons. The South African Head office of the Unilever operations is based in Durban. It operates four factories in KZN - a tea factory in Pietermaritzburg and three companies concentrating on spices, sauces and dressings located in Phoenix and Prospecton.

The sub-sectors of the beverage industry operational in KZN include malt and soft drink production. South Africa's major beer producer South African Breweries (also the majority shareholder of SA's largest soft drink bottler Amalgamated Beverages) has a large plant in Durban. In addition, a specialized small brewery at Nottingham Road in the Midlands, the Nottingham Road Brewery, produces four products in limited qualities. National Sorghum Breweries, the main sorghum beer brewer, has a brewery in Durban.

Other South African breweries service the KZN market through warehousing and distribution facilities. The soft drinks industry is dominated by Amalgamated Beverages Industries (ABI), which accounts for 40% of the national soft drinks market. It has the production and distribution rights for brands such as Coca Cola, Fanta and Appletizer. The company has a production unit in Durban.

A major international trend in the food and beverages sector is that of mergers and consolidation. In keeping with global trends, the South African Division of Unilever merged with local company Robertsons Foods in 2002, the biggest such merger in the food industry in South Africa. The merger brings together the international expertise of the Unilever Group with the Innovation and local knowledge of the Robertsons Group.

Associated with the trend towards mergers is a contraction of employment in the food and beverages sector across all occupational categories. While outsourcing of non-core operations has also been a trend in the industry, this is in traditional sectors such as distribution, merchandising, office service cleaning, catering and some manufacturing.

There is currently no substantial capital investment taking place in the industry. Investment is primarily in innovation, marketing and new products (for example, Liptons Ice Tea – a new brand introduced to the market in 2001).

Growth in the food and beverages sector is largely dependent on the overall growth prospects of the South African economy. Emerging trends will be that of increased out of home consumption of food, and an expected faster growth in the beverages sector than that of the food industry.

2.4.6 Clothing

South Africa's clothing sector is concentrated in KZN (especially Durban) and the Western Cape (Cape Town in particular), with some activity in the Free State. The clothing sector is one of the most labour-intensive industries in the world. Hence the contraction or expansion of output has a large impact on employment. The reduction of tariffs in this sector, coupled with pressure from retailers to reduce prices, has led to an apparent contraction of employment and output. In KZN, the data demonstrates that this sector has contracted at an average annual rate of 0.6% between 1995 and 2001.

This contraction is more apparent than real because the number of people employed in this sector in KZN has increased, but formal manufacturers have moved into the informal sector, de-registered from the bargaining council and become sub-contractors. This was done to reduce costs in order to compete with cheap imported clothing. It also explains why the statistics show a dramatic decline the output and employment of this sector.

Exposure to global competition has meant that specialisation and exporting is central to the survival of clothing firms. Economies of scale dictate that high volumes must be produced to reduce prices. Many KZN firms have taken up this challenge by operating as design houses by outsourcing the clothing manufacturing to small businesses and doing the design and marketing.

Preferential access for clothing to the US market within the framework of the Africa Growth and Opportunities Act (AGOA), provides an obvious export strategy for clothing firms. After much trial and error, KZN-based clothing firms have found their niche in the US market, after initially being deterred by the large size of the orders and the fact that the retailers wanted to supply their own designs. By exporting to medium-sized US retailers that require design services from the clothing manufacturers, clothing manufacturers based in KZN have successfully penetrated the US market.

The DTI's duty credit certificate scheme (DCCS, discussed in some detail in appendix A) is an additional support for clothing exporters. It enables exporters to accumulate duty credits when they export, which can then be utilised to rebate duties on imports. It is viewed by the industry as a powerful incentive to export.

Between 1996 and 2000, 39% of investment in this sector was destined for KZN, the largest proportion of aggregate investment going to any single province. New investments in knitwear capacity were also disproportionately large in KZN, while contracting in the Western Cape and the Free State. In aggregate, the spread of investment across the country in this sector demonstrates that it has been contracting in the Western Cape while expanding in KZN.

Industry experts are of the view that KZN is a relatively more attractive location because of its low cost structures and the fact that much of the labour force is not unionised. Moreover, proximity to the Port of Durban is an obvious advantage for exporters.

There is much controversy about the informalisation, casualisation and sub-contracting that has characterised the clothing industry over the past few years. While some view this as a "race to the bottom" because those working in the industry are worse off, others see it as the emergence of a lower cost, more flexible network of production.

Clearly, if KZN-based clothing manufacturers had not gone this route, many jobs would have been lost. The expansionary trends in the industry are a strength on which to build. Success in exporting to the US is the key to further expansion of the industry, given that domestic demand is limited by slow national growth.

2.4.7 Textile

The textile sector had undergone a substantial contraction since trade liberalisation commenced in 1995. In KZN, it has shrunk at an annual average rate of –6.2% per annum during the 1995 to 2001 period. In aggregate, the industry has contracted by almost 40% between 1995 and 2001. The reduction of tariffs on textile products, together with duty rebates in terms of the DCCS has resulted in substantial import penetration in this industry.

Interviews with industry experts point to the fact that the trends in KZN are driven by firm closures and the contraction of the output of firms that remain operational. Sasol Fibres and Mooi River textiles are two notable examples of textile firms that have recently closed down.

The textile sector in KZN accounts for 53% of South Africa's yarn spinning capacity, 45% of weaving capacity and 24% of fabric knitting capacity. Textile firms in KZN play both dominant and secondary roles in the supply chain. Frame Textiles is the biggest textile company in South Africa and is involved in spinning yarns, weaving and knitting fabrics, dyeing and printing, and the production of household and industrial textiles. There are other firms that do only spinning, weaving and knitting, and the finishing of the fabrics.

Textile firms historically located in KZN (Durban, in particular) to be close to ports as it is easier and cheaper to transport the raw cotton in bales from inland than to transport finished goods from inland to the ports. These factors are also applicable to the Western and Eastern Cape, where the balance of textile manufacturers is located.

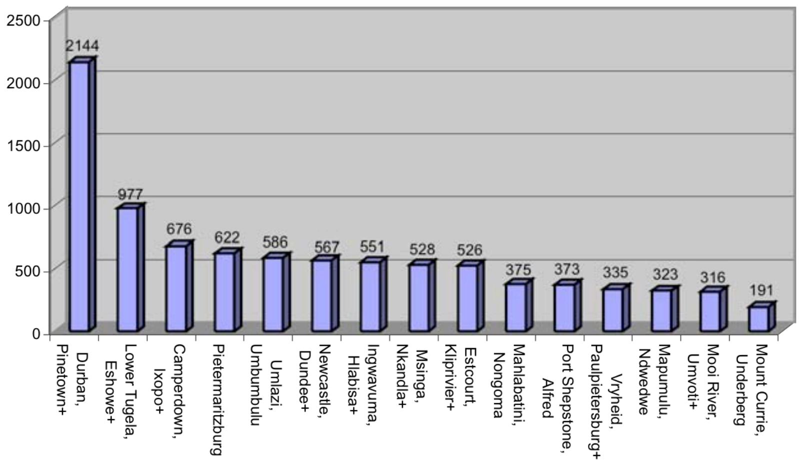
In a context of import penetration and the slow growth of domestic demand, the survival and expansion of this sector in KZN is highly dependent on a successful export strategy. AGOA is the key for the realisation of such a strategy, as clothing exported to the US must be made from yarns and fabrics produced in Sub-Saharan African countries. Not only is South Africa one of the approved supplier countries, it is also the only country in Africa with sufficient capacity to supply fabric at the required scale and quality.

In terms of the KZN government's support for this industry, the priority is to assist it to penetrate the US market by supplying textile to clothing manufacturers in South Africa and other African countries whose final products are destined for the US, in terms of the preferential market access afforded by the AGOA.

2.5 Spatial distribution of economic activity

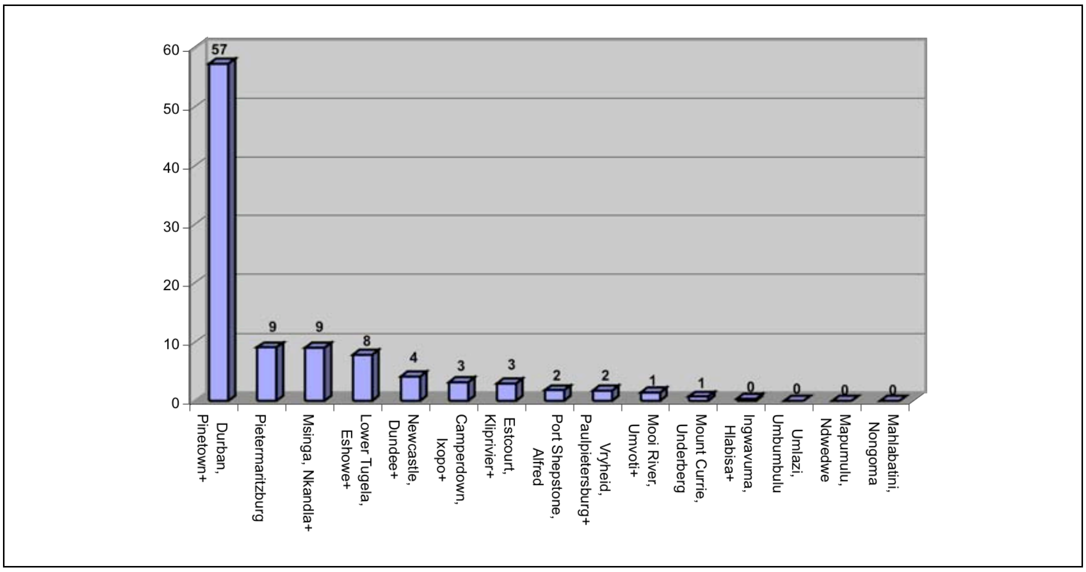
As is the case in the broader South African economy, in KZN economic activity is concentrated in three centres: Durban, Pietermaritzburg and Richards Bay. As illustrated in Figure 2.19, 2.14 million (24%) of KZN's population reside in Durban; 977,000 (11%) in Lower Tugela, Eshowe (the Richards Bay area); 676,000 (7.4%) in Camperdown, Ixopo and 622,000 (6.8%) in Pietermaritzburg. The remaining 51% of the population are scattered across the other 10 statistical regions.

Figure 2.19 – Population by statistical region, 2001



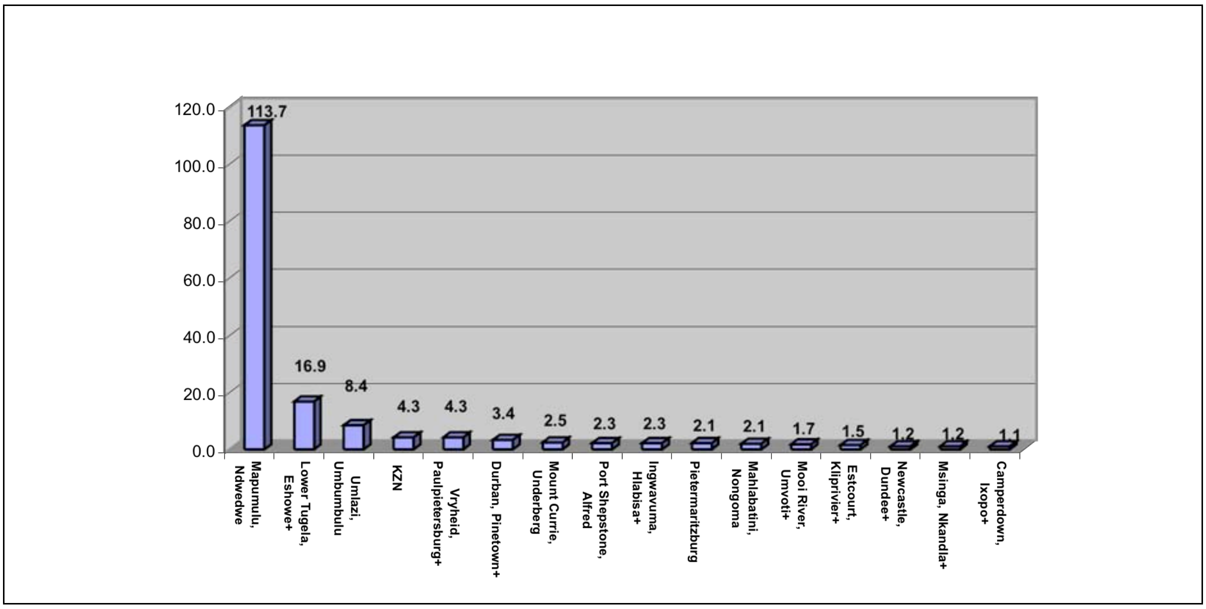
As is the case with KZN's population, the spatial distribution of economic activity is highly concentrated in the Durban, Pinetown area which accounts for 57% of KZN's GGP. The only other significant areas of economic activity are Pietermaritzburg (accounting for 9% of GGP), Msinga, Nkandla (accounting for 9% of GGP) and Lower Tugela/Eshowe (accounting for 8% of GGP) (see Figure 2.20).

Figure 2.20 – KZN distribution of GGP: 2001



Average annual growth rates of GGP per statistical region are depicted in Figure 2.21. It illustrates that in the four urban areas where economic activities are concentrated, only one (Lower Tugela, Eshowe) is growing faster than the KZN average of 4.3% per annum during the 1995 to 2000 period. Indeed, Durban grew by 3.4% during this period, with Pietermaritzburg and Masinga lagging behind at 2.1% and 1.2% respectively.

Figure 2.21 – KZN average annual GGP growth by statistical region, 1995- 2000

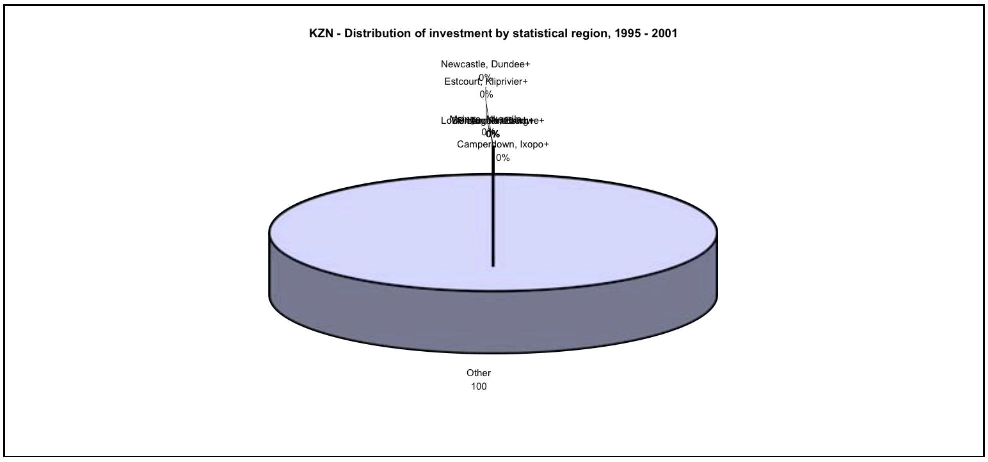


The Mapumulu, Ndwedwe statistical region experienced a spectacular growth rate of 137% per annum over this period, as a consequence of a R60-million investment in a magnet production plant by Tridelta. The growth rate is spectacular because the region was previously extremely depressed. Other high growth statistical regions are Lower Tugela, Eshowe (i.e. the Richards Bay area) with an average growth rate of 16.9% and Umlazi, Umbumbulu with a growth rate of 8.4% per annum.

In the case of Richards Bay, the buoyant growth of the local economy may be attributed to R28.4-billion in gross capital investment between 1995 and 2001. This investment was mainly to support the development of the aluminium cluster that is developing in that area with investment flowing to, inter alia, the following sectors: chemicals (R14-billion), non-ferrous metals (R8.7-billion), transport & communications (R3.7-billion), mining & quarrying (R1.9-billion), and paper & paper products (R1.1-billion).

In terms of investment during the 1995 to 2001 period, the pattern of concentration in three urban centres evident in indicators of economic activity is reflected in this key indicator of growth. Durban attracted a massive 57% of investment flowing into KZN during this period, followed by Lower Tugela/Eshowe (i.e. Richards Bay) with 10% and Pietermaritzburg and the Msinga, Nkandla statistical regions with 8% each (see Figure 2.22.).

Figure 2.22 – KZN distribution of investment by statistical region, 1995 - 2001



The spatial distribution of economic activity within KZN, highlights a key challenge for the provincial government: to encourage the development of economic activity beyond the metropoles of Durban, Pietermaritzburg and Richards Bay.

2.6 Nodal developments

Spatial development initiatives (SDIs) and industrial development zones (IDZs) constitute the two policy instruments of national government to promote regional economic development. Responsibility for the implementation of the SDIs has recently been transferred from national to provincial and local governments. In the case of IDZs, their designation and creation is the responsibility of provincial and local government. Consequently, SDIs and IDZs are central policy instruments of the KZN government for promoting nodal developments.

The following nodal developments are currently being implemented in KZN:

- The Lubombo SDI;
- The Richards Bay SDI;
- The Pietermaritzburg-Msunduzi SDI;
- The Dube Trade Port IDZ; and
- The Richards Bay IDZ.

In addition, the DEDT is promoting the following nodal developments:

- A number of industrial properties in rural and peri-urban areas in KZN, that are owned and managed by Ithala; and
- The South Coast initiative, aimed at strengthening tourism in the area.

Before providing an overview of these nodal developments, it is necessary to contextualise them within the framework of national government's industrial policy. Spatial policies are, in essence, supply-side measures that target particular geographical locations and provide a range of support measures to develop industrial capacity or build on existing capacity. In the context of industrial policy, spatial development initiatives (SDIs) and industrial development zones (IDZs) have been the key instruments to influence the spatial distribution of industrial activity. They are a means of achieving greater geographical equity in the spread of economic activities and investment. They are also a way of focusing resources on select locations, where opportunities are identified within this spread.

The DTI initiated the Spatial Development Programme (SDIs) in 1996, with the aim of developing regions with inherent economic potential that were under-resourced due to apartheid spatial planning. Ultimately, the aim was to build interest in new economic activity and areas: this would be done by identifying opportunities and eventually generating regional sites/clusters of economic agglomerations and so a virtuous circle of development would ensue. Private sector investment would be crowded in by a range of public interventions, including infrastructure provision, institutional de-bottlenecking, promotional activity, the identification of investment opportunities, and the facilitation of investment in anchor projects to support further investment resulting in forward (or even backward) linkages. Three of the thirteen SDIs are located in KZN.

In the case of IDZs, their explicit aim is to attract export-oriented investment, both foreign and domestic. The DTI designed them with the aim of "generating sustainable local and foreign direct investment while creating employment, encouraging skills and technology transfer, encouraging the participation of small, medium and micro-enterprises, and increasing foreign exchange earnings" (DTI, 2002).

IDZs (which are being implemented three decades after they became popular policy tools in other developing countries) differ from the orthodox EPZ model of export zones primarily in that the incentives offered are much more limited and they are not exempt from the labour laws that prevail in the domestic economy. Like the orthodox EPZ model, however, they are confined to specific spatially designated, fenced-in areas, minimise the bureaucratic red tape associated with investment and trade and allow duty free importation of goods used for export. A further, and significant, incentive offered in IDZs is that they are exempt from VAT where inputs are sourced from the domestic economy. As well as widening the cost of domestically produced inputs between firms based in IDZs and those located in the domestic economy, this incentive serves to foster backward linkages into the domestic economy. Although the promotional material for IDZs highlights access to additional incentives such as the

Strategic Investment Programme (SIP), the Small and Medium Enterprise Development Programme (SMEDP), the Critical Infrastructure Fund and the Skills Training Programme, these incentives are available to any firm that meets their criteria and hence do not advantage firms locating in IDZs relative to those based in the domestic economy. Moreover, the exemption from import duties for firms located in IDZs is also available to export-oriented firms in the domestic economy through the DTI's 470.03 rebate scheme as well as the Duty Credit Certificate (DCC) scheme which applies exclusively to the clothing and textiles sector and the Motor Industry Development Programme (MIDP) which makes provision for duty drawbacks for firms exporting in the automotive industry. Hence, in strict definitional terms the only incentive that is particular to IDZs is VAT exemption from domestically sourced inputs.

Their effect is, however, unequivocal: they significantly reduce disincentives to produce for export rather than for the domestic market. While this is an important incentive for export-oriented firms, it may not result in new investment (including FDI), because relative to other economy-wide incentives, the only quantifiable incentive is VAT-exemption. This, in turn provides a competitive advantage only if domestic inputs are utilised.

As a policy instrument – in addition to exemptions from VAT and customs duties and subsidised infrastructure – IDZs offer a competitive advantage to firms locating there by virtue of their potential to create agglomeration economies. The creation of a one-stop administrative centre to facilitate approval and permitting processes, together with a dedicated customs office providing inspection and clearance services is likely to substantially reduce the time and transaction costs associated with production and trade and hence bolster the competitiveness of firms located in IDZs.

The agglomeration economies that are likely to occur within IDZs as a consequence of a large number of firms within the same cluster, industry and/or sector being located there, provides a further incentive (albeit unquantifiable) for firms to locate in IDZs. In particular, it provides a platform from which to access resources from DTI (for example, the Strategic Investment Programme (SIP), the Small and Medium Enterprise Development Programme (SMEDP), the Critical Infrastructure Fund and the Skills Training Programme) designed to bolster export competitiveness.

The final, but probably most important, advantage offered by IDZs is their proximity to key transport nodes, as this will enhance competitiveness by reducing both transport costs and the lead-time required to transport goods to seaports and airports.

Five IDZs (two of which are located in KZN) have, to date, been proposed and are provisionally moving forward: Coega, East London, Dube, Richards Bay and the Johannesburg International Airport (JIA). With the exception of Coega (which is a greenfield development), an important shared characteristic of all the IDZs is that they build on existing manufacturing capacity and proximity to transport infrastructure in their various localities.

The establishment of the five IDZs identified to date has been driven by provincial governments in concert with local governments in a local economic development paradigm. In contrast to the SDIs, which were initiated and driven by national government, this is a significant feature of IDZs because the commitment of provincial and local government is key to their successful implementation. The viability of all the IDZs depends on the ability of their promoters to harness additional resources such as subsidised public finance for infrastructure and other incentives to attract investment.

This means that there will be competition among provinces for scarce government resources. The fact that public finance to the tune of R5.2-billion has already been allocated to Coega – on the one hand setting a precedent for other IDZs to request such resources, but diminishing the public resources available to them on the other – suggests that a coherent policy framework is required at the national level for the division of public resources among provinces. Given the difficulties encountered by government in spending budgetary allocations earmarked for infrastructure investment, however, IDZs present an opportunity for all tiers of government to collaboratively channel these resources to areas of high economic potential.

While provincial and local governments can hasten the granting of licences to commence with the establishment of IDZs, their success in attracting investment and fostering export-oriented production is dependent on a range of interventions that fall within the jurisdiction of national governments and state-owned enterprises. These include the restructuring of Portnet and Spoornet and the allocation of public finance for infrastructure essential to the success of IDZs.

The three SDIs and two IDZs at various stages of implementation in KZN are the central mechanisms for promoting economic development by encouraging inward investment, the expansion of existing industries and the creation of new industries. Each of these nodal developments is elaborated upon below.

2.6.1 Lubombo SDI

The Lubombo SDI is a cross-border development with Mozambique and Swaziland, to develop the area as a high profile eco-tourism destination. This SDI fits very well with the original criteria with resources underdeveloped as a result of Apartheid politics. The idea of a Wetland Park was the outcome of a highly contested process, debating proposals by Richards Bay Minerals to mine in St. Lucia. Ultimately, the application to mine was rejected, and the Natal Conservation Service was asked to develop an alternative eco-tourism proposal. This led to the proposal for a World Heritage Site, the foundation for the current development, which aims to establish the Greater St. Lucia Wetland Park (GSLWP).

The Lubombo SDI is centred on 3 phases: laying out basic economic infrastructure, investment facilitation, and the development of tourism supply chain activities (such as craft, tours, etc). The SDI has been very successful in garnering financial support for infrastructure and has moved quickly on implementation. The central programmes have included:

- Road upgrading;
- Tourism 'infrastructure', such as game stocking;
- Environmental rehabilitation to restore the wetlands;
- The cross-border malaria control programme;
- The unification of land title to enable development, in a context of 18 forms of private and public land holdings;
- The establishment of the GSLWP authority, to act as the local authority for the park;
- The packaging of sites for investor interest; and
- The facilitation of small scale economic activity, primarily centred on craft

The SDI has been successful in most of these activities, and there is clear evidence of forward movement. The SDI's ability to attract new investment still needs to be tested. In fact, even if the SDI is very successful in this regard, the main impact of these activities will be to raise occupancy of existing facilities in the area, raise earnings per bed per night, and open up sites on the sea. At this point, the existing businesses do not take advantage of cluster-based synergies, so the eco-tourist developments and 'branding' should help to consolidate economic activity in the area.

In this light, interventions focussed on assisting local businesses to collaborate for added efficiencies and better access, seems a strategy worth considering. For example, some hotels are part of tourism routes, but these were initiated from entrepreneurs based outside Lubombo. Some participants report feeling isolated and having difficulty shifting forward without assistance: this should be a key area of intervention.

While the intention for the SDI was to develop agriculture-linked activity in tandem with tourism, most work has been done on tourism development. Most significantly, the SDI developed a very useful analysis of potential agriculture development on the Makhathini Flats. This could potentially generate more new jobs and earnings than the GSLWP. However, hotly contested land claims weakened political support for the initiative and it was shelved. A very unfortunate result, since this is top grade arable land. It is therefore uncertain why organisational and political resources cannot be applied to unlocking the potential in the Makhathini Flats.

Overall, national government intervention, in this case the Department of Environmental Affairs and Tourism, along with the DTI, has played a useful, if limited role in an under-resourced area.

2.6.2 Richards Bay SDI

Richards Bay was developed from the 1970s as a location for the handling of bulk commodities, extracted in the region. The deep-water port was built to handle bulk cargo, and handles more than half of SA total sea faring cargo. The main challenge for the SDI in Richards Bay was to promote more downstream production in the region. Most employment is generated through large, short-term construction projects and 'side-stream' multipliers in services. The larger minerals investments are already attracted to Richards Bay and mainly need the kind of local support that is provided by an effective local council. Many of the projects had already been identified, since the local community is relatively sophisticated in terms of needs awareness and institutional development.

The central SDI projects focused on infrastructure upgrading, local institutional development and the promotion of small and medium scale downstream processing:

- The central infrastructure projects included:
    - The upgrading of the John Ross Highway;
    - The addition of a container terminal at the Port;
    - The privatisation of the airport; and
    - A smoothing of power for smaller industry.
- The central institutional projects included:
    - Police station upgrading;
    - The establishment of an Investment Centre;
    - The establishment of an IDZ; and
    - The mobilisation of finance for SMMEs, with a credit line of R1-billion organised through the European Investment Bank (also partly aimed at water supply projects).
- The central investment promotion projects included:
    - The aluminium cluster development, including the promotion of both small and large initiatives, in cooperation with Billiton; and
    - A variety of smaller projects in charcoal, furniture, aquaculture/ hydroponics and recycling.

This SDI has had a positive impact according to all participants interviewed. However, its full impact is yet to come - it must be recognised that downstream production multipliers and linkages can take many years.

The levels of national intervention, however, may not have been sufficient and a lack of policy support may have implemented the implementation of specific projects. The ability to expand downstream production over the longer term depends more on the delivery of central infrastructure projects and on other factors, than it did on on-the-ground SMME facilitation. So, for example, the inability of Portnet to install a container facility in RB has been a serious constraint on a town that is essentially outward oriented. Moreover, the wharfage charges continue to bias toward bulk cargo, as it was calculated on an ad valorem basis, therefore discriminating against higher value exports. So, it appears that the PM accomplished as much as might be expected in the absence of high-level policy direction from national government. For example, some of the demonstrable successes include the facilitation of the airport privatisation, the credit line for SMMEs, the establishment of the Investment Centre with high-level local participation, and movement forward on upgrading the John Ross Highway.

The critical forex-generating investments seem to be moving ahead, and RB attracted considerable investment in mega projects in the 1990s. Downstream production need not necessarily take place in RB. National government's role could entail unblocking central institutional and pricing problems related to the logistics parastatals, as well as other infrastructure delivery. Otherwise, RB appears to be sufficiently resourced to finance its own small Investment Centre, facilitating local institutional and infrastructure development.

2.6.3 Pietermaritzburg-Msunduzi SDI

The Pietermaritzburg Msunduzi SDI aims to develop globally competitive industries in the footwear, wood products and furniture, aluminium and local tourism sectors in order to create sustainable wealth and employment. It aims to combine public and private resources to secure sustainable development, based on the realisation of the competitive and comparative advantages offered by the area. It further aims to achieve this through the establishment of clusters, and the promotion of investment projects. The SDI has focused on unlocking projects in the sectors outlined below.

The footwear industry is the single largest manufacturing employer in Pietermaritzburg, employing some 4,800 people. KZN is a major contributor to the production of footwear in South Africa. South African footwear manufacturers are generally not export orientated due to the difficulty of competing with the low cost, high volume producers in Asian countries and the high quality producers of Europe. Due to an inability to export in the past, the production of components and materials for the local market only was seen as not viable. A range of components and synthetic materials for the manufacture of footwear are therefore imported.

The potential exists for South African footwear manufacturers to produce for certain niche markets, viz. men's leather footwear, protective footwear and other uniquely South African products such as the 'leather veldskoen'. With the world markets open for South Africa the viability of producing footwear components and materials locally and exporting it specifically to manufacturers in the rest of Africa could also be reconsidered.

With the number of large and small footwear industries in the borders of the Msunduzi Municipality utilising leather either imported or brought in from other parts of the country, the opportunity arises for the creation of small niche tanneries including an 'upper' leather tannery and a business park for small shoemakers on land at Khan/Old Greytown Roads to supply specific leather needs to the footwear industry. The DTI is at present investigating the possible location of a leather tannery in Pietermaritzburg.

The wood products and furniture industries together employ 2,370 people. The linkages in the cluster are weak, and the individual industries viz., sawmilling wood panel manufacturing, fixtures, fasteners, are poorly developed. There is scope for the upgrading of products if they are to become globally competitive.

The aluminium industry comprises 112 companies employing a total of 3,448 people. Much of the industry is capital intensive, but there are opportunities for small businesses, particularly in the sub-contracting field. There is a clear absence of upstream and downstream activity, including painting, anodizing, design, training and information systems. The advantages presented by close proximity to material suppliers are outweighed by poor technical support and long lead times. Studies have identified possible viable projects as being tubes and side plates; packaging; building, construction and factory transport; camping equipment. However, a lack of good engineering and artisan skills in the province is an inhibiting factor.

The local tourism industry presently caters for some 1 100 beds, with the opportunity to encourage at least one new hotel, a bush and tented camps. A number of potential tourism opportunities have been identified including the Bisley-Mkondeni valley eco-tourism Initiative, the development of Oribi Airport and management concession, Freedom Square development, the Msunduzi Waterfront, possible restaurant and museum at Worlds View, the Gandhi statue trading site, and the possible development of a long distance bus terminal - linked to the footwear industry.

2.6.4 Richards Bay IDZ

The Richards Bay IDZ forms par of the SDI and builds the locality's industrial capacity in dominant sectors of the KZN economy including non-ferrous metals, industrial chemicals and paper and paper products. The following companies currently undertake these activities:

- Billiton: Hillside and Bayside aluminium smelters;
- Richards Bay Minerals (RBM): producing heavy metals;
- TICOR/IHM: producing heavy metals;
- RBCT: the world's largest bulk coal terminal;
- Mondi Paper: manufacturer of paper;
- Bell Equipment: manufacturer of heavy duty articulated dump trucks; and
- IOF: manufacturer of phosphoric acid for fertilisers.

The key industrial focus of this IDZ is to attract investment into activities to beneficiate the output of established resource-intensive industries (in particular, the aluminium smelters) in Richards Bay. The Industrial Park to be established will house manufacturing operations that beneficiate intermediate products such as aluminium, zirconium, titanium, rutile, high-quality pig-iron, timber, coal, sugar, paperboard, phosphoric acid and water. In physical terms, the IDZ will comprise an office complex, an industrial complex, a hi-tech complex and bulk services infrastructure.

It is deemed to have a strategic economic advantage because the beneficiation of aluminium, ferrochrome and high quality pig-iron is geared towards the manufacture of components for the automotive and machinery industries, which have been identified as growth sectors. Moreover, the proximity of the IDZ to the aluminium smelters (Bay-side and Hillside) allows for hot aluminium to be transferred from the smelter to the manufacturer, resulting in significant energy cost savings to the IDZ tenants.

It also coheres with the national imperative of promoting SMMEs and BEE. The SDI Investment Centre is facilitating the establishment of an aluminium cluster comprising SMMEs and BEE consortia to manufacture household goods from aluminium. As these products will be supplied to domestic retail outlets, which currently import them, they are expected to have cost benefits to consumers due to stabilised pricing.

In order to forge linkages with agricultural activity taking place in Northern KZN and the hinterland around Richards Bay, the intention is to establish a wood-processing complex within the IDZ for the manufacture of furniture and building wood products.

The success of the Richards Bay IDZ is dependent on:

- The provision of public finance for bulk infrastructure;
- A commitment by the three tiers of government to upgrade the John Ross Highway linking Richards Bay and the N2 highway as well as the surrounding towns of Empangeni, Esikhaweni, Vulindlela, Ngwelezani, and Nseleni; and
- Upgrading the Port of Richards Bay as soon as there is evidence of increased demand.

2.6.5 Dube TradePort IDZ

The Dube TradePort (DTP) IDZ is the DEDT's most critical policy instrument for integrating KZN within the global economy and generating multipliers at a scale that will create sufficient employment and growth to significantly enhance the province's prospects of redressing poverty and unemployment.

The IDZ will be located at La Mercy, within the Durban Metro area on a site of 3 000 hectares. It is positioned to take advantage of the logistics infrastructure provided by the Port of Durban, King Shaka International Airport, and the rail and road links to the inland port at City Deep in Gauteng. The intention is to attract enterprises to the zone that are positioned within global supply-chains by creating a value added logistics platform. Of the five proposed IDZs, the DTP is unique in that it offers a location with close proximity to both a seaport and an airport.

A core aspect of the DTP IDZ is the establishment a CyberPort that will facilitate virtual buying and selling transactions related to the productive capacity of the enterprises located in the IDZ and beyond (as it will become part of a national logistics platform). A further innovation is the development of high-value organic farming projects which can utilise the airport to export perishables to high value markets in the EU and US. This will create employment in KZN's labour-intensive agricultural sector. This objective will be pursued through the creation of a pilot organic operation within the IDZ.

Although a defined industrial cluster has not yet been identified to populate the IDZ, the intention is to provide an environment in which both high technology projects in the field of electronics, biotechnology, and advanced manufacturing as well as labour-intensive agricultural activities can enhance their international competitiveness by locating within the IDZ.

In terms of the development impact of the DTP, it has been conservatively estimated that 15,000 direct jobs will be created within the first 10 years of its operation. A further 45,000 indirect jobs should also be created in this period.

The implementation of the DTP IDZ will take the form of a public-private initiative through the creation of a Special Purpose Vehicle (SPV). The SPV will incorporate, among others, Ithala, representatives from the KZN province and the Durban Unicity.

2.6.6 Ithala's industrial properties

Ithala's Property Division manages over 1 million square metres of factory space, much of which is located in the rural and peri-urban areas of KZN and geared to servicing businesses whose main market is emerging markets. Details of the location and utilisation of this factory space is attached as appendix B. There are 70 mini-factory industrial complexes specifically designed to house Somme's, sited at Bhongweni, Donnybrook, Empangeni, Esikhawini, Ezakheni, Gamalakhe, Gezinsila, Hammersdale, Hlabisa, Imbali, Ingwavuma, Izingolweni, Kokstad, KwaMasane, KwaMashu, Ladysmith, Madadeni, Mandeni, Magabheni, Manguzi, Maphumulo, Mbazwana, Mkhuze, Mondlo, Mpendle, Mpophomeni, Ncotchane, Nkandla, Nondweni, Nqutu, Nseleni, Osisweni, Ozwathini, Phungashe, Pietermaritzburg, Tugela Ferry, Ulundi, Umgababa, Umlazi and Wembezi.

Commercial Properties include shopping centres and office blocks designed for the businesses looking to access emerging markets. These are detailed in the table below. This division of Ithala is acting as a prime lever for SMME development while simultaneously functioning as a facilitator of Black Economic Empowerment for smaller firms. The spread of investment across the portfolio of shopping centres is consistent with the expansion of retail activities close to residential nodes hitherto less than adequately serviced.

2.6.7 The South Coast initiative

The South Coast, visited by more than 2 million domestic and 65,000 foreign tourists per annum, relies heavily on tourism as a form of economic activity. Proposed projects to further strengthen tourism in the area include the proposed Hibberdene marina, the Umzimkulu Game reserve and the Port Shepstone Marina & Golf Estate.

The proposed Hibberdene marina is a private sector project driven by local landowners supported by the Ugu District Council and Hibiscus Tourism (the district tourism office). The project concept includes the proposed development of a marina and linked property development requiring an estimated R1.5-billion to R2.5-billion investment. It is assumed that the proposed Hibberdene yacht basin and marina would house 350 yacht berths enabling sailing between Durban and the South Coast. The concept plan incorporates associated developments including a yacht club, 18 hole golf course, beach resort, water front villas, a 100 bed hotel operational on a timeshare basis, shopping and entertainment and tourism facilities. The required Environmental Impact Assessment, funded by the Ugu District Council, is currently being undertaken. The project initiators have entered into consultation with Spoornet to move the railway line, which abuts the land. The Department of public works have been approached to sell vacant land, which abuts the proposed development to the local landowners. The project initiators are further seeking funding for the conducting of Financial Feasibility of the project. The main market for the project is considered as international investors.

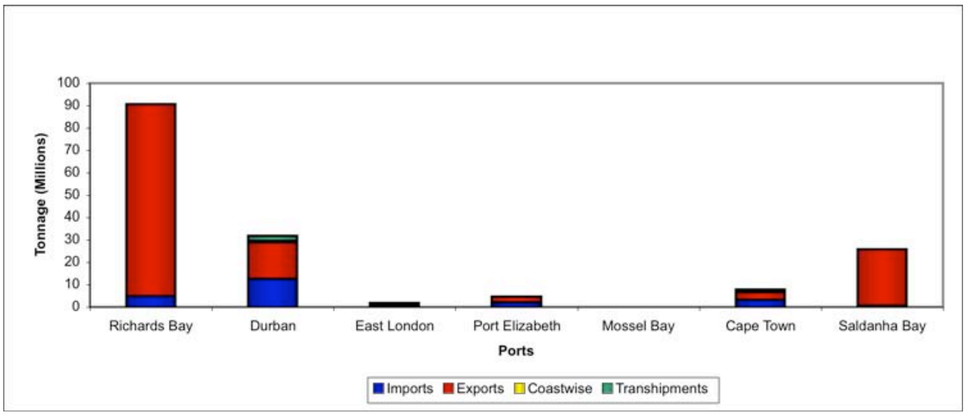
A joint initiative between local communities and private investors is planned for the establishment of a 30 kilometre big-five game reserve in the Umzimkhulu River valley. The proposed Umzimkulu Game reserve is supported by the DEDT, the Ugu District Municipalities and local tribal authorities. The project concept includes an upmarket hotel, conference facility, lodges, hutted and tented camps access infrastructure and internal roads. The main market for the project is likely to consist of both foreign and domestic tourists. The budget for the entire project is R5-million to R7-million. A pre-feasibility study has been completed which includes, mapping the perimeter fence lines once a workable boundary line has been demarcated, consultation with tribal leaders and surrounding communities, making recommendations on the siting of park facilities and the mapping of proposed accommodation, training and veterinary facilities.

A R550-million concept plan has been developed for the establishment of a marina and golf estate at the mouth of the Umzimkulu River which would include the Umzimkulu South Wharf with potential developments including a Budget Hotel, Shoppertainment Complex, Commercial offices, townhouses, apartments, and a Port Shepstone Beach front theme park. This project is however constrained by the fact that the harbour mouth is not suitable for a harbour development.

2.7 The role of the ports of Durban and Richards Bay

A key competitive advantage of the KZN province is the logistics platform it offers by being home to the ports of Durban and Richards Bay. As illustrated in figure 2.23, in volume terms, in 2001 Richards Bay handled 56% of South Africa's cargos (of which 95% was bulk and 5% break-bulk), while the port of Durban handled 20% of cargoes (of which 24% was bulk, 25% break-bulk and 51% containers). The Durban Port handles 65% of South Africa's sea-borne container traffic.

Figure 2.23 – Summary of cargo handled at the SA ports: 2001/02



The vast majority of imports and exports leaving and entering South Africa come through the ports of Durban and Richards Bay, which in volume terms account for 72% of imports and 75% of exports. Richards Bay handles higher volumes (63% of exports and 20% of imports) but lower value goods, while Durban handles lower volumes (12% of exports and 52% of imports) of higher value cargos.

Notwithstanding the fact that the minerals sector (which historically represents the heart of the South African economy) is primarily located in Gauteng, the low share of GDP emanating from the KZN province is surprising in light of the competitive advantage offered to manufacturers exporting or utilising imported inputs of locating closer to these ports.

2.7.1 The port of Richards Bay

Prior to the mid-1970s, the port complex of Richard's Bay was a large natural lagoon, home to the exuberant wildlife of the coastal region of Northern KZN. In April of 1976 the port was officially opened after being converted to a 19m deep man-made port. It is currently the country's largest exporting port, handling more than half of all cargo passing through South African ports.

The Port of Richards Bay has two terminals: a multi-purpose terminal and a dry-bulk terminal. The multi-purpose terminal is situated in the deep-water port of Richards Bay and is the product of the merging of two separate terminals, the Bulk Metal and Combi Terminals. The resultant integration of infrastructure and facilities has enhanced the terminal's ability to logistically manage a variety of cargo types, namely breakbulk, neo-bulk and containers.

The terminal serves the vibrant hinterlands of Kwa-Zulu Natal, Mpumalanga, Gauteng and even as far a field as Zimbabwe, with a strong emphasis on the export of raw and semi-processed materials. It handles the following commodities: ferro-alloys, steel, scrap steel, pig iron, aluminium, project cargo , granite, pitch coke, forest products, containers and loose bulk. Annual throughput of cargo is 5.6 million tons.

The dry bulk terminal is unique in that it handles multiple products over its conveyor system. This means that no conveyor (or 'conveyor' route) is dedicated to any one specific commodity. To avoid contamination, belts, transfer points, rail trucks and vessel loaders and unloaders require thorough washing after each loading/unloading of a parcel, before commencing the next product handling.

The National Ports Authority (NPA) has announced its intention to invest R2.35-billion in the Port of Richards Bay. The establishment of an additional coal terminal is expected to cost R350-million, while the establishment of a dry dock is expected to cost in the region of R2-billion. In terms of its medium-term capital budget, the NPA has made no commitment to establishing a container terminal in Richards Bay, despite evidence that it is constraining industrial development and is essential to the success of the IDZ.

2.7.2 The port of Durban

The Port of Durban is the busiest on the African continent and the biggest in terms of container capacity. It handles 31.4 million tons of cargo, valued in excess of R50-billion each year. It has four terminals: a car terminal, a container terminal, the Maydon wharf multi-purpose terminal and the Durban multi-purpose terminal.

The car terminal facilities comprise a 366m quay with a depth alongside of 10.9m, backed by 8.5ha of surface storage with logistical road and rail access, vehicle inspection facilities and administrative block with a state-of-the-art cargo tracking system, CCTV surveillance monitoring – all surrounded by floodlit security fencing. Its dedicated berth (Q/R), is able to accommodate the largest deep-sea car carriers, with an average of one call every two days

The present facilities, with a capacity of 3,500 vehicles (i.e. design capacity of 60,000 vehicles per annum), is inadequate to meet present and future demand, and plans are underway to create additional capacity for 3,000 vehicles in a three-storey parking garage within the terminal security perimeter, which will be directly linked to the quayside by a new bridge.

Imports of new cars from manufacturers all over the world arrive in Durban, as well as second hand vehicles destined for neighbouring countries. Exports have grown over the last few years, as a consequence of the Motor Industry Development Plan.

The Durban Container Terminal is the largest and best-equipped container terminal in the southern hemisphere. The terminal opened in 1977 and has experienced unfaltering growth from 6 000 containers handled per month in 1979 to the current level of more than 1.2 million TEUs per year.

Durban's location on the east coast of South Africa makes the terminal a pivotal hub for the whole of the Southern African region of the Indian and South Atlantic Oceans – serving trade routes linking North and South America with the Middle East, India, Asia and Australasia. The terminal also serves as a crucial interface for the distribution of cargoes between ocean carriers and the markets of South Africa, Botswana, Zimbabwe, Zambia and Zaire.

The Maydon Wharf Multi-purpose Terminal handles a variety of containerized, breakbulk and bulk cargo. Historically, the Maydon Wharf area has been home to a vast majority of privately operated terminals. The terminal operated by the Port Operation division of Portnet focuses on niche markets, specializing in the handling of specific commodities including: timber, salt, fertilizer and steel (including scrap steel).

The terminal also handles both import and export containers, handling on average 15,000 TEUs per annum with a potential to handle up to 30,000 TEUs per annum. Despite the focus on niche markets, the terminal has the resources to handle most types of break-bulk and neo-bulk commodities.

The Durban Multi-purpose Terminal is the largest general cargo handling facility in the Port of Durban and is directly involved in the logistical handling of breakbulk, certain bulk and containerized cargoes. The terminal operates across twelve berths and is the combination of two separate terminals, Point and Pier 1, situated on opposite sides of the port.

Despite its impressive scale, the Port of Durban is well below international standards in terms of its operational efficiency. This is widely attributed to limitations imposed by its geographical setting and the fact that Portnet operates most terminals, when the global trend has been to privatize cargo handling.

2.7.2.1 Restructuring the port of Durban

Two initiatives are currently underway to restructure the Port of Durban. The first, termed the *Port of Durban Development 2005,* involves the expansion of the port's capacity through investment and the re-engineering of the operations of the four terminals. The second, which is part of a broader project to restructure South Africa's entire ports system, involves the transfer of cargo handling (or port operations) from Portnet to the private sector through concessions. The intention is to fast-track this process with respect to the Durban Container Terminal.

The *Port of Durban Development 2005* project involves an investment of R1.34-billion (in 2000 prices) by the National Port Authority over a 4-year period. It involves three components. First, increasing the capacity of the Durban Container Terminal from 1.3 million to 1.6 million TEUs per annum. Second, the conversion of pier 1 (the multi-purpose terminal) into a container handling facility, will increase its container handling capacity by 325,000 TEUs per annum. Third, the City Terminal Development, which involves the construction of a new deep-water quay walls further into the bay through the reclamation of 20 hectares of land, in order to relocate the multi-purpose terminal (currently occupying Pier 1) there.

While this initiative will enhance the physical capacity of the Durban Port, it will not resolve a deeper problem – the inefficiency of the cargo handling services offered by Portnet's port Operations Division. At present, all container terminals in South Africa are operated by Portnet (compared to bulk and break-bulk terminals, where in excess of 50% of these terminals are operated by the private sector). The high *ad valorem* wharfage charges (which have been converted to unit based cargo dues since May 2002) and poor turn-around times with respect to cargo handling at South Africa's ports are a critical constraint to international competitiveness of South Africa's exports. Durban was close toe being categorized by international shipping lines as a congested port and urgent remedial action had to be taken to prevent this.

These inefficiencies are well documented and have been the subject of much lobbying to transfer cargo handling to private operators since democratisation in 1994. Indeed, it has been estimated that the Durban Container Terminal operates at 60% of the capacity of similar sized ports elsewhere in the world.

The current status of the restructuring project is that consultants have been appointed by the shareholder – the Department of Public Enterprises – to assess the manner in which the terminal should be concessioned. At issue is whether the scale of operations is sufficient to warrant more than one concessionaire. The consultants will present their report by the end of February, whereafter Cabinet will be expected to approve or reject their recommendations.

The complexity of the decision-making process within government, and the protracted nature of negotiations with stakeholders (in particular, organised labour) suggest that a concessionaire is unlikely to be in place before the end of 2003.

The introduction of a private operator will provide a major impetus for the KZN economy. In addition to bringing operational efficiencies in line with international best practice, it is likely to generate interest in back-of-port operations. International evidence suggests that that private operators often act as a catalyst for the development of manufacturing activities around their terminals.

The KZN provincial government should ensure that it provides the necessary support and direction to exploit this avenue for economic development to its fullest potential. Moreover, a world-class private terminal operator will greatly mitigate the risk of traffic being diverted to other ports, in particular Maputo and Ngqura.

2.7.3 Spoornet

The inefficiencies associated with transport logistics in KZN are not confined to its ports. The well-documented inefficiencies within Spoornet serve to undermine South Africa's international competitiveness. Cargo owners that use the rail service between Gauteng and Durban are of the view that these inefficiencies are the consequence of too few carriages, a lack of tarpaulins and antiquated equipment. This is exacerbated by the frequent theft of cargo and rails.

The inefficiency and unreliability of rail transport is evidenced by the fact that there have been a number of incidents of late delivery to Portnet, causing delays to shipping or even missed vessels. The cost of these transport failures is high, not only in monetary terms, but also because they affect South African exporters' reputation as reliable international suppliers.

Spoornet's inefficiency is a well-documented economy-wide problem that government seems unwilling or unable to address. Initiatives to restructure Spoornet – which is currently 100% government-owned under its holding company, Transnet – by introducing private sector participation were effectively thwarted by opposition from organised labour and management. Commitments on the part of Spoornet's senior management to improve the efficiency of its General Freight Business have also not been honoured.

Consequently, freight is increasingly being shifted from rail to road, at a great cost to government in terms of maintenance and regulation and at a great cost to the economy because of the negative externalities generated by road freight from pollution, congestion and accidents on South Africa's roads. The *status quo* is unlikely to change unless the crisis deepens. This is because the dialogue on Spoornet's restructuring has been confined to government (in its capacity as the shareholder), Spoornet's senior management and organised labour. Conspicuous in its absence is any representation of the views of rail users.

Spoornet's inefficiency and lack of customer-orientation will not be remedied unless there is a profound restructuring of the rail network that shifts some measure of ownership and management to the private sector. This is obviously a political hot potato. From the perspective of the Secunda cluster, the only way to address the logistics problem is to acknowledge that it is a political problem and lobby government to implement radical reforms in concert with other rail users.

2.8 The small, micro and medium enterprises sector

A myriad of complex regulations effectively prevented the entry of firms of this scale to many industries during the apartheid era. More to the point, the Apartheid government made most forms of black business ownership illegal. In a bid to reverse this legacy, government has dismantled these regulations and provided a range of financial and non-financial instruments to promote this sector.

In a context of high and growing levels of unemployment, the SMME sector remains an important source of job creation. This is because SMMEs are generally more labour-intensive than larger firms and hence have a higher labour-absorption capacity. The evidence suggests that employment growth in the SMME sector is not from the expansion of existing SMMEs, but from the formation of new micro and survivalist enterprises (Berry et al, 2002). As the majority of SMMEs operate in the non-traded sector, its growth is dependent on domestic demand.

However, a mere 6% of SMMEs use national government's financial and non-financial support programmes due to distrust of external agencies and incapacity to raise awareness about their existence and efficiency (Berry *et al*, 2002). This suggests that provincial and local government has to play a much more active role in promoting enterprises of this scale across economic sectors.

To that end, the SMME Chief Directorate of the DEDT actively promotes the SMME sector in three functional areas: sector Development, business development services and black economic empowerment. The latter is addressed in the discussion of black economic empowerment.

2.8.1 Sector development

A high proportion of SMMEs in KZN are located in the retail sector. Consequently, the SMME Directorate has undertaken the following initiatives to encourage SMME development in the manufacturing sector:

- The eThekwini Footwear and Leather Hub based in Umlazi;
- The Richards Bay furniture cluster;
- The Richards Bay aluminium cluster;
- Arts and Crafts producer development. A project has been established to develop a craft emporium to market products for local and international markets;
- The entertainment (film and music) industry. The DEDT sponsored programme is undertaken in partnership with the Bat Centre. Twenty-five trainees have benefited from training and capacity support in technical skills such as sound and lighting. On successful completion of the training programme, they are placed in established companies for further skill development;
- The automotive components cluster. The partnership initiative includes the Durban Metro, Department of Trade and Industry, DEDT and the MAC. It aims to enhance the competitiveness of the regional automotive manufacturing industry through co-ordination and facilitation of information sharing and joint activities. The DAC is underpinned by four business plans, each developed by industry representatives in conjunction with the facilitation services of KZN Benchmarking. Programmes implemented include an HRD Programme, Supplier Development Activities, Logistics, and Benchmarking; and
- Provision of support for the tourism sector activities undertaken by the MAC including provision of assistance to emerging entrepreneurs to design products and systems.

2.8.2 Business development services

The Directorate undertakes a number of activities designed to improve business development skills and build the capacity of SMMEs. Some of the innovative measures implemented by the SMME Directorate in KZN include the following:

- Management of the KZN Business Rehabilitation Trust Fund set up by the provincial legislature to address the concerns of small businesses devastated by political violence. The Trust Fund operates as a credit guarantee scheme whereby loans from financial institutions are guaranteed and a business mentorship programme implemented;
- Consultation with finance institutions;
- Encouraging SMMEs to develop a culture of savings by participation in community and village banking aided by the establishment of Village Banks;
- The development of policies that aim to support SMME development. Policy development is undertaken in partnership with the DTI and various government agencies;
- Providing strategic direction, information and capacity support to the Local Business Service Centre (LBSCs) Network that comprises sixteen LBSCs operational throughout KZN. In 2002 a study was conducted to determine the most effective mechanism to provide support to LBSCs to ensure quality services. The LBSC Network is funded by the Directorate, Ntsika and donor agencies;
- Support for Tender Advice services offered to SMMEs through the four Tender Advice Centres operational in KZN;
- Provision of support for the four Manufacturing Advisory Centres operational in KZN. The KZN Manufacturing Advisory Centre (MAC), which has four offices in KZN, plays an important role in all programmes undertaken by the DEDT;
- Co-ordination of the service provider's forum, the only such forum in South Africa. The forum is responsible for the provision of a basket of holistic support services to encourage SMME development. The forum is able to build close working relationships with government services and undertake joint programmes. In 2002 a programme was undertaken with the NPI to improve productivity levels and organizational capacity of SMMEs in KZN;
- Leverage resources from CSIR, SABS & NPI and international donors;
- Support business linkages in targeted sectors;
- Support training and capacity building of special groups such as women and youth; and
- Encouraging SMMEs to be export focused and adjust to opportunities and challenges in the international and global environment. This has included the provision of support to SMMEs attending SITEX, where the KZN SMME delegation won awards in 2002. In addition, SMMEs have been assisted to participate in foreign trade missions.

The SMME Directorate has also played a leadership role in developing SMME programmes in KZN, leveraging support from stakeholders and encouraging service providers to respond to challenges. The Directorate intends to strengthen its delivery capacity in 2003 by:

- Strengthening the support services provided to SMMEs in KZN including LBSC networks, tender advice centres, and expanding the KZN MAC to areas such as Richards Bay, Port Shepstone and Pietermaritzburg;
- Extending the levels of expertise in the Directorate in order to undertake qualified sector specific support activities. The 2003 financial year will focus on improving the human resources capacity of staff, and employing new staff; and
- Additional resources are required to implement programmes directed at youth enterprise development. The Directorate intends to undertake innovative partnerships with tertiary institutions to encourage the development of entrepreneurship and mentorship programmes.

2.9 Black economic empowerment

Black economic empowerment in KZN is likely to follow national policy and trends, particularly because the National strategy relies heavily on sector-focused strategies. The major sectors influenced at this time are the Liquid Fuels and Mining and Mineral beneficiation sectors, both in the process of finalising and implementing agreed goals and targets. Not all sectors will be the subject of charters in the future however.

Major movement on BEE can be expected where government disposes of any right, or grants a licence or enters into a partnership arrangement. In these events, an empowerment performance requirement will be agreed. This places new emphasis on the mechanism of Public/Private Partnerships (PPP's) and the ability of the PPP to deliver implementable solutions.

President Mbeki, in his state of the nation address, suggested that the BEE focus of the future would be on directing empowerment to new, productive investment rather than rearranging share ownership. Indeed, he noted that, "the government will lay greatest stress on black economic empowerment that is associated with growth, development and enterprise development and not merely redistribution of existing wealth".

The scorecard approach will be adopted, as will an outcomes-based approach, in the framework of a broad-based process covering ownership; management; employment equity; skills development; procurement; corporate social responsibility; investment and enterprise formation.

No data is available regarding BEE on a provincial basis. Data are not collected at this level and disaggregation of national data is often not possible. Many of the major sectors in KZN are considered global players upstream, specifically, Aluminium, Automotive components, Pulp and Paper, and as such, exhibit lower propensity for BEE at the equity level. For these sectors, BEE opportunities vest largely in downstream value added manufacturing activities, as well as in representivity at the decision making levels in the firm. Other sectors are characterised by the presence in the Province of subsidiaries of national or multinational firms. In consumer-focused sectors, opportunities for BEE in the first instance are typically found in distribution.

Much current activity is taking place, as can be expected, in the Liquid Fuels and the Mining and Minerals Beneficiation sectors, supporting the often stated assertion that it is where government has leverage that BEE will be implemented at an equity level. The area where this is most likely to be effective for KZN as a province is in the area of logistics and transport, since major assets in this regard are held by the state, and in the area of projects such as the Dube Trade Port IDZ, where government may similarly, through procurement policy, exert pressure. Tourism, as a resource based sector is similarly open to BEE but often requires shared investment strategies where Government invests in infrastructure, marketing, training and SMME support, and the Private sector invests in tourism plant, marketing, training and procures from Black owned SMMEs.

No statistics are available with regard to BEE other than at the equity participation level. The following represents a snapshot of activity in BEE, sourced from BusinessMap's BEE database, the BusinessMap Empowerment Index and various BEE Updates issued by The BusinessMap Foundation. All of these events will impact on BEE in KZN.

What is clear from this list is that the pace of BEE is speeding up, and the spread of BEE throughout the economy is increasing. The possible exception is BEE in the rural areas where some estimates (C Reddy, BusinessMap Foundation) suggest that since the vehicle for BEE in rural areas is largely the SMME or the co-operative, support for these entities is extremely limited and the failure rate is between 70% and 80% over a three-year period (Khula).

2.9.1 National[14]

A snapshot of the kind of BEE deals underway at this time in some of the sectors relevant to KZN indicates where the activity lies. The BusinessMap Foundation, which tracks and reports on these deals, notes that in the long term empowerment is likely to increase, driven by the Liquid Fuels and Mining Charters in the first instance. Empowerment groups have bought 67% of properties sold by the State, which made a profit of R114-million this year.

2.9.2 Liquid fuels

The Liquid Fuels Empowerment Charter has led to the industry's rapid transformation. Today, 14% of the oil industry is black owned. This represents 11% of operating profit. Government wants 25% of the oil industry to be in the hands of black South Africans by 2014 and oil companies have until 2004 to formulate policy on what empowerment means, how it is to be achieved and whether different types of empowerment will be recognised. Government will set aside 10% of every new gas exploration licence for empowerment companies.

[14] The information regarding BEE deals in this section is directly quoted by kind permission the BusinessMap Foundation © 2002

Excel Petroleum is an empowerment oil group that is likely to achieve a R3-billion turnover for 2002, giving it an estimated 7% of the commercial and retail market. The group has more than 130 franchised retail petrol outlets. The Strategic Fuel Fund has sold a shipload of oil worth between R150-million and R250-million to empowerment company Biz-Africa 1057. African Legend Investment, an empowerment consortium led by Mashudu Ramano, has acquired a 25% share in Caltex Oil SA. The deal is worth more than R4-billion in annual sales. Up to 100,000 taxi owners and operators have become shareholders in Caltex because of the SA National Taxi Council's involvement in the empowerment consortium. Finally, empowerment company Kulani Africa Gas plans to establish franchised natural gas filling stations to provide taxis and fleet industries with a cheaper fuel alternative.

2.9.3 Automotive industry

As regards the automotive sector, a survey conducted by Franchize Directions found that a number of black-owned outlets in the automobile industry would not grow robustly over the next few years. Government is trying to grow the number of small and medium-sized businesses run by HDSAs and some success has been achieved in this regard. One of the constraints, especially for KZN, is the global nature of the First tier suppliers to the OEMs, smaller businesses often begin entry as subcontractors to main suppliers due to very high quality requirements.

However, the Joint Supplier Council that represents leading car manufacturers believes that 30% of the local automotive components manufacturing industry will be black controlled by 2012. Empowerment firm ShikishaDira has formed a joint venture company, Shikisha Rubbers and Tyres, with US tyre manufacturer Goodyear worth R25-million. The company will supply tyres to rural areas. Black-owned investment company African Genesis Construction has acquired a 70% stake in Goodyear's South African distribution company Intertyre. The deal makes Intertyre the biggest black-owned tyre distribution company in South Africa

2.9.4 Services

Empowerment group Community Healthcare Holdings and Network Health Care Holdings (Netcare) have been awarded a R100-million contract to manage over 200 private beds and five operating theatres at Universitas and Pelonomi hospitals. New local empowerment passenger airline Inter Link Airlines has taken to the skies, offering a daily business-class service between Johannesburg and Cape Town. Transnet has sold 51% of its shares in ground-handling airport service company Apron Services to empowerment consortium Equity Aviation. The deal includes an opportunity for Equity Aviation to acquire a further 34% share if certain performance criteria are met.

Boitumelong Waste Services has formed a 50/50 joint venture worth R6m with Otto Industries SA, a subsidiary of Otto Holdings International, to create Otto Waste Systems. The deal will create over 100 jobs and give Boitumelong access to Otto Industries' resources.

In Tourism, a consortium including Metallon Corporation is buying all Global Resort's operations for about R1bn in loans and shares. The sellers are RMB Holdings, which held 48%, Genbel Securities with 26%, listed investment trust Aquila Growth with 23% and management, which held 3%.

2.9.5 Professional services

A new law regulating South Africa's accounting profession will accelerate the transformation of the industry by broadening the pool of professionals that may be registered as auditors. The Accountancy Profession Bill will replace the Public Accountants and Auditing Act. Black trainees are entering into the accounting profession in large numbers; today typically 40% of an auditing team is black and 50% female. However on a chartered accountant (CA) basis only 1,336 of the 17,000 CAs working in SA are black and only 253 of those are African. From a BEE equity point of view, PriceWaterhouseCoopers will merge with black-owned accounting firm Mokua & Associates.

Examples of BEE driven social responsibility projects are the R62-million Thuthuka project, which is aiming to uplift the maths and accounting levels of matric students in 288 Eastern Cape schools and the Courtwell Consulting project, where the property-training specialist firm will train 100 black unemployed graduates interested in the commercial property sector. Property loan stock company Spearhead Property Holdings and empowerment group Lukhanyo have formed a joint property trading operation. The venture, which aims to control assets worth R500m, will allow Lukhanyo to take a majority stake in the company

The Association of Black Securities and Investment Professionals (Absip), a member organisation of the Black Business Council (BBC), is working towards an empowerment charter in the financial services industry. Only asset managers with substantial empowerment credentials will be considered when government employees' pension fund assets are put out to tender.

In the ICT sector, many new BEE deals are emerging. Dell Computer Corporation's empowerment strategy includes investing into a number of empowerment programmes and launching the Dell SA Foundation, Digicore has successfully fulfilled large tenders with the Mpumalanga Health Department and several KZN government departments. The company is also well placed as the preferred supplier for the R4bn taxi industry overhaul and Comparex is actively searching for an empowerment partner.

Mulitconsult SA has signed a joint venture agreement with US multinational Paradyne Corporation. The deal will enhance the position of Multiconsult's subsidiary Multiconsult Technologies in the information and communications sector and ensure that skills transfer and exposure to the latest telecommunications technologies takes place.

Leseding Electronics Investment and Spescom Software (UK) have made a deal with empowerment group Tactical Software Systems that will allow eB document management software to be distributed in SA.

2.9.6 BEE in KZN

While KZN participates in national trends in BEE, there are specific interventions that occur at the provincial level. In the sugar sector, KZN's agriculture and environmental affairs MEC Narend Singh has requested that sugar cane producers get a stake in milling operations. South Africa's three largest milling companies, Illovo Sugar, Transvaal Sugar and Tongaat Hulett Sugar, have embarked on empowerment initiatives that include releasing land to emerging black farmers.

From the heavy industry perspective, Anglo Coal and BHP Billiton, the two largest shareholders in the Richards Bay Coal Terminal, have agreed to forgo their 6.5 Mt/year entitlement to make room for Sand Dune Coal Terminal members. In turn, the Sand Dune Coal Terminal will set aside 500,000 Mt/year of export capacity for empowerment companies and ensure that they receive no less that 50% of the Terminal's entitlement.

Large entities are beginning to crack down on attempts at fronting. Transnet cancelled a contract with black empowerment catering company Arejeng-Sinclairs, a joint venture between Arejeng Caterers and Sinclairs Signature Specialities, after Arejeng directors complained that Sinclair had been using the company as a front to secure the contract.

In the tourism sector, Wilson's Wharf, Durban's first waterfront development, has provided the training ground to fast-track BEE and is a springboard into the burgeoning construction industry in the Greater Durban area for 32 emerging contractors from historically disadvantaged backgrounds. The R25.1-million 4,200 square metre Wilson's Wharf opened to the public at the beginning of the Summer holiday season. The TKZN's ability to access R30-million from the National Department of Environmental Affairs and Tourism for projects that benefit historically disadvantaged communities during 2002 has further boosted BEE in the tourism industry. These projects are primarily based in rural KZN.

Advocate Trevor Hyman, a Durban-based entrepreneur (and HDSA) led an international consortium in the acquisition of 51% of the shares in ground-handling airport service company Apron Services. Those that were close to the transaction are of the view that its successful conclusion was due to Hyman's skill and tenacity in terms of both establishing the consortium (which includes world-class players in this sector) and navigating the consortium through difficult negotiations.

Ultimately, BEE in KZN will follow national trends. It can be stimulated downstream through PPP's with upstream firms to support downstream development in value added manufacturing and services, and by a focused education and training strategy and delivery on the part of the Province and in partnerships with Industry. The extent to which provincial institutions support and underpin national strategy will in large measure determine the value of BEE transactions in the province. Targets set in charters are national. The challenge for KZN institutions is to ensure KZN-based firms that are subject to the charters (for example, SAPREF and ENGEN in terms of the Liquid Fuels Charter) meet their targets.

Black Economic Empowerment is a key element of DEDT's economic strategy. It is recognized that the full growth potential of the economy is only possible through bringing the majority of South Africa's people into the mainstream of economic development. BEE is thus regarded as a necessary stimulus and an indispensable condition for real economic "take off". The DEDT adopts a multi-dimensional and integrated approach to BEE initiatives, with BEE addressed in all programmes undertaken by the DEDT. BEE is nevertheless packaged as a separate programme to ensure focus on specific priorities that include:

- Promoting affirmative procurement practices;
- Packaging investment initiatives that provide opportunity for black entrepreneurs;
- Internal trade policy initiatives that favour black business;
- Sectoral strategies for BEE;
- Support for emerging contractors;
- Community equity participation;
- Providing support for gearing of finances and assisting mobilizing finances including community banking;
- Monitoring how public and private institutions comply with national guidelines; and
- Supporting initiatives aimed at supporting affirmative procurement by encouraging linkages between small and large companies.

Finally, BEE firms are the recipients of the overwhelming majority of Ithala's commercial and industrial loans, making it the key institution in KZN promoting economic development. These projects are discussed in detail in section 4 of the report.

2.10 The informal sector

In South Africa, declining formal sector employment has resulted in an increase in employment in the informal sector of the economy. The informal sector is defined as an aggregate of activities that result from the need of labour market participants to generate their own employment to earn a living because other sectors of the economy are unable to provide a sufficient number of adequate employment and income opportunities for a rapidly growing labour force (ILO, in Department of Labour, 2002).

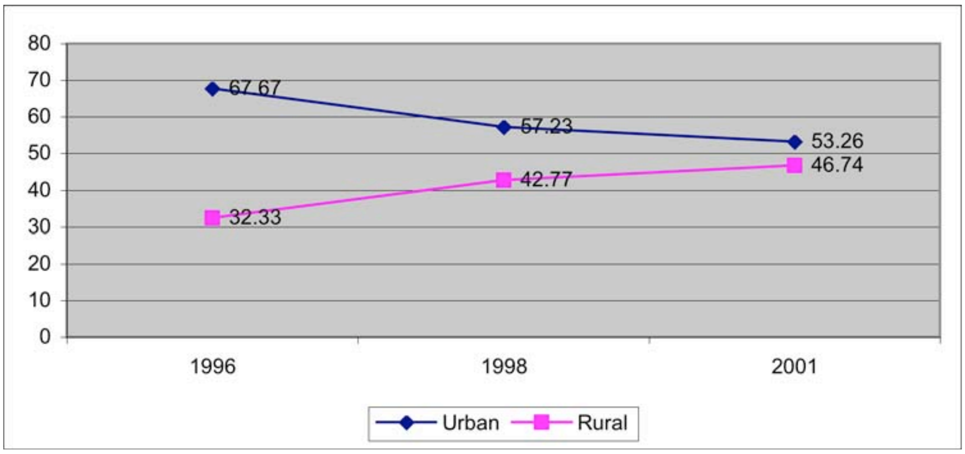
The informal sector encompasses different types of economic activities (including trading, manufacturing and the provision of a wide variety of services), in a context of different employment relations (the self-employed, paid and unpaid workers and disguised wage workers) and activities with different economic potential, such as survivalist activities and successful small enterprises (Devey *et al*, 2002). The activities are generally of a small scale and can easily escape certain government requirements such as business registration, tax and social security obligations and health and safety rules. Moreover, people involved in this sector do not have any social benefits from the state to fall back on.

The dynamics of this sector, coupled with variations in the activities of workers, creates a pyramid type of hierarchy, comprising survivalist informal enterprises, such as street traders, shoe shiners and garbage collectors, at the bottom; informal enterprises such as home-based manufacturers with some growth potential in the middle; and high growth informal enterprises such as web designer consultants or e-business operators at the top of the pyramid (Devey *et al*, 2002). The formal and informal parts of the economy are, however, linked and the boundaries between them are becoming increasingly blurred.

Due to the diffuse and unregulated nature of the informal sector it is notoriously difficult to analyse trends in economic activity and employment. The most reliable source of information is official employment statistics. This section therefore uses data from the October Household Surveys of 1996 and 1998, as well as the Labour Force Survey of September 2001. It provides a detailed picture of the informal sector in KZN in terms of the locality of informal workers, the sectors in which they are active, occupational categories, and the gender, race, age, and educational attainment of participants. The informal sector includes employees, as well as those individuals who are self-employed.

Figure 2.24 summarises the distribution of workers by locality in KZN. The number of workers from rural and urban areas was gradually converging between 1996 and 2001, making the distribution close to equal in 2001. In 1996 the proportion of informal sector workers was higher in urban areas (68%) and declined in 2001. In contrast, the proportion of rural informal workers grew from 32% in 1996 to 47% in 2001. This increase is more apparent than real – it reflects the fact that employment statistics started to include subsistence farmers in the informal sector from 1998. Before that, they were not included at all in official statistics.

Figure 2.24 – Locational distribution of workers in the informal sector, SA and KZN, 1996-2001



In 2001, informal sector workers in KZN were concentrated in trade and domestic work, accounting for 66% of the total. The services (6.8%), manufacturing (6.8%), agriculture (6.8%) and construction (6.4%) sectors account for a significant proportion of informal sector workers, although employment has been declining in construction and agriculture since 1996 (see Table 2.8).

Table 2.8 – Industrial sector of workers in the informal sector

Sectors	1996 National	1996 KZN	1998 National	1998 KZN	2001 National	2001 KZN
Unspecified	11.33	7.11	1.38	2.23	0.78	0.42
Agriculture	12.18	5.4	10.61	10.62	12.71	6.81
Mining	0.15	0	0.2	0.25	0.08	0
Manufacturing	9.31	11.58	6.28	7.28	6.31	6.84
Utilities	0.29	0	0.23	0.88	0.06	0
Construction	9.81	11.85	8.57	8.61	8.16	6.39
Trade	31.03	40.56	27.52	28.71	29.69	31.55
Transport	4.15	3.1	4.32	5.84	3.26	3.75
Financial	10.56	8.23	2.7	2.62	2.57	2.5
Services	10.12	12.18	5.39	6.53	5.21	6.86
Domestic	1.08	0	32.8	26.43	31.15	34.87
Total	100.00	100.00	100.00	100.00	100.00	100.00

Table 2.9 summarises employment in the informal economy by occupational category. Domestic workers, elementary, craft related, sales and agricultural workers dominate the sector. The management, professional and technical jobs have actually been declining within the informal sectors, both nationally and in KZN. KZN has, however, been experiencing an increase in the number of elementary workers since 1996, while craft workers have been declining.

Table 2.9 – Occupational categories of workers in the informal sector

Occupational categories	1996 National	1996 KZN	1998 National	1998 KZN	2001 National	2001 KZN
Unspecified	8.51	7.11	1.27	1.77	0.78	0.42
Managers	12.27	16.94	4.16	5.22	2.01	2.65
Professionals	6.75	3.9	0.83	1.49	0.68	1.22
Technicians	10.65	12.38	2.87	5.14	2.95	4.5
Clerks	2.09	4.12	1.84	0.65	1.07	1.53
Sales	11.07	13.3	13.69	14.81	12.06	12.61
Agriculture	9.06	4.08	3.7	6.48	11.91	6.82
Craftsmen	20.97	23.98	15.03	17.94	15.14	14.21
Operators	3.44	3.67	5.16	4.46	3.2	3.59
Elementary	15.18	10.53	19.42	16.38	23.08	21.73
Domestic Workers	0.00	0.00	0.00	0.00	27.13	30.72
Army	0.00	0.00	32.04	25.68		
Total	100.00	100.00	100.00	100.00	100.00	100.00

Figure 2.25 illustrates that although men dominated the informal sector in KZN in 1996, its gender composition has shifted substantially, with females starting to be dominant, especially in 1998 and 2001. For KZN, female participation was almost double that of male participation in 2001, accounting for 64% and 36% respectively.

Figure 2.25 – Gender composition of workers in the informal sector, SA and KZN

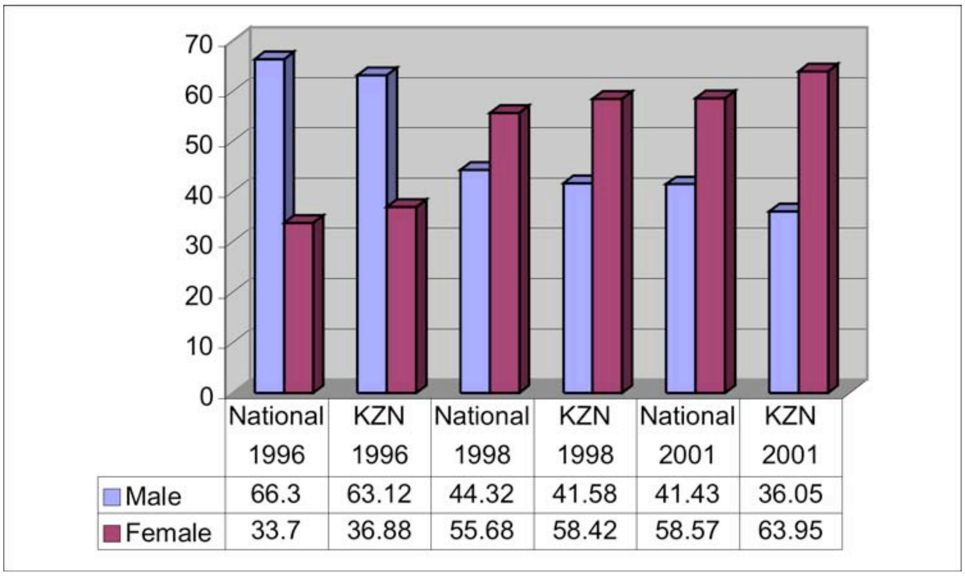
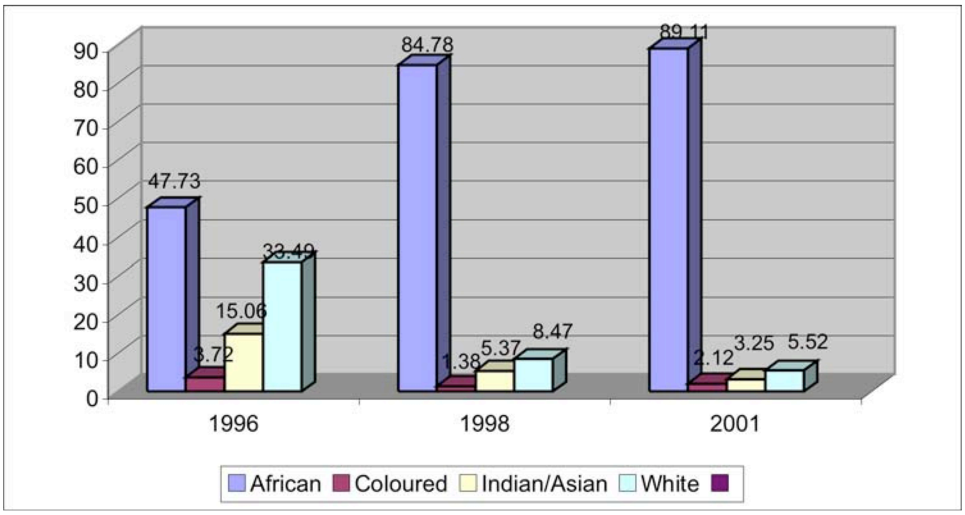


Figure 2.26 illustrates the racial composition of the informal sector in KZN. A clear racial pattern is evident. Africans represent the vast majority of workers engaged in the informal economy, and their participation in this sector has increased over the

years. For other racial groups, a relatively small proportion of workers are engaged in the informal economy with, for example, just 6% of whites in 2001 compared to 90% of Africans.

Figure 2.26 – Racial composition of the informal sector in KZN, 1996 - 2001



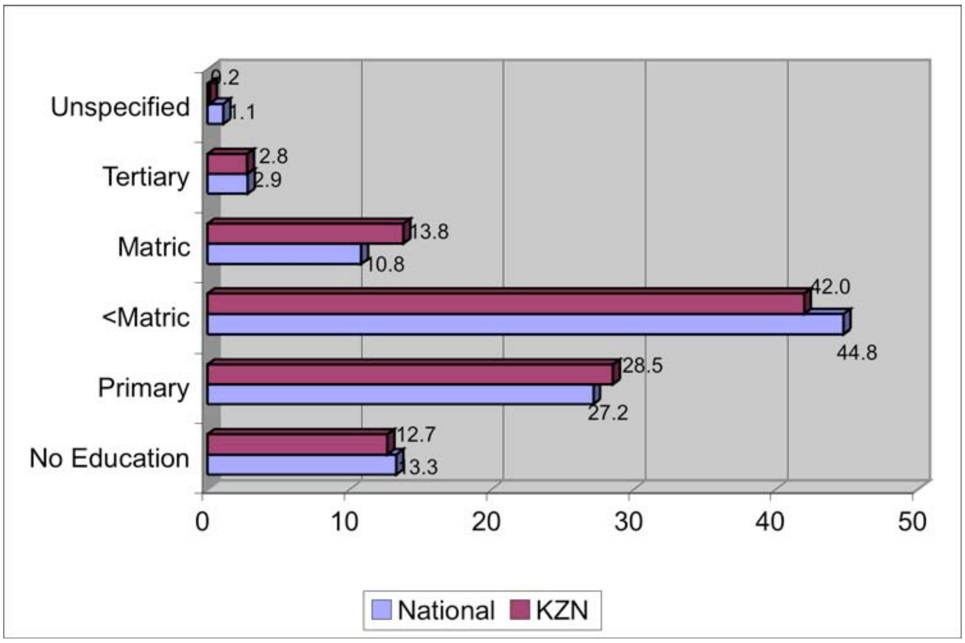
In terms of the age distribution of informal sector workers in KZN, table 2.10 indicates that the highest proportion of informal workers fall in the 25 – 44 age group, while those in the age groups 45 - 64 constitute the second largest. In 2001, for example, there were only 11% of informal workers aged between 16 and 24 in KZN, compared to 60% of those aged between 25 and 44. The high unemployment rate among the youth in the country has probably contributed to an increase in the percentage of youth (16-34 age category) in the informal sector. KZN has however, experienced a decrease in the number of informal workers in this age category, particularly in 2001.

Table 2.10 – Age distribution of workers in the informal sector, SA and KZN

Age groups	1996 National %	1996 KZN %	1998 National %	1998 KZN %	2001 National %	2001 KZN %
16-24	7.09	6.34	11.99	14.6	12.6	10.68
25-34	24.58	26.64	28.79	29.04	26.62	30.29
35-44	31.61	34.82	31.2	31.49	28.02	29.7
45-54	21.62	17.65	18.26	15.99	19.44	18.24
55-64	15.09	14.54	9.77	8.88	13.32	11.09
Total	100.00	100.00	100.00	100.00	100.00	100.00

In terms of the level of education reported by workers in the informal sector, figure 2.27 illustrates that in conformity with the national picture, the majority (80%) of workers in the informal sector in KZN have not attained matric, while 12.7% report having no education at all. This is probably due to the changing nature of formal work in the economy, which requires higher levels of skill and consequently pushes unskilled or semi-skilled workers into the informal sector.

Figure 2. 27 – Educational attainment of workers in informal sector for 2001



The number of worker in the informal sector with matric and tertiary education for South Africa as well as for KZN has also been decreasing between 1996 and 2001 (table 2.11). In 2001, the low proportion of informal sector workers with matric (14%) and tertiary (3%) qualifications might reflect the economic push factors in KZN. It may also be argued that given the elementary nature of work in the informal sector, higher levels of education may have no discernable impact on workers in the informal sector.

Table 2.11 – Educational attainment of workers in the informal sector

	1996 National %	1996 KZN %	1998 National %	1998 KZN %	2001 National %	2001 KZN %
No education	8	7	17	13	13	13
Primary	16	16	26	30	27	29
Matric	29	36	38	35	45	42
Matric	26	19	15	16	11	14
Tertiary	20	21	3	5	3	3
Unspecified	0	0	0	0	1	0
Total	100	100	100	100	100	100

The picture that emerges from this analysis is that the most vulnerable members of the labour force – females, Africans and people with low educational attainment – dominate the informal sector in KZN. From a policy perspective, the key issue is to identify ways in which to enhance the productivity and earnings of informal sector workers in order to improve their quality of life and contribution to the economy. In this regard, the DEDT's SMME policy framework is an appropriate instrument for developing the informal sector in KZN.

2.11 Conclusion

The analysis of the KZN economy has highlighted the fact that while it is growing faster than the national economy, it remains the fourth poorest province in South Africa. This position is not commensurate with its competitive advantages, including a high proportion of South Africa's manufacturing capacity and a logistics platform with the highest volumes of imports and exports in the country.

During the 1995 to 2001 period, the average annual growth rate of 4.3% per annum was driven by the expansion of a few sectors, notably financial and business services, transport and communication, paper and paper products, non-ferrous metals and petroleum. The rapid growth of the former two sectors has entrenched the dominance of the services sector in the KZN economy.

Within the manufacturing sector, while growth has been driven by the expansion of non-ferrous metals, other chemical products (petroleum) and paper & paper products, industries that currently account for a relatively small proportion of provincial GGP have also been growing. These include beverages, motor vehicles, printing and publishing, non-electrical machinery, iron and steel, professional equipment and wood furniture. Declining sectors include food & food products, retail & wholesale, clothing, textile and fabricated metal products.

The analysis of factors contributing to the growth and decline of selected sectors, highlighted the fact that each industry has its own set of competitive factors and constraints. Industrial policy – in particular, trade liberalisation and supply-side measures (elaborated upon in appendix A) – has influenced the patterns of growth and decline in specific industries. While exposure to international competition has contributed to the decline of some industries (notably, textile), it has strengthened others by enhancing their global competitiveness. South Africa's enhanced export performance has clearly benefited KZN, as evidenced by buoyant growth in transport and communication (i.e. logistics services).

The imperatives of BEE and SMME development loom large in KZN. While the framework within which they will be promoted is set by national government, the DEDT has an important role in facilitating the entry of such firms into the provincial economy. The impact of policy measures that are currently in place to achieve this must regularly be evaluated.

As regards the informal sector, while it is a significant source of employment in KZN, its activities are concentrated in the low-productivity, low-wage end of the economy. The imperative is therefore to facilitate the movement of its participants up the value chain in order to increase their income and contribution to the economy.

The performance of particular industries should be more closely linked to the nodal developments (in the form of SDIs and IDZs) that are currently being implemented in KZN. The manufacturing opportunities that are likely to be unlocked in the wake of the restructuring of the Port of Durban must also be focussed on specific industrial sectors. As key instruments of provincial industrial policy, these initiatives are likely to have a significant impact on the regional economy. It is, however, imperative that they are linked not only to particular industries, but also to the development of industrial clusters located within global supply chains. Such an approach will significantly reduce the risk of failure and enhance the multipliers generated by these nodal developments.

Of note is the spatial concentration of economic activity in three metropoles: Durban, Pietermaritzburg and Richards Bay. Indeed, with the exception of the Lubombo SDI all the nodal developments are located in these metropoles. In the long-term, the location of standard manufacturing enterprises in large and congested metropoles is likely to undermine their cost-competitiveness. Consideration should therefore be given to creating alternative sites for production outside the metropoles.

3 The KZN labour market: employment, human resource development and HIV/Aids

3.1 Introduction

The most critical challenges facing South Africa at present are high and growing levels of unemployment in a context where skill shortages are constraining economic expansion and the negative economic impact of the HIV/Aids pandemic. In KZN, both unemployment and the incidence of HIV/Aids are significantly higher than the national average.

For this reason, an important focus of this project is an analysis of patterns of labour absorption in KZN and the related imperative of a human resource development strategy that is aligned to the demand for labour emerging from industry. Both will be affected by the incidence of HIV/Aids. Hence a detailed analysis of its impact on labour markets and the broader provincial economy is provided.

The economic upliftment of the people of KZN is the overarching objective that will inform the province's industrial strategy. As the end of all economic development is the enhancement of the quality of life of a country or region's citizens, an understanding of the extent to which they engage in the economy (through employment) and the position they occupy within it (by virtue of their skills) shapes the parameters of what is attainable in terms of economic development strategies, and facilitates the identification of priorities with respect to such strategies.

3.2 Labour absorption

South Africa's high and growing unemployment problem is the most important economic challenge currently facing policy-makers. The scale of the problem is such that of a broad labour force of 18.5 million, 7.5 million are employed in the formal sector and commercial agriculture, 3.3 million are working in the informal sector, subsistence agriculture and domestic work, and 7.7 million workers are unemployed (of which 3.2 million are discouraged and hence not accounted for in the 'strict' definition of unemployment).

This situation unsustainable and poses a certain brake on long term growth and human development. Indeed, Altman (2002) argues that an economy needs a minimum proportion of its labour force sufficiently active to support less productive groups, with the exception of oil exporting economies that have so much income that they support large welfare states.

3.2.1 The national context

The unemployment problem in South Africa is certainly not a recent phenomenon although the communications of the apartheid government might make one believe it is (Altman, Bhorat and Hodge 1999, Edwards 2000, Kaplinsky 1995, Klasen & Woolard 2000, Meth 2001, RSA 1998). Apartheid government publications put forward unemployment rates in the region of 1% to 2%, thereby primarily focusing on that amongst Whites.

In fact, net employment has been stagnant or falling since the early 1980s. The structural characteristics of falling employment were caused by a number of factors related to Apartheid government policies aimed at promoting "Separate Development". For example, the supply of labour suitable to a middle income economy was constrained by a complementary set of adverse education, population control and labour market measures, whilst at the same time having the effect of diminishing household incomes and therefore a nation's greatest resource: its people.

In itself, this is probably one of the greatest brakes on current growth and labour absorption rates. At the same time, markets were constrained by a closed economy and legal constraints to black entrepreneurship, amongst others. The direction of development has further limited labour absorption, by putting the economy on a firmly capital-using path.

Consequently, a large stock of unemployed people has built up over many years, and each year the economy has trouble absorbing not only this stock but new entrants as well. Formal sector employment has been stagnant at best: 900,000 formal jobs were lost over the 1990s (Edwards 2000, Meth 2001), mostly in resource-based industries, construction and the public sector, generally due to a range of technological and policy-induced changes.

Any job creation that did occur absorbed higher skill labour, leaving those retrenched with little place to go. Alongside stagnant formal employment, is a context of high population growth and net inflows into the labour market: the labour market expands on average by about 600,000 net new entrants each year. By 2001, the strict and broad unemployment rates had risen to 30% and 41% respectively. Even by the strict definition, unemployment continues to rise by about 2% to 3% each year.

3.2.2 Measuring unemployment

Measuring unemployment is a tricky affair. Properly measuring employment and unemployment across the full population is really a new activity: there have been many changes in the measurement instruments over the 1990s, as SA has sought to make improvements[15]. Hence, it is preferable to draw broad trends rather than focus on precise point estimates.

[15] The best measurements of employment are drawn from the household surveys, notably the October Household Survey (OHS) that ran between 1994 and 1999, and the Labour Force Survey (LFS), run

Unemployment can be measured in a number of ways. The accepted international norm focuses on 'strict' (or 'official' or 'narrow') measures that include only workers still actively looking for work. The 'broad' (or 'expanded') definition includes those parts of the labour force that say they would like to work, but have become discouraged. In South Africa, the review of both measures is important due to the racial and gender biases: by far, the majority of discouraged workers are 'African' rural women**.** Of the 7,698 million workers who were unemployed in 2001, 3,173 million are discouraged**.**

The chronic nature of unemployment is demonstrated by the fact that only 41% and 32% of urban men and women respectively that were defined as strictly unemployed had previously had a job. One-third to one-half of the 'strictly-defined' unemployed had been out of work for more than 3 years. Although some argue that many of these people may well be working in small piece jobs or in the formal sector, the LFS is covering any and all economic activity, including unpaid labour, so should be capturing this possibility. Labour force participation rates are quite high and more people are looking for work: this may mean that people are more hopeful or alternatively more desperate, as the picture is still quite bleak.

Even by the strict definition, unemployment is expanding each year. While unemployment is rising for all race groups, the racial incidence is enormous, mostly falling on African workers. As the problem lies in the both the stock of 'unemployed' and the 'flow' (related to entry and exit), the main contributors to growing unemployment include: an expanding labour force due to population growth, increased participation rates (with the end of apartheid – freedom of movement to urban areas, increased hopefulness; increased female participation) and no net increase in the number of job opportunities.

3.2.3 Salient characteristics of the unemployed

In a comprehensive analysis of national unemployment, Altman (2002), highlights the following characteristics of the unemployed:

- Unemployment rates for 'African' workers are much higher than for other groups. However, unemployment rates have been growing substantially for every other group, aside from Whites, particularly from the late 1990s. Even so, 35.5%, or 3.9 million African workers were unemployed in 2001, compared to 21.8% of 'Coloured' and 18.2% of Asian workers, numbering only 0.5 million.
- There is a substantially higher rate of discouragement amongst rural African women than for any other group, reaching 58% by the broad definition.
- The number of young unemployed is growing much faster than any other group, thereby boosting the economy-wide unemployment rate each year because of the inability of the economy to absorb new labour market entrants.

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twice a year since 2000. In this submission, we use the September LFS to enable better comparisons to the previous OHS.

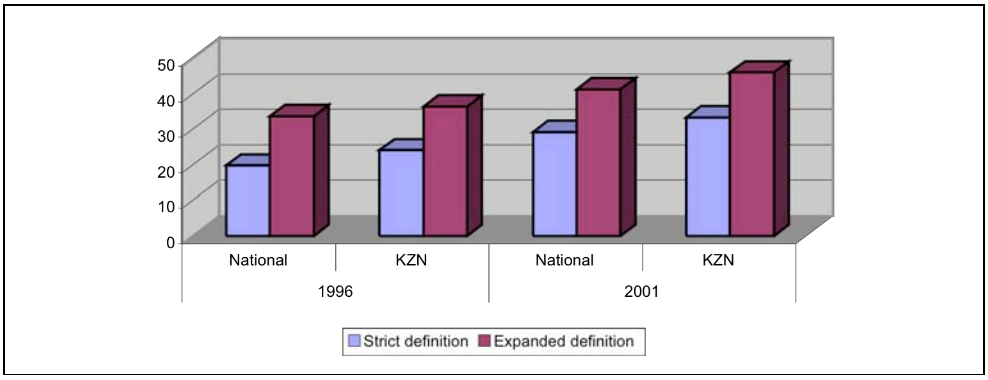
- In the non-agricultural formal sector, employment has been stagnant, ranging between 6.4 million and 7.1 million workers.
- Commercial agriculture lost 750,000 jobs between 1994 and 1996, and is now stagnant, with employment in the region of about 660,000.
- It is estimated that about 1.2 million people work in the public sector.
- While it is difficult to track changes in informal employment, there is evidence that this sector has been growing in the post-1994 period and currently employs 2.4 million to 2.7 million workers.

Trends in labour market absorption at the national level explain why employment creation has become a major preoccupation of policy-makers. The phenomenon of "jobless growth" is driven by a growth trajectory in which the demand for lower skill labour has fallen, in the context of a very large oversupply, and the demand for higher skill labour has risen in the context of a severe skills shortage. This is underpinned by a growth trajectory in which skill, capital and technology-intensive sectors have been expanding, while semi-skilled and unskilled labour-intensive sectors have been contracting.

3.2.4 Labour absorption trends in KZN

KZN has significantly higher levels of unemployment than the national average, in terms of both the strict and expanded definition of unemployment. Figure 3.1 demonstrates that unemployment in KZN exceeded the national average in 1996 by 4.3% of the strict definition and 2.8% of the expanded definition. In 2001, the gap between national and KZN levels of unemployment had closed slightly, but in terms of the expanded definition had increased by 2 percentage points. In the context of national unemployment, KZN accounts for 17.9% of employment in South Africa. This is disproportionate to the province's share of the country's population, which is 21%.

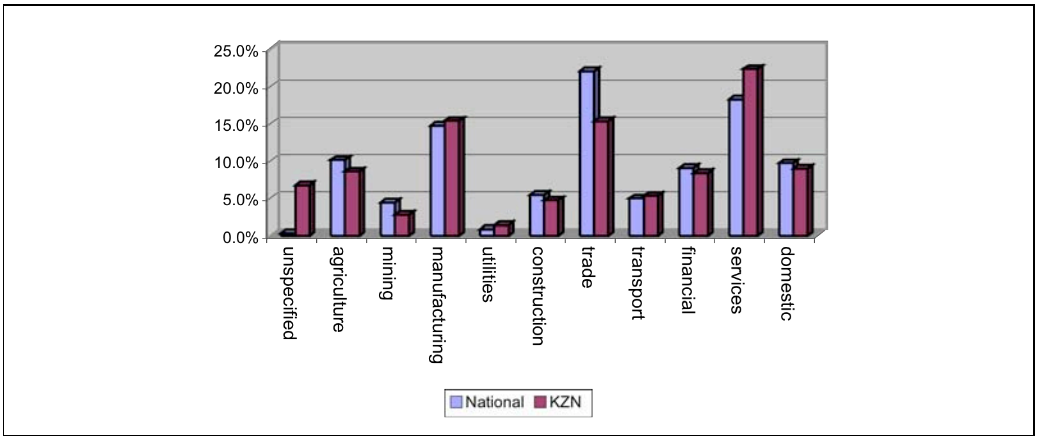
Figure 3.1 – Unemployment rate: SA and KZN – 1996 and 2001



The magnitude of the unemployment problem in KZN is such that in 2001, in terms of the strict definition 986,850 (33.3%) of KZN's labour force were unemployed. The expanded definition provides a far grimmer picture, with unemployment at 1,681,406 (46%) of the labour force. To redress these high and growing levels of unemployment – between 1996 and 2001 unemployment grew by between 9.3% (strict definition) and 9.6% (expanded definition) – a large number of jobs need to be created.

The sectoral composition of the demand for labour reflects the structural characteristics of the KZN economy analysed in section 2. Figure 3.2 illustrates that in 2001 the proportion of the KZN labour force employed in the primary sector was below the national average. Agricultural employment accounted for 7.8% (compared to a national average of 10.1%), while the mining sector absorbed a mere 0.2% of the labour force (compared to a national average of 4.4%). In contrast, the manufacturing sector accounted for a substantially higher proportion of the KZN labour force (20.6%) than the national average of 14.7%. A further deviation from national trends is that a higher proportion of the KZN labour force is employed in the transport sector (6.3%, compared to 5% at the national level).

Figure 3.2 – Employment by industrial sector, 2001

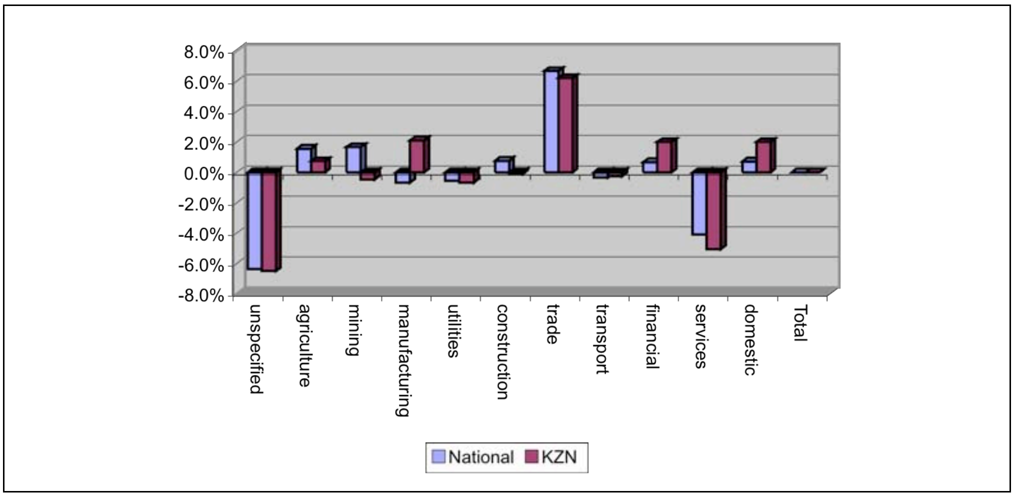


In terms of growth trends, as illustrated in figure 3.3, the most striking aspect is that in KZN between 1996 and 2001 employment has been growing in the manufacturing sector, while it has been declining at a national level. In the financial and domestic services sectors, employment growth has also been substantially higher than the national average over this period.

In contrast, employment in the agriculture and construction sectors has been growing more slowly in KZN than the national average, while the negative growth in the utilities and services sectors has been higher for KZN than the national average. Employment growth in the trade sector, while robust at 6.2%, has been below the national average of 6.7%. This pattern of labour demand must be interpreted in a context where skill shortages are constraining the expansion of skill-intensive sectors.

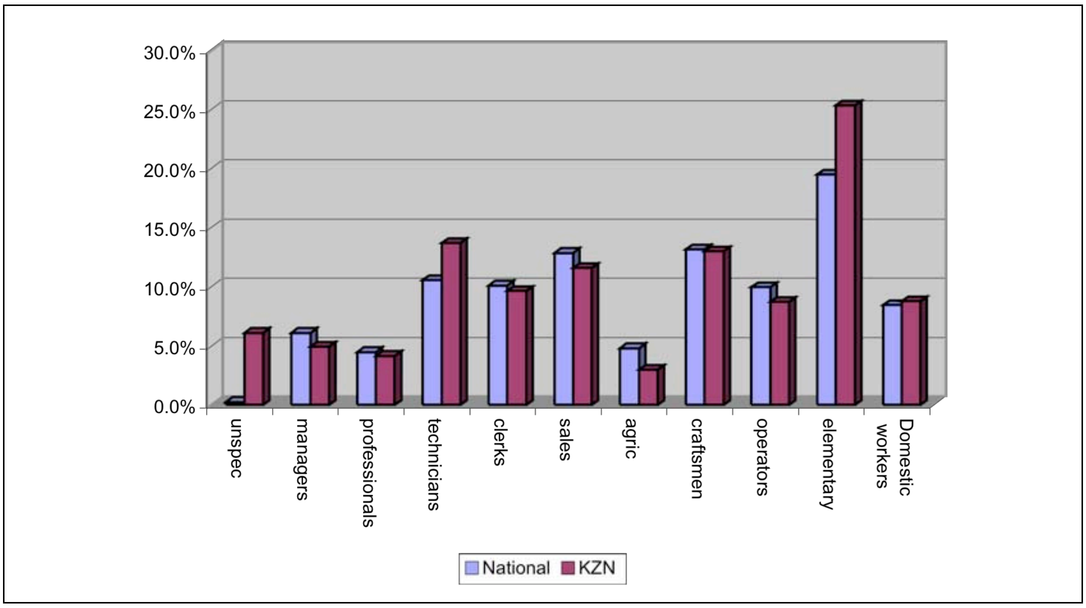
Moreover, the expansion of economic activity in capital and technology-intensive sectors has resulted in job losses.

Figure 3.3 – % change in employment by industrial sector: 1996 – 2001



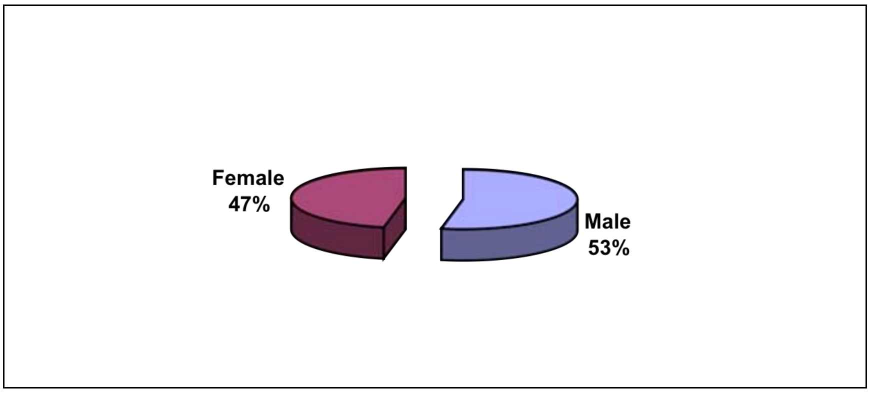
In terms of the occupational categories of workers, KZN broadly conforms to the national picture, as illustrated in figure 3.4. KZN has a slightly higher proportion of managers, professionals, technicians, operators and domestic workers and a slightly lower proportion of agricultural workers, and craftsmen.

Figure 3.4 – Employment by occupational category, 2001



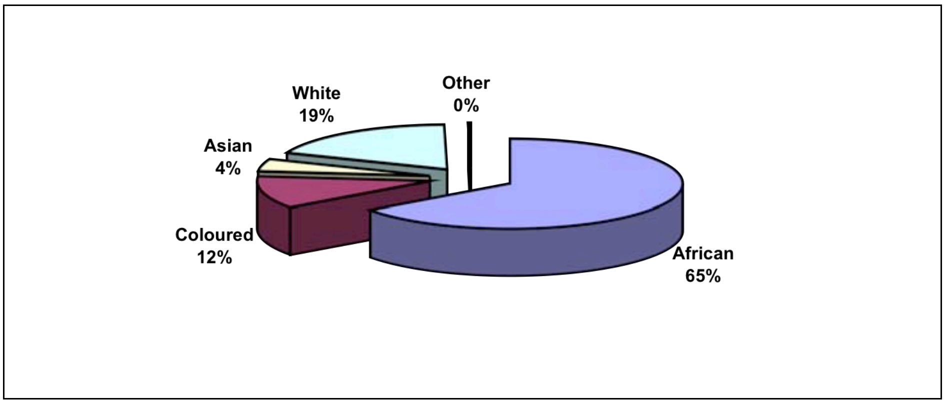
In 2001, 53% of KZN's active labour force was male and 47% female. This compares favourably with the gender composition of workers at a national level, where males account for 55.9% of the active labour force and females 44.1%. Of significance is the fact that males have been losing jobs and females entering employment between 1996 and 2001. In KZN, the growth of the active female labour force (4.7%) exceeded the national average (4.3%).

Figure 3.5 – Gender composition of employed workers in KZN, 2001



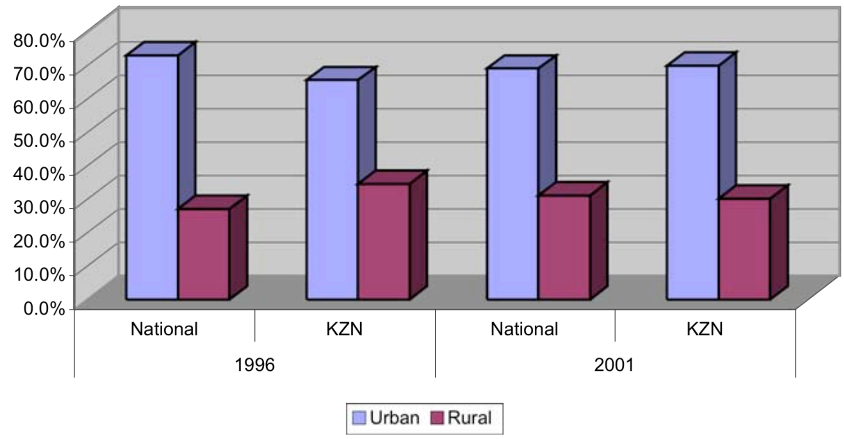
The racial composition of the active labour force is illustrated in figure 3.6. It reflects the composition of KZN's population, but differs from the national picture in that a slightly higher proportion of Africans (2.8%) and a significantly higher proportion of Asians (10.3%) form part of KZN's active labour force. In contrast, the white and coloured racial groups are under-represented in KZN, relative to the national average, by 5% and 8.9% respectively.

Figure 3.6 – Racial composition of KZN's active labour force, 2001



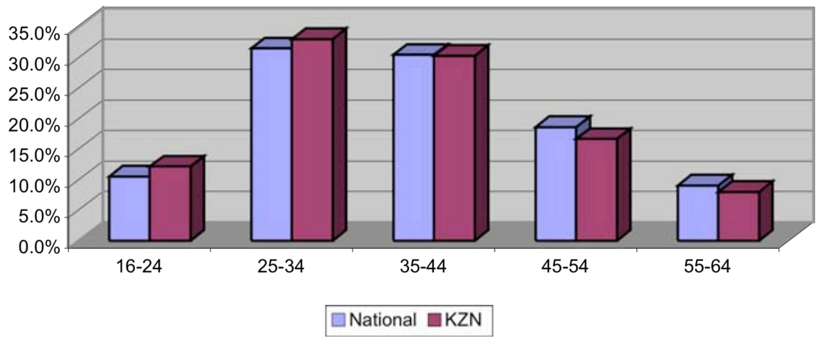
In conformity with national trends, the majority of KZN's active labour force is located in urban areas. However, as illustrated in figure 3.7, between 1996 and 2001, the proportion of urban workers grew by 4.3% in KZN, while at the national level this figure declined by 4%. This suggests that the urban bias in employment is becoming more entrenched in KZN.

Figure 3.7 – Location of workers, 1996 and 2001



The age distribution of workers in KZN differs markedly from national aggregates in that, as illustrated in figure 3.8, a higher proportion fall in the younger (16-34) age group, while a lower proportion are in the older (35 - 64) age group. This suggests that there is a higher level of entry for young people, while the "stock" of unemployed is increasing.

Figure 3.8 – Age composition of the active labour force, 2001



In terms of the distribution of the active labour force across the formal and informal sectors, Table 3.1 illustrates that KZN conforms broadly to national trends with informal employment accounting for 27% of total employment, compared to 29% at the national level. In KZN, however, there are a higher proportion of employees in the formal sector relative to owners of informal enterprises. Unfortunately, it is not possible to track trends in informal sector employment because since 1999 Statistics SA changed the way they looked at employment activity and included subsistence agriculture in the informal sector, whereas it was largely ignored before.

Table 3.1 – Disaggregation of the employed by the formal and informal sectors, 2001

Sectors	SA	KZN
Formal sector	71%	73%
Informal sector – employee	18%	15%
Informal sector - owner	11%	12%

The analysis of trends in labour absorption in KZN paints a decidedly grim picture of the nature of the unemployment problem confronting the province. This is underlined by the fact that KZN is home to the highest proportion of South *Africa's population and has the highest level of* unemployment. This explains the relatively weak position of KZN within the South African economy, despite its competitive advantage in transport logistics and a range of industrial sectors.

Although the challenge facing the province is formidable, it is also a basis upon which to harness resources from national government to pursue a regional industrial strategy. In a context where there appears to be an absence of criteria to allocate economic resources across provinces, national government's preoccupation with redressing unemployment presents an entry point to lobby for resources to pursue a provincial industrial strategy that is employment creating.

3.3 Human resource development

The centrality of human resource development in broader economic development strategies has become imperative in a context of globalisation where skills rather than the resource base of regions determine their competitiveness (Shankar & Shah, 2001). Indeed, as alluded to in section 3, the South African economy (including the KZN economy) has been growing in skills-intensive sectors. This pattern of development will not be sustainable unless there is a rapid increase in skilled labour, driven by a pro-active human resource development strategy.

A key challenge for the KZN province is to align its economic development strategies with its human resource development strategies, within the policy framework of national government. In light of the challenges posed by high and growing levels of unemployment two priorities are apparent: to upgrade the skills base of KZN's labour force in the long-term and create employment for semi-skilled and unskilled workers – who constitute the vast majority of the unemployed – in the short- to medium-term.

3.3.1 Human capital and unemployment

Employment growth depends on human and physical capital formation; the latter ideally applied to labour absorbing investments. In addition to weak physical capital formation, to explain stagnant or falling employment it is necessary to look to the causes of weak human capital formation. The historically slow growth in South Africa's secondary and tertiary sectors can be attributed to the Apartheid minerals economy that restricted international interaction, small business entry, effective demand and labour market functions such as skilling, spatial and occupational mobility, affordable cost of job search, and circulation of market information. These conditions were created by the approach to import substitution industrialisation, international sanctions, legal restrictions on ownership of assets and businesses by the black population, and controls over the labour market and access to education.

One legacy is the severe gap in skills attainment: less than a third of 'African' men and women that work in the urban formal sector have completed high school. Generally less than 10% of informal and non-urban 'African' workers have finished high school (Meth 2001, October Household Survey 1999). Indeed, South Africa is a highly distorted middle income economy, with a cost structure and domestic market-oriented production sectors that reflect this middle-income status but a skills level that is more reflective of a less developed country (Kahn and Black 1998, Klasen and Woolard 2000; Altman 2001).

According to Statistics South Africa (1999), only 11 percent of South Africans of 20 years or older hold some form of post high school diploma, degree or other qualification and 12% have no education at all. The racial bias in educational attainment is evidenced by the fact that while 3.7% of people over 20 hold university degrees or higher qualifications, this breaks down into 16.5% of whites over 20, but only 1.5% of other race groups.

Of the active labour force of approximately 10 million, 3 million are skilled and highly skilled, while 7 million are semi-skilled and unskilled (Department of Labour, 2001). Of the unemployed, 50% percent are young people who have completed at least nine years of schooling. The Department of Labour (2001) argues that youth unemployment was aggravated by inadequate provision of technical and vocational training opportunities.

3.3.2 Educational attainment

The level of education of the labour force is a means of measuring the quality of a country's human capital and is an indication of the ability to successfully undertake training and acquire useful skills. In South Africa there is an oversupply of people with a low level of education and a great shortage of skilled workers. This skill profile is more closely aligned to a low-income than middle-income developing country, and is the consequence of the majority of the population being denied adequate education and training during the apartheid era.

Figure 3.9 illustrates that while few people have no education, the vast majority have not attained matriculation level. Just over a quarter (25.1%) have matric and a mere 15.1% have tertiary qualifications. While KZN conforms to the national trend of educational attainment, it has a larger proportion of matriculants, and a lower proportion of people with no education, less than matric level education and post-matric qualifications.

Figure 3. 9 – Distribution of educational level, 2001

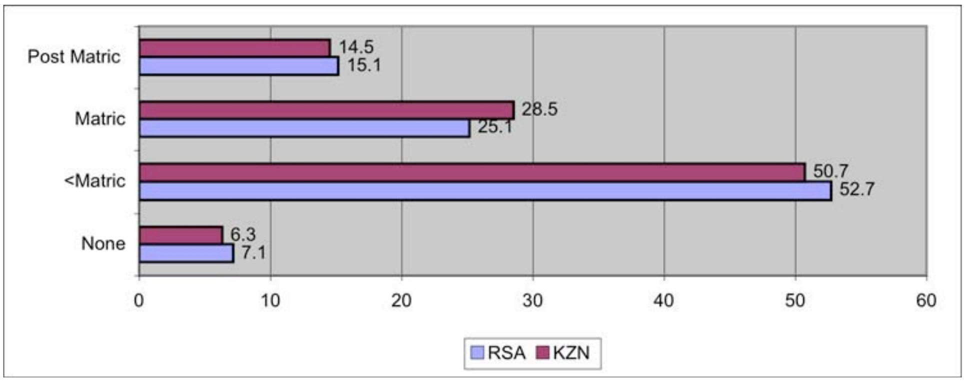
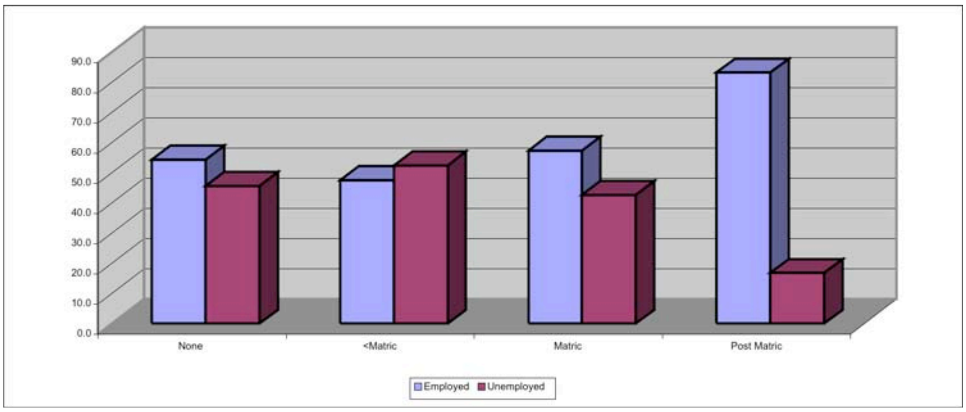


Figure 3.10 illustrates the relationship between educational attainment and employment in KZN. A high proportion of people with post matric qualifications (83.2%) are employed. Of those with matric more than half (57.3%) are employed. Fifty two percent of people with less than matric and 45.7% with no education at all are unemployed in KZN. There are 16.8% of unemployed people with post matric qualification in the province. The question in this regard is whether the labour market cannot absorb them because of a lack of demand for their skills, or because information flows between the demand and supply sides of the market are inadequate.

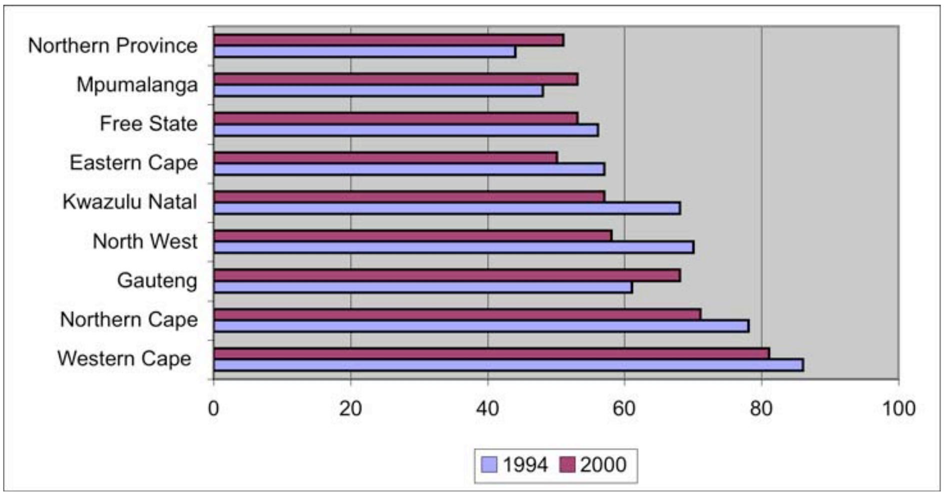
Figure 3.10 – Educational level of both employed and unemployed in KZN



In terms of attainment of a senior certificate (matric), KZN has the second largest number of candidates (with an average of 18% since 1994) in the country, but ranks fifth in terms of the pass rate. The Western Cape recorded the highest pass rate and also the highest proportion of candidates who obtained university exemptions, as it is highlighted in figure 3.12.

Of concern is the fact that of the 96,423 candidates who sat for the matric examination certificate in 2000 only 57% passed. This is a significant decline from the pass rate of 68% attained in 1994. These statistics must, however, be interpreted against a background in which the total number of candidates writing the matric exams increased.

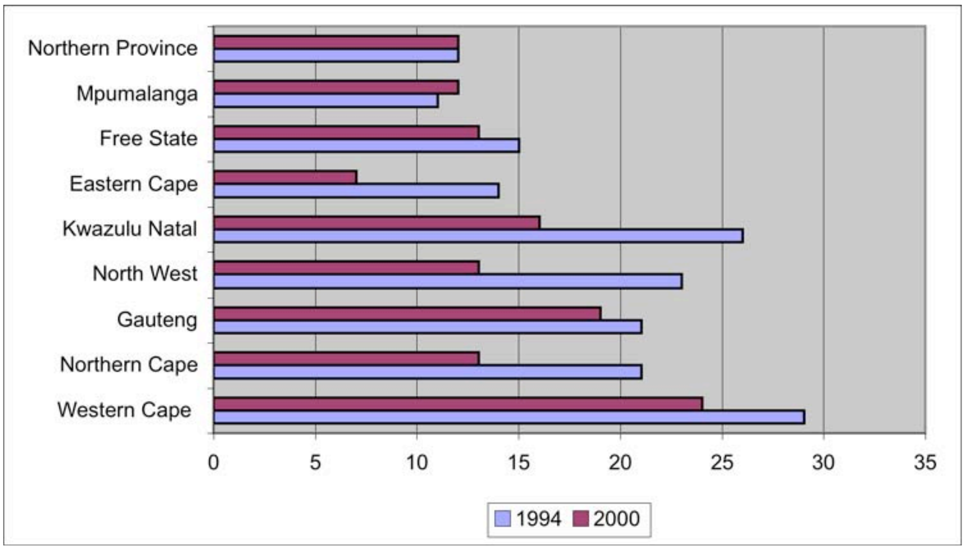
Figure 3.11 – Senior certificate: provincial pass rate, 1994 and 2000



[Source: South African Survey 2001/2002]

The number of university exemptions granted to candidates that passed matric has also dropped by 10% between 1994 and 2000 in KZN. Figure 3.12 illustrates the number of university exemptions attained in the 9 provinces. For KZN, the number dropped from 26% in 1994 to 16% in 2000. This conforms to the national trend, as most provinces experienced a decline in university exemptions.

Figure 3.12 – Senior certificate: provincial university entrance, 1994 and 2000



[Source: South Africans Survey 2001/2002]

The level of educational attainment (a static indicator) when combined with matric pass rates and university exemptions (a more dynamic indicator) in KZN suggests that the poor level of skill within the labour-force is not being redressed at a pace that will impact significantly upon low growth and unemployment.

3.3.3 HRD strategy

South Africa's HRD strategy is directed specifically at the supply side of education, such as further education and training and higher education in order to target the problem of a paucity of high-quality skills that are more responsive to societal and economic needs. Within this framework, tertiary institutions are seen as key drivers in providing the labour market with high level competencies and expertise necessary for the growth and prosperity of a modern economy. They are seen as a developmental base that is central to HRD Strategy. The restructuring of both the higher and further education sector was proposed for these reasons.

The proposed changes do not only influence the curriculum within higher education, but also alter the institutional landscape of all provinces. Further Education and Training (FET) institutions in South Africa are seen as drivers of technical and vocational education and training that is currently needed for tackling a high level of youth unemployment. Nationally, the 152 technical colleges were merged with colleges of education and/or manpower training sites to form 50 new institutions.

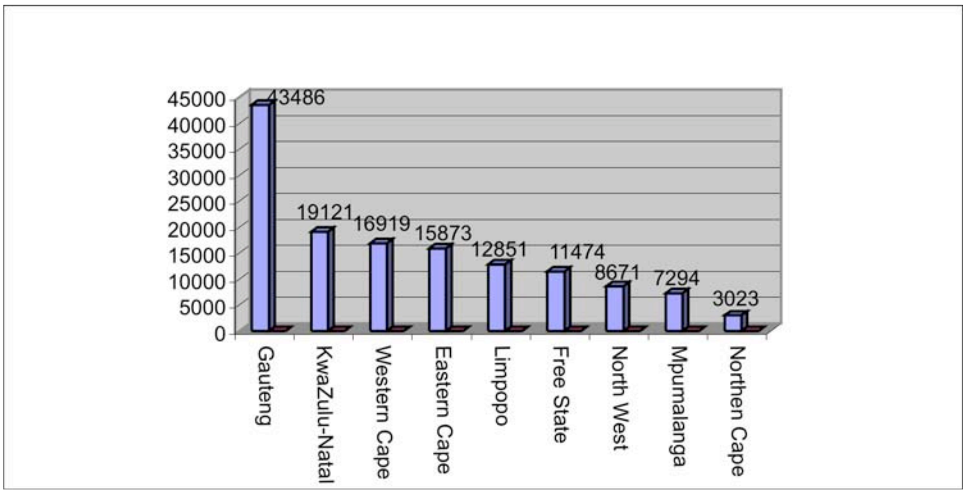
KZN has three technikons, (namely, ML Sulton, Natal and Mangosuthu) which have recently merged to form the Durban Institute of Technology. A merger is also proposed between the university of Durban-Westville and Natal. The university of Zululand is to focus its mission and become a comprehensive institution offering technikon-type programmes, as well as a limited number of relevant university-type programmes, with its future growth linked to the Richards Bay region (Department of Education, 2002).

Significantly, KZN has the highest percentage of FET institutions in South Africa - 18% of the 50 new FETs, followed by Gauteng and Eastern Cape province, both with16% (Powell and Hall, 2002). However, in terms of the participation rate, it is 2% for KZN, below the National average of 2.7%. The participation rate provides an indication of the extent to which the population, at national and provincial level, is enrolled for education and training in FET colleges. This suggests that KZN has the institutional capacity to supply the high level skills needed by its economy, but there are few people utilising it, as evidenced by student enrolment profile.

Of the total number of 138 172 students enrolled for FET in 2000 (figure 3.13), 63% were enrolled in four provinces: Gauteng (31%), Eastern Cape (11%), Western Cape (12%) and KZN (14%). It should be noted that these students were enrolled for both Department of Education (DoE) and non-Department of Education Programmes.

For Powell and Hall (2002), provision of non-DoE tertiary education is a proxy indicator of the extent to which FET colleges are responding to new market opportunities. Of the total number of students enrolled at FETs (138,172), 12% (16,853) were enrolled for non-DoE programmes. This pattern of enrolment within the two programmes varies across provinces. Unlike other provinces, in KZN, the Western Cape and Limpopo in excess of 15% of FET enrolments are in non-DoE programmes.

Figure 3.13 – Total FETs enrolled in FET colleges in 2000 by province

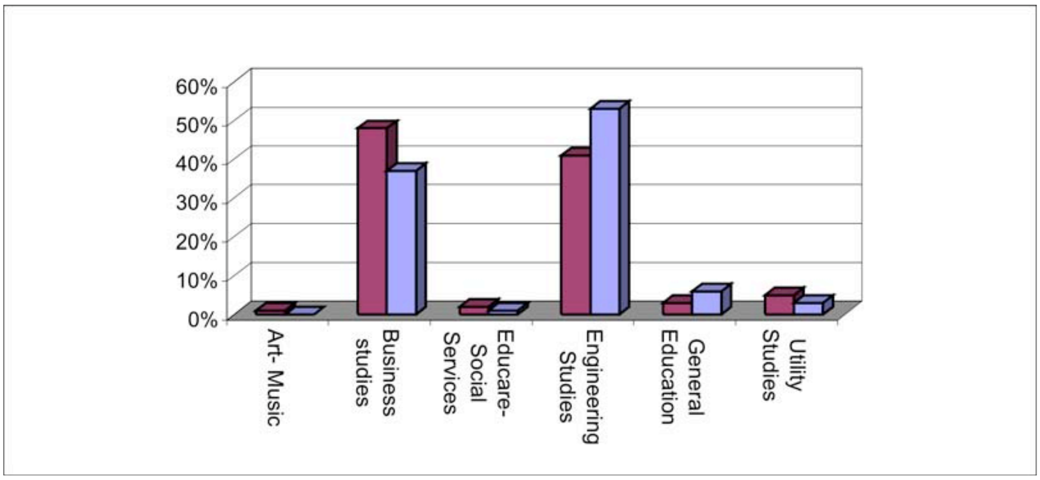


[Source: Powell and Hall (2000)]

The programmes presented at FET colleges offer some insight into the responsiveness of colleges to both economic and social needs. The programmes provided are categorised in six broad vocational fields: Art-Music, Business Studies, Educare–Social services, Engineering Studies, General Education, and Utility Studies.

Figure 3.14 illustrates the distribution of students across these vocational fields. Of total national enrolments in these fields, 89% are enrolled in two vocational fields: Business studies (48%) and engineering (41%). This trend is similar for KZN, with Business studies accounting for 37% of total enrolment and Engineering 53%. This pattern of vocational training suggests that there a closer alignment between the demand and supply of skills is emerging.

Figure 3.14 – FET enrolment for DoE programmes by vocational fields, 2000



[Sources: Powell and Hall (2000)]

The major objective of the new FET policy framework is to make FET institutions such as technical colleges more responsive to the needs of other education and training institutions, industry and local communities. FETs are also seen to play a role in the development of export- led growth in the marginalized SMME sectors and the informal and rural economies (Kraak, 1999). For these reasons, technical colleges need to align themselves appropriately to respond effectively to new skills needs in KZN province.

However, a study conducted by Kraak and Hall (1999) on transforming FETs in KZN found that a high degree of isolation from the broader education framework still characterises the large majority of colleges. Moreover, there are few links between technical colleges and senior secondary schools (General Education and Training Band), an area where innovative linkages are necessary for basic development of high skill human resources. There is some evidence of partnerships between Higher Education and Training institutions and FETs, mostly through satellite distance education.

The links between industry and institutions of higher learning in SA have not been formalised and this shortcoming is seen to limit economic growth potential in the long term. These linkages should be promoted not only in training for a more skilled labour force, but also in terms of assisting in the continuous improvement of plant processes and product innovation. In KZN, although colleges have responded in terms of course offering, they are not part of any strategic initiatives with employers to promote new employment sectors (Kraak, 1999). For example, the colleges appear to be completely uninvolved in the SDI development.

3.3.4 Drivers / impediments to growth arising from the status quo

Generally, South African institutions have not responded adequately to the demand emanating from industry. KZN's institutions are no different in this regard. They are still passive and dependent and have not been able to act independently of the state (Kraak and Hall, 1999). Although there are some exceptions, few attempts have been made internally at developing these institutions in order to break free from the bureaucratic chains that suppress innovation (Kraak, 1999).

The restructuring that is currently underway in all institutions of higher learning represents an important beginning in establishing a more regulated labour market environment that seeks to balance market responsiveness with the supply-side and longer-term skill formation. However, the new framework will not succeed on its own without the combined efforts of other cross-sectoral state planning initiatives. Critically, institutions of higher learning must align their programmes to the pattern of labour demand emanating from the generation of economic growth and job opportunities in key niche growth areas in the province. Without these complementary processes, both learners and trainees will continue to be trained by colleges for jobs that do not exist.

3.3.5 Take up of the national skills development strategy in KZN

Take up of the National Skills Development Strategy (NSDS) in KZN represents a key driver of the province's future human resource endowments. It was adopted by the Minister of Labour with the aim of overcoming, the structural rigidities and inequalities inherent from the apartheid era and to meet the dual challenges of social development and the need to compete in the global economy.

It also hopes to transform the labour force from a low skills base to one that is committed to high quality life long learning. Furthermore, it seeks to make the labour market more responsive and better able to cope with the consequences of poverty and disease on the work force; and finally to improve the employability of the country' workforce (NSDS, 2001).

The Skills Development Strategy is provided for in the Skills Development Act of 1998, through which employers pay a levy. While 1% of payroll Levy is placed on all firms, only those firms that train will qualify for a grant. The training strategy has a sectoral focus and is aimed at providing generic skills. It also attempts to address the constraints placed on first-time entrants to the labour market by putting in place a learnership system, which combine learning and work experience for job competence areas where there is a clear demand

On a sectoral level, twenty-five Sector Education and Training Authorities (SETAs) were established for linking the NSDS to economic sectors in the country. The NSDS programmes for both the employed and the unemployed have already been implemented in the country. The programme for employed workers is conducted through the 25 Sector Education and Training Authorities (SETAs) nationally and for the unemployed through the provincial departments of Labour.

SETAs are expected to perform the following functions:

- Develop sector skills plan;
- Promote the implementation of the skills plan in the sector;
- Promote and register learnership agreements;
- Collect and disburse skills development levies in the sector;
- Assists and encourage employers to prepare workplace skills plans and pay mandatory grant to employers who prepare such plan; and
- Improve information flow in the sector about employment opportunities in the labour market

Within the SETAs, training levels can be measured through skills levy payments and the disbursement of training grants to firms that develop workplace skills plans. For the year 2001/2002 the total amount collected from 120,225 firms was R3.2-billion (Department of labour, 2002). However, a mere 21% of the firms claimed back the levy, the majority of which are large firms. An analysis of workplace skills plans submitted to the 25 SETAs at the end of 2001, reveals that there are a minimum of 315,836 workers in structured learning programmes (Department of Labour, 2002).

A baseline study on training within South African companies, conducted by the Human Science Research Council, found there is a significant training variance across economic sectors (Kraak, 2000). Table 3.2 provides training rates per SETA. For KZN, this information sheds some light on what is happening within the main sectors in terms training.

Table 3.2 – Training rates per SETA

	Economic sector/SETA	Training rates %
1	Financial and Accounting Services	56.6
2	Banking	64.2
3	Chemical Industries	31.9
4	Clothing, Textile, Footwear and Leather	41.7
5	Construction	22.3
8	Energy	57.2
9	Food and Beverages	34.1
10	Forest Industries	24.9
12	Information Systems, Electronics and Telecommunication Technologies	35.8
13	Insurance	80.0
15	Media, Advertising, Publishing, Printing and Packaging	30.5
16	Mining	39.8
17	Manufacturing, Engineering	34.4
20	Primary Agriculture	16.2
22	Secondary Agriculture	14.8
23	Services	38.3
25	Tourism and Hospitality	40.6
26	Transport	33.7
27	Wholesale and Retail	57.0
	Total	44.9

The SETAs representing the key economic sectors identified in section 2 were contacted on numerous occasions with requests for information about the take-up of skills development in KZN. Unfortunately, none of them disaggregate this information at a provincial level. Even at a national level, this information is scanty and difficult to access.

Of relevance to KZN is the fact that the take up of funding for skills development through SETAs is extremely limited, particularly in the case of SMMEs. This is because firms of this scale do not have the capacity to develop workplace skills plans in order to access the funds, which they are entitled to through their contributions to the SETAs. This suggests that measures to facilitate access to these funds are a key policy priority for the DEDT.

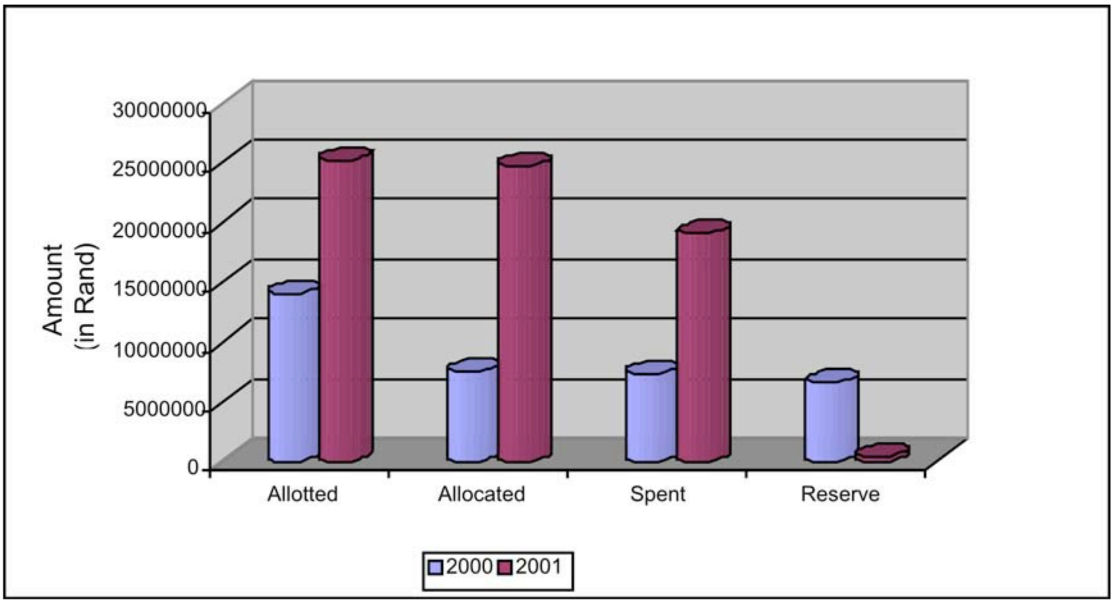
3.3.6 National skills development strategy: programme for the unemployed in KZN

The Department of labour has undertaken an ongoing restructuring of its unemployment-training scheme over the past five years. In theory, the focus has shifted from supply to demand driven systems of skills development. The provincial labour offices are now expected to analyse provincial needs in terms of the provincial economy, the provincial labour market and skill development in order to determine job opportunities in commercial, quasi-commercial and social development projects (NSDS, 2001).

The KZN provincial department have been taking up training of the unemployed through the use of the National Skills Fund (NSF). The total amount allotted for 2000 was R14-million and was increased to R25-million in 2001/2002. Figure 3.15

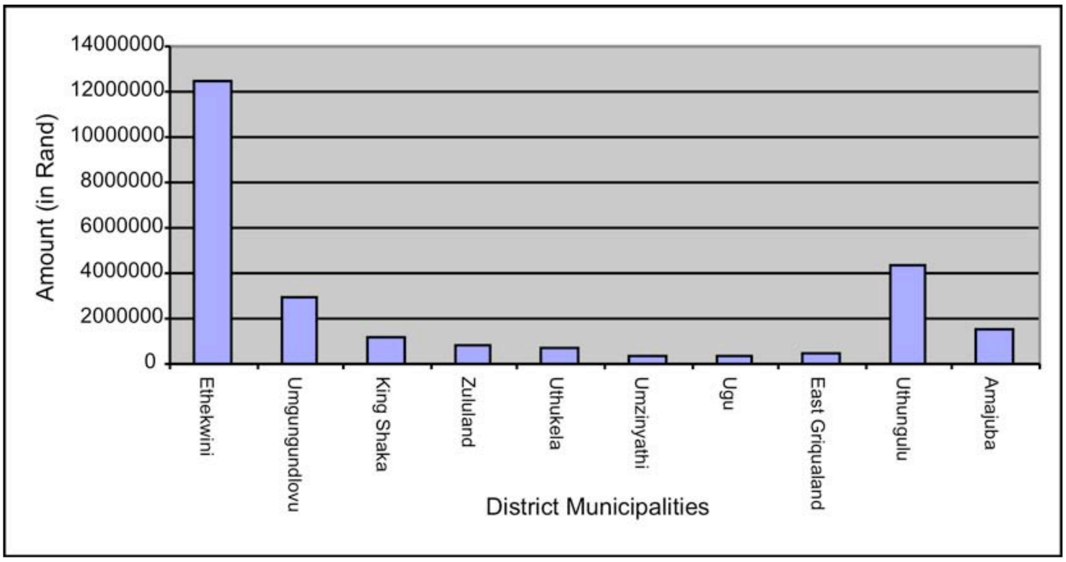
illustrates the distribution of these funds over the two years that the NSF has been in operation.

Figure 3.15 – NSF allocation to train the unemployed in KZN, 2000 and 2001



Of the total allotted by the NSF during 2001, R24.8-million (99%) was allocated to service providers by the KZN Provincial Skills Development Forum (PSDF). To date, R19-million (75.7%) has been utilised/claimed back by service providers. This is 23.3% lower than the overall spending rate for the year 2000. According to the KZN provincial department of labour (2002), the current spending rate is expected to improve as service providers finalise their claims for training conducted during the year.

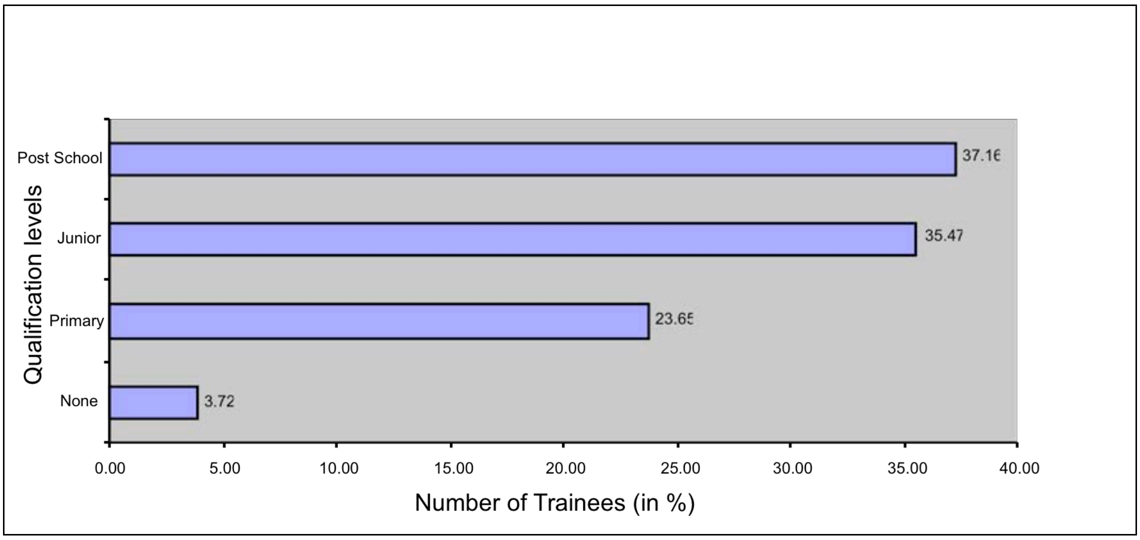
Figure 3.16 – Allocation of funds per district municipality, 2001/2002



Of the total amount allocated between January 2001 and March 2002, 49% was allocated to Ethekwini District Municipality. Uthungulu and Umgungundlovu District Municipalities were allocated 17% and 11% respectively. The remainder of the district municipalities were allocated between 2% and 6% each.

As illustrated in figure 3.17, the majority of trainees under TUP have a Post School qualification (37.17%), followed by those with a Junior Certificate qualification, who account for 35.47% of all trainees. With such a significant number of trainees holding post-matric qualification, the question arises as to whether it would not be more appropriate for the Department to engage with the Sector Education and Training Authorities (SETAs) to explore whether these learners can participate in learnerships.

Figure 3.17 – Qualification of trainees, 2002



In terms of the age of trainees, the majority of trainees were between 26 and 35 years of age (31.35%), followed by those aged between 19 and 25 years (27.45%). 36 to 45 years and 46 to 65 made up 21.27% and 19.10 respectively. The participants in the training programme fall within the 'youth' category, which is the focus of Objective 5 of the National Skills Development Strategy. Once more, the learnership option seems to be a way forward for KZN in this regard.

The NSDS intentions are good and there seems to be progress in its objectives in KZN. If strong coordination between different stakeholders, employers, service providers, and government is sustained, the skill level of the labour force can be developed in tandem with the demands emanating from industry. The effectiveness of this programme, however, depends on employment growth within the province, both in the formal and informal sectors.

3.3.7 Strategic interventions

In order to align the supply of skills with the demand emanating from growth sectors as structural change proceeds within the KZN economy, interventions should focus on forging strong partnerships between institutions of learning and industry. For schools, this will facilitate a process of learning about programmes in institutions of higher learning and the world of work. For higher education institutions, it will facilitate curriculum design, to render it more flexible and responsive to employer needs. It will also help these institutions to innovate and develop learning and teaching programmes that produce high quality graduates with the knowledge, competencies, skills and attitudes that are necessary to economic and social development. To make these partnerships effective, it is also vital that capacities within the province are developed for monitoring and interpreting labour market needs and trends.

3.4 Impact of HIV/Aids on the KZN economy

The challenges confronting the KZN economy in the realm of employment creation and skill formation are further complicated by the high prevalence of HIV/Aids in the province. It will impact on both the KZN labour market (by reducing the number and productivity of both skilled and unskilled workers) and the broader economy. It will also generate demand for health services, which opens an avenue for employment creation, yet creates further pressure on efficient health service delivery.

Given the anticipated profound impact of HIV/Aids on the South African labour market, and through it on a range of other economic variables, this section analyses the major findings and data relevant to the impact of HIV/Aids on the KZN economy. Most of the HIV/Aids projections are based on the assumption that significant changes or interventions will not occur to significantly redirect the trajectory of the HIV/Aids epidemic. The main factors that render the KZN economy vulnerable as a consequence of the extremely high prevalence of HIV/Aids are increased costs borne by the provincial government, businesses, households and individuals.

It is common cause that the HIV/Aids epidemic in KZN has historically been the severest and fastest growing compared to other provinces in South Africa. However, recent findings from the Mandela/HSRC study on HIV/Aids, based on a nationally representative sample of households, indicate that the prevalence of HIV/Aids in KZN may be less severe than the Antenatal Clinic surveys indicate.

3.4.1 Scope of the HIV/Aids epidemic in KZN

Findings from the Antenatal Clinic survey data (the most consistent HIV surveillance data tracking trends in terms of HIV and STD infections) indicate that KZN has the worst HIV/Aids epidemic relative to the rest of the country, as shown in Table 3.3.

Table 3.3 – HIV prevalence among pregnant women attending antenatal clinics by provinces, 1998 - 2001

	1998	1999	2000	2001
National	23%	22%	25%	25%
Eastern Cape	16%	18%	20%	22%
Free State	23%	28%	28%	30%
Gauteng	23%	24%	29%	30%
KZN	33%	33%	36%	34%
Mpumalanga	30%	27%	30%	29%
North West	21%	23%	23%	25%
Northern Cape	10%	10%	11%	16%
Limpopo	12%	11%	13%	15%
Western Cape	5%	7%	9%	9%

[Source: Department of Health, 2000, 2001]

In the period 2000 to 2001, HIV prevalence amongst pregnant women declined from 36% to about 33.5% (Department of Health 2001). The increase between 1999 and 2000 indicates that it is perhaps too early to ascribe the current decline to a generalised maturity of the epidemic in the province. Of note is the view that the KZN epidemic may be overestimated, especially given reported biases in the sampling of KZN sentinel sites. These are more often located close to main roads and transport routes with potentially greater exposure to high- risk groups such as truck drivers and sex workers (Colvin 2002).

In line with this assertion, the Mandela/HSRC study on HIV/Aids indicates that, compared to other provinces, KZN has the fourth highest HIV prevalence level at 11.7% amongst all persons of two years and older. Whilst this is substantially lower, it reflects HIV prevalence among all person two years and older, and is therefore not directly comparable to prevalence among pregnant women, generally regarded as a high-risk group. However, the same study also shows that the provincial HIV prevalence rate rises to 19.5% amongst women aged 15-49 years. This is still unacceptably high, and indicates a relatively mature epidemic among adult women.

Thus, even with more representative data, the impact of HIV/Aids will still be severe among key sub-groups in the economically active population in KZN. Of course, further in-depth analysis of the Mandela/HSRC study as well as follow-up studies, will add to the validity and reliability of HIV/Aids findings, both nationally and provincially. In the absence thereof, the projections that follow remain relevant, even if extrapolated from the antenatal clinic data.[16]

[16] The Mandela/HSRC study argues that the lower ranking of KZN prevalence rate may be ascribed to differences in sampling sentinel sites, as well as a relatively low proportion of informal settlements (5%), an indicator of high HIV prevalence.

HIV antenatal prevalence is projected to peak at 39% in 2005 before declining to 37% in 2010, as illustrated in Figure 3.18 (ASSA 2000).

Figure 3. 18 – Projected HIV antenatal prevalence rate for KZN and national 2000 - 2010 (ASSA2000)

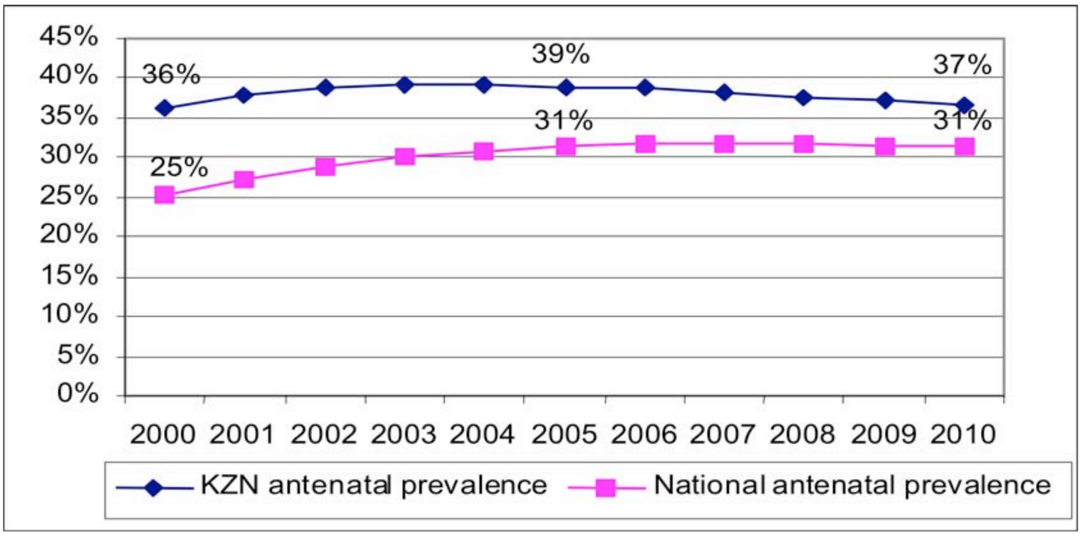
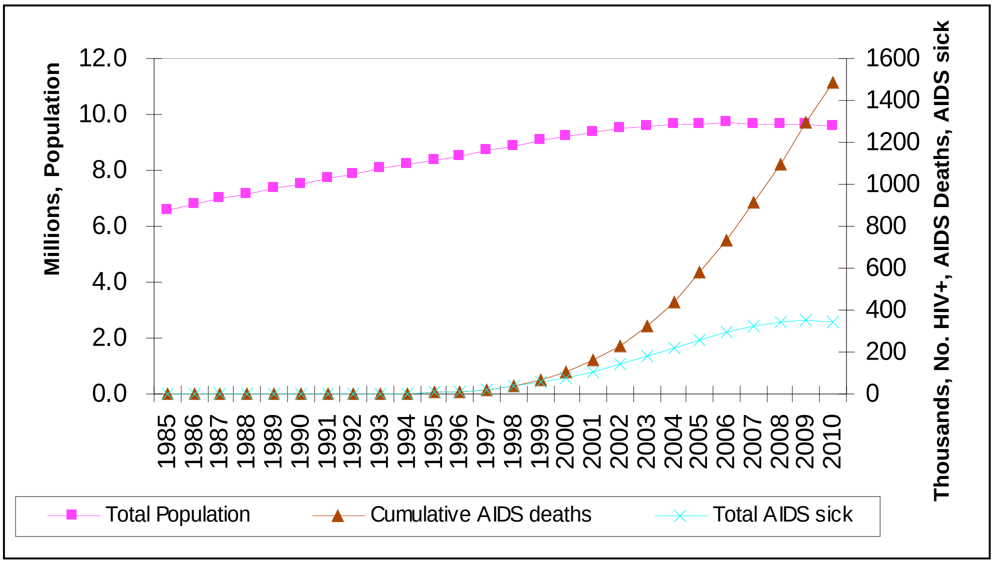


Figure 3.19 shows that the HIV epidemic is concentrated amongst KZN's economically active population, with a concentration in the 15-49 age group. HIV prevalence rates are high among adult men and women, with negative implications for the composition, size and growth of the labour force. Adult men have a particularly high prevalence rate, peaking at 36% in 2005.

Figure 3.19 – HIV prevalence rate for adults (20-65 years) adult men and women and the total population in KZN (ASSA2000)

In terms of projected Aids mortality, by 2010, 1.5 million people in KZN will have died of Aids, whilst just over 300 000 will have contracted Aids-related illnesses. Figure 3.20 shows that given the combination of cumulative Aids deaths, and an anticipated decline in life expectancy in the period 2000 to 2010, the projected KZN population will remain stagnant. This is in line with projected stagnant growth in the general South African population ascribed to Aids.

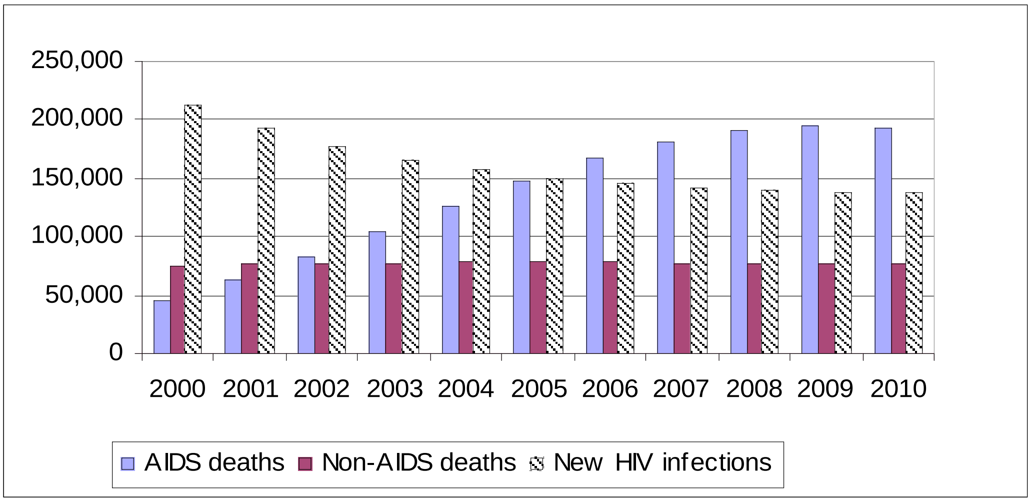
Figure 3.20 – Impact on the KZN population, cumulative Aids deaths and total Aids sick (1985 - 2010)



The most recent mortality data from the Medical Research Council (Dorrington et al, 2001) projects that in 2000, 40% of adult deaths in the age range 15-49 will be caused by HIV/Aids. Hence Aids will be the single biggest cause of death in South Africa.

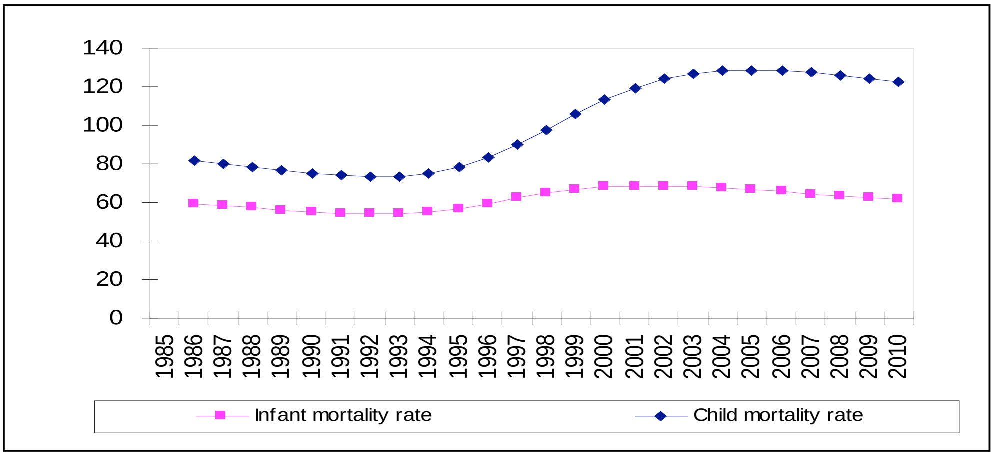
Figure 3.21 illustrates the swift increase in Aids-related deaths compared with non-Aids deaths commencing in 2002 and peaking in 2009. At the same time, the annual incidence of projected new HIV infections declines steadily from 2000, stabilising at below 150,000 by 2010.

Figure 3.21 – Projected annual Aids and non-Aids deaths and new HIV infections in KZN (2000 - 2010) ASSA2000



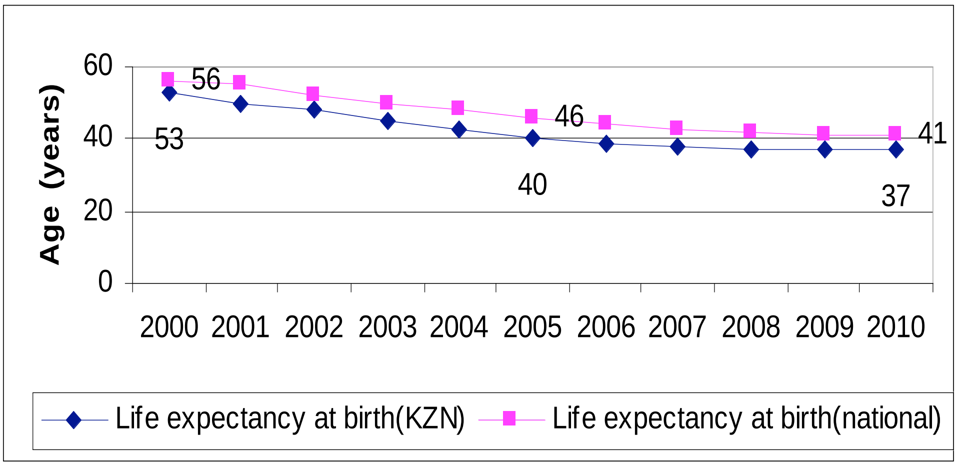
As a result of mother to child transmission (MTCT), mortality amongst infants (0-4 years) show some increases early in the decade, but remain at 1985 levels for the rest of the period as demonstrated in Figure 3.22. However, the projected child mortality rate (5-14 years) increases substantially over the period. This has negative implications for general school enrolment and completion levels, which have already declined significantly (Badcock-Walters 2000).

Figure 3.22 – Projected infant and child mortality rates in KZN 1985 - 2010 (ASSA2000)



Related to increased deaths among adults and young children is the projected decline in life expectancy at birth in KZN to below the national level, as illustrated in Figure 3.23.

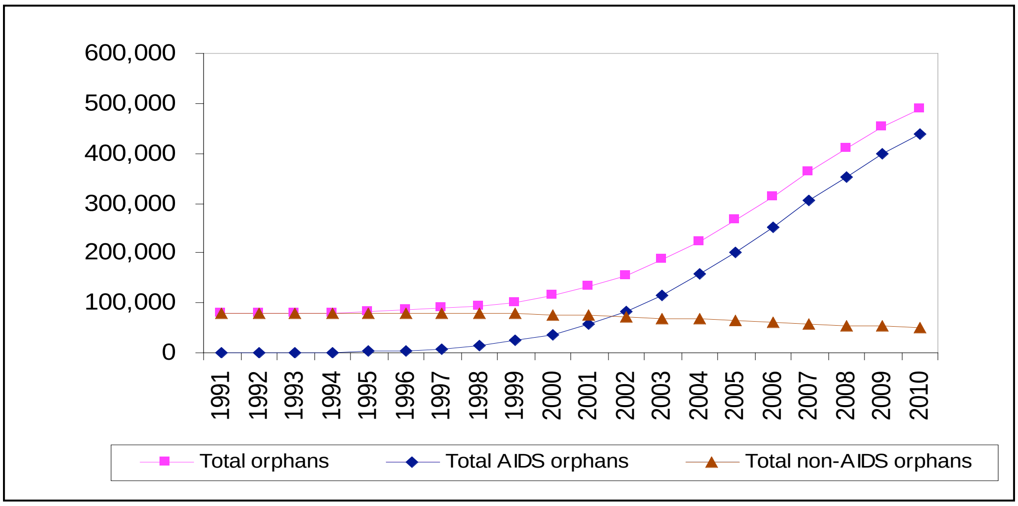
Figure 3.23 – Life expectancy at birth in KZN and national 2000 - 2010 (years) (ASSA 2000



[Source: ASSA 2000]

Figure 3.24 illustrates that the projected number of orphans - associated with the loss of parents due to Aids - is expected to rise significantly in the period 2000-2010. The reduction in the economically active population will place an increased burden on the social welfare system, to both place orphans with suitable families as well as finance the care of such children. The potential also exists for increased child labour as more orphans enter the labour market in search of more reliable sources of income.

Figure 3.24 – Projected total orphans, total Aids orphans, total non-Aids orphans (1985-2010) ASSA2000



[Source: ASSA 2000]

The grim picture emerging from the foregoing analysis of the current and projected prevalence of HIV/Aids in KZN, begs the question as to what constitutes the driving forces. There is a range of socio-economic and cultural reasons underlying the high level of susceptibility to HIV infection among the KZN population and the adult population specifically.

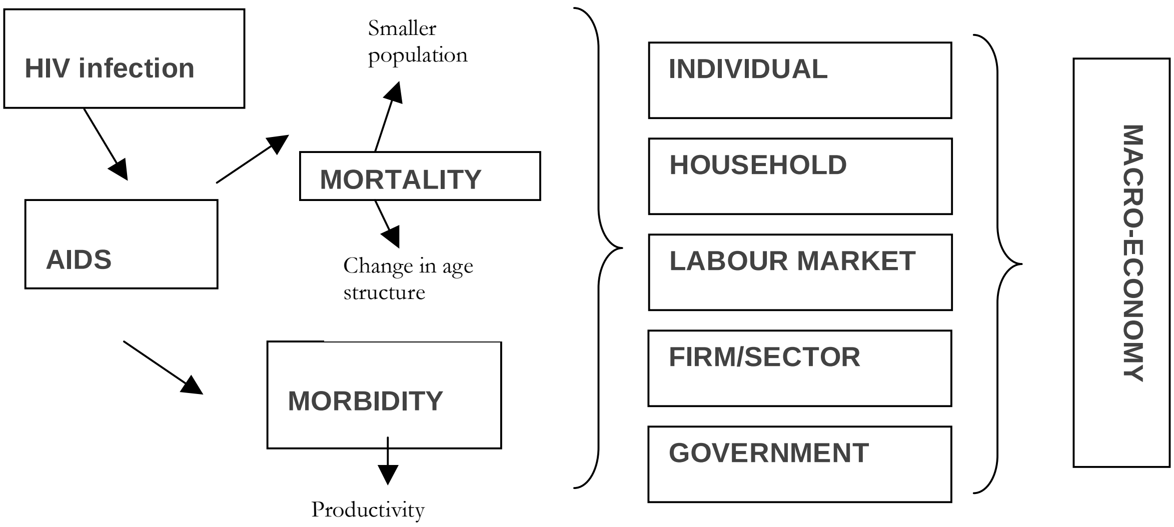
HEARD (cited in KZN Department of Health 2000:10) attributes the high prevalence of HIV/Aids to the following:

- A history of political violence leading to instability and high levels of displacement;
- Major transport routes including the trucking industry and the ports of Durban and Richards Bay;
- High levels of male absenteeism from families and communities;
- Urbanisation and squatter camps associated with rural-urban migration;
- High levels of mobility and migrant labour;
- High levels of unemployment;
- Poverty;
- Dominance of cultural traditions that affect poor and inconsistent condom use;
- Low social and economic status of girls and women; and
- The absence of male circumcision, which have been shown to reduce HIV transmission.

3.4.2 Impact on the KZN Economy

HIV/Aids has a negative impact on the overall economy as a result of the increased burden of Aids-related costs. There are many problems and limitations related to macro-economic modelling of the impact of HIV/Aids. However, it is generally assumed to progress through the main channels at individual, household, labour market, firm, sector and government levels as outlined in Figure 3.25.

Figure 3.25 – HIV/Aids channels of impact on the macro-economy



[Source: Badcock-Walters. 2002. HEARD, University of Natal]

There is no comprehensive analysis specific to the macro-economic impact in KZN, but it is possible to extrapolate national projections. It should, however, be noted that the impact of HIV/Aids is highly differentiated among households, firms and sectors. Thus, aggregate data tend to hide extreme scenarios at either end of the spectrum. Further, all projections and modelling exercises are based on underlying assumptions within which all results must be interpreted. Hence the analysis set out here should be regarded as indicators of likely trends. They should be subjected to ongoing scrutiny and verification through reliable empirical data.

The impact of HIV/Aids on the national economy has been summarised as follows, based on a macro-econometric simulation study BER (2001:2):

- A decline in the population and the labour force thus affecting the production potential (GDP) and expenditure;
- Increased direct costs and indirect costs to private business;

- Increased government expenditure given increased direct and indirect costs and increased demand for public health care and social welfare given the care of Aids orphans;
- Increased cost burden for households given additional non-discretionary expenditures on health care products and services as well as funeral costs.

The study also suggests that the decline in the population and the labour force are substantially larger than the decline in economic output, employment and income, when compared to a no-Aids scenario by 2015. These effects are echoed to varying degrees in other studies on the macro-economic impact on HIV/Aids. Given the higher incidence of HIV/Aids in KZN, the burden of these negative economic impacts will be disproportionately borne by this province.

HIV/Aids impacts on the economy through morbidity and mortality. The initial HIV infection is asymptomatic, but Aids-related illnesses and secondary infections such as tuberculosis and pneumonia develop within 6 to 8 years from initial infection in the absence of anti-retroviral (ARV) treatment. Once full-blown Aids develop, about 1 to 2 years from the onset of Aids-related illnesses to death, this translates into an absolute loss as the mortality increases and infected individuals die. Increased deaths leads to a decline in the size of the population, with projections that by 2015, the population will be 21% smaller. The projected reduction in the population growth rate is at zero percent in 2009, and enters negative growth of -0.5% by 2015 (BER 2001).

3.4.3 Impact on labour markets

Macro-modelling results indicate that Aids-related death and disability will result in a smaller labour force compared to a no-Aids scenario. The national labour force is projected to decline between 18 to 21% by 2015 (Quattek 2000, BER 2001). This is as result of the progression of HIV/Aids through the workforce and related impacts on life expectancy and mortality.

Table 3.4 illustrates the progression of HIV/Aids in the labour force and demonstrates how an initial wave of HIV infection will be followed after some time by increased Aids morbidity as the infected workforce contracts secondary Aids-related infections and illnesses and die. Thus, between 0-7 years after the initial HIV infection, the labour force will experience increased levels of morbidity as increased Aids-related illnesses contribute to temporary labour turnover as increased absenteeism and a general decline in productivity take place. This is followed by permanent labour losses as infected employees develop full-blown Aids, approximately 1-2 years before death or ill-health retirement (Rosen *et al*, 2001).

Table 3.4 – Progression of HIV/Aids in the labour force

Timeframe	Projected effect on the workforce	Effect on company costs
Year 0	Employee becomes infected with HIV.	No cost to company.
Year 0-7	Morbidity begins (secondary infections, increased absenteeism, sick and compassionate leave)	Morbidity-related costs (e.g. absenteeism, individual and workforce productivity, management resources, medical care and benefits)
Years 7 -10	Employee leaves workforce by resigning, retirement or death due to Aids.	Termination –related costs including death benefits from retirement benefits, funeral costs, loss of morale, loss of skills and experience, loss of workplace cohesion.
Years 7-10	Company hires replacement employee.	Turnover costs including recruitment, training, loss in productivity.

[Source: Rosen, Simon, Thea, Macleod and Vincent.2001. The impact of HIV/Aids on businesses in Southern Africa]

The composition of the labour force also changes as those in the age range 15-49 years are most hard hit, resulting in a potential age imbalance. Thus, the labour force becomes older as those closer to retirement stay longer in the workforce. Moreover, younger children may enter the labour force due to Aids orphan-hood and financial pressures.

3.4.4 Projected impact on companies

HIV/Aids increases the cost burden of disease to companies and sectors. The costs related to HIV/Aids morbidity and mortality, as summarised in Table 3.4 are of a direct, indirect and systemic nature. Thus, direct costs include contributions to employment benefits such as medical insurance, retirement, death, disability and funeral benefits. Other direct costs relate to the recruitment and training of new employees to replace employees lost to Aids, as well as HIV/Aids related prevention programmes such as peer counselling, education and awareness.

Critically, in order to control increasing labour costs companies may consider capital substitution, especially in labour intensive sectors such as consumer manufacturing, thus affecting employment levels. A concomitant outcome of increased costs is a decline in profit levels (BER 2001).

3.4.5 Projected national impact on main economic sectors

National projections by ING Barings (Quattek 2000) show that HIV/Aids will differentially affect economic sectors. Table 3.5 demonstrates that the rate of HIV positive workers per 100 workers is highest in the transport & storage, accommodation, agriculture, fishing & forestry and manufacturing sectors. These are all sectors that are important contributors to the growth of the KZN economy, thus increasing its overall vulnerability through increased morbidity and labour turnover costs. Increased vulnerability of these sectors also may impact on their capacity to generate future employment.

Table 3.5 – HIV-positive per 100 workers by selected main economic sectors (Quattek, 2000)

Sector	2000	2005	2010	2015
Finance and insurance	8.9	12.4	12.5	11.7
Business service	11.9	15.6	15.1	14.3
Communication	12.1	16.5	16.3	15.3
Health	14.9	20.0	19.0	16.6
Retail	16.2	21.3	20.7	19.3
Chemicals	16.6	21.6	20.7	19.3
General government	17.2	24.5	26.0	26.1
Consumer manufacturing	17.3	23.0	22.9	21.3
Agriculture/forestry/fishing	17.3	23.2	23.2	21.8
Accommodation & catering	17.9	23.0	22.2	20.8
Transport and storage	18.5	23.5	22.0	20.2

[Source: Adapted from WEFA as cited in Quattek, 2000: 49]

The prognosis for the public sector is more complex. Thus, whilst HIV prevalence and Aids death rates are relatively lower in the health sector, the general government sectors has among the highest rates. This points towards increased future volatility in labour supply and turnover in critical public sub-sectors, which will impact negatively on the capacity and efficiency of government to deliver services to general public and the private sector.

A study of educator demand in KZN (Badcock-Walters and HEARD 2001) finds that HIV/Aids will result in a decline in the supply of teachers and a decline in the demand for education. This may compromise the capacity of the education system to ensure a constant supply of sufficiently skilled labour to the rest of the economy. Moreover, given that the education budget constitutes the largest proportion of the provincial budget, the cost of replacement of educators will add a further burden.

3.4.6 Projected impact of HIV/Aids on skills levels on a national basis

The projections, by Abt Associates/Metropolitan and ING Barings in Table 3.6 and Table 3.7 show that *all* skill categories are significantly affected and have unacceptably high HIV /Aids prevalence levels even at high skill levels (BER 2001, Quattek 2000). The implication is that all sectors, irrespective of skill levels will experience losses in labour, increased labour turnover and decline in productivity as workers fall ill and die of Aids-related illnesses.

At the same time, the existing projections as well as anecdotal evidence also indicate that there is an inverse relationship between skill level and HIV/Aids prevalence levels. Thus, projections show higher prevalence levels for lower -skilled and poorer paid workers compared to higher skilled and better-paid workers

Table 3.6: HIV prevalence rate by skill levels[17] in the labour force: 2000-2015 Abt/Metropolitan

Skill levels	2000	2005	2010	2015
Highly skilled	7.2%	13.3%	16.7%	18.3%
Skilled	12.1%	20.2%	23.8%	25.4%
Unskilled	14.3%	22.8%	26.3%	27.6%

[Source: Bureau for Economic Research, 2001]

Table 3.7: Aids prevalence by skills levels: 2000-2015 Abt/Metropolitan

Skill levels	2000	2005	2010	2015
Highly skilled	0.3%	1.4%	2.7%	3.5%
Skilled	0.5%	1.9%	3.5%	4.2%
Semi-unskilled	0.6%	2.2%	3.9%	4.7%

[Source: Bureau for Economic Research (2001)]

Abt Associates (2000) project that the by 2010 the labour force will decline by 8% for the highly skilled, 10% for the skilled and 11% to 13% for the semi-and unskilled in the absence of replacement. These are indicators that in the context of the existing skill shortage, those sectors that are dependent on scarce skills will experience increased cost vulnerability.

The current structural inability to increase the pool of sufficiently skilled employees may increase the replacement needs of skill intensive sectors such as transport, manufacturing, chemicals, government and health. In the absence of anticipatory succession planning and training, the skills deficit may worsen as the size and quality of the skill pool decreases faster than the skills replacement capacity. Further, Quattek (2000) argues that an Aids-induced skills deficit may further contribute to obstacles to economic growth.

Whilst all economic sectors are vulnerable to increased Aids costs, those employing unskilled and semi-skilled workers may have reduced benefit and replacement costs, especially given the pool of unemployed. On the other hand, low risk sectors, such as finance and communication, employing high skilled employees may face increased costs related to benefit and replacement costs.

3.4.7 Impact on national economic indicators

The main macro-economic impact studies conclude that Aids will reduce the size and growth of the economy. Arndt and Lewis (2000) predict that year on year GDP growth rates will decline to 1% until 2008, with slight improvements into 2009 and 2010. By 2010 real GDP will be 17% lower than a no-Aids scenario.

[17] Highly skilled include managers and professionals; skilled included technicians and assoc professionals and artisans; semi-and unskilled include sales and service workers, clerical and elementary occupations.

The BER (2001) concludes that the economic impact of HIV/Aids will be negative in that all major economic indicators will be declining. In comparison with a no-Aids scenario, real GDP is projected to be 1.5% lower by 2010 and 5.7% lower by 2015. Thus year on year GDP growth rates will decline by an average of 0.5% per annum over the period 2002 to 2015.

ING Barings projects that real annual GDP will decline by 3.1% in 2006 to 2010, whilst in 2011 to 2015 it is expected to decline by 4.7% (Quattek 2000) By 2015 the average year on year GDP growth will be 0.3% to 0.4% lower than the comparable rate under a no-Aids scenario.

While the size of both the economy and the population will be smaller, per capita GDP will decline by 8% by 2010 compared to the no-Aids scenario. This will reduce private discretionary expenditure, which will disproportionately be spent on essential health and food costs (Arndt and Lewis 2000).

In spite of the differing results on HIV prevalence for KZN as noted earlier, the negative macro-economic impacts surveyed here will be significant for KZN, because the province has amongst the highest, if not the highest prevalence of HIV/ Aids within the national economy.

3.4.8 Impact on employment, unemployment and wages

It is predicted that the demand for labour, particularly unskilled labour, will decline due to the slowdown in economic growth. Hence employment levels will not increase, whilst the unemployment rate will not change significantly. Arndt and Lewis (2000) predict that unemployment among the unskilled increases marginally, but not resulting in major changes in the overall unemployment rate. This is largely due to the offsetting effect of an Aids-induced reduction in the unskilled labour force and a reduction in labour demand due to slower economic growth.

Wage rates, especially at skilled level, will increase as a consequence of skill shortages. However, this will be offset by increased direct costs related to benefit payments by the private and public sector and productivity declines. The overall result is a decline in the demand for labour (BER 2001).

3.4.9 Impact on the public sector

Most macro-economic projections conclude that public sector costs, both direct and indirect will increase. The main contributory factors relate to increased benefit and replacement costs of public sector employees (BER 2001). Further, given the limits of private sector health care provision, there will be an increased demand for public health care. The decline in the economically active population and the accompanying increases in Aids orphans means that demands on social welfare grants such as old age pensions and child grants are assumed to increase. Most projections assume that government will increase its current expenditure away from fixed or capital spending or shift expenditure between various functions (BER 2001). A possible increase in the budget deficit is projected compared to a no-Aids scenario (BER 2001).

Health and welfare are concurrent functions of both national and provincial governments. Thus, increased pressure at national level on public spending will be exacerbated at the provincial level.

3.4.10 Implications for the KZN economy

In summary, the HIV/Aids epidemic will have a profound impact on the KZN economy. From the perspective of policy-makers, the following implications are pertinent:

- Given the severity of the HIV/Aids epidemic, KZN will experience significant declines in the size and nature of its population and labour force;
- Economic growth is likely to decline, although by a much smaller margin than the projected contraction of the population and the labour force;
- The impact on labour and skill supply will pose problems for vulnerable sectors. In particular,
- Economic sectors, such as transport, tourism (see accommodation and catering) and manufacturing that are drivers of the provincial economy are vulnerable given increased labour turnover and replacement costs;
- In the public sectors, health and education are especially vulnerable in terms of responding to the increased demand for public healthcare, as well as the reduced capacity of education to supply labour to the rest of the economic sectors;
- Private sector costs are likely to increase which will translate in a decline in labour demand and lower fixed investment;
- Public sector spending is likely to increase, putting pressure on the provincial budget.

These are aggregate impacts, which may disguise more nuanced dynamics at a provincial level. Given the highly differentiated impact of HIV/Aids at a provincial level, an economy wide analysis may not be adequate to develop a provincial strategy to mitigate the negative economic impacts.

In terms of the identification of the level of risk faced by key economic sectors and strategic planning on skills replacement needs and requirements, the analysis is constrained by the lack of empirical data specific to KZN.

The aggregate data point unequivocally to an increased burden of disease, translating into increased costs at household, firm, sector and government levels. In order to mitigate these effects at provincial level, a multi-sectoral approach that is inclusive of all the major stakeholders in the KZN economy is required.

3.5 Conclusion and synthesis

The analysis of unemployment, HRD and the prevalence of HIV/Aids in the KZN economy highlight the importance of a people-centred approach to economic development. Unless KZN's economic development trajectory is able to create jobs and develop skills, it will not enhance the lives of its people. Moreover, the high prevalence of HIV/Aids will be costly to the economy in terms of both its negative impact on growth and the resources required to provide care for those that are afflicted.

Strategies to create employment and enhance skill formation should be guided by the reality that the potential for mass employment expansion in South Africa through labour intensive exports is quite limited. In a context of small and slow growing domestic markets, it is reasonable to assume that employment expansion will depend on foreign markets as an important source of demand. Although jobs can be generated through exports, expectations that large unemployment problems can be directly addressed in this way are unrealistic for middle and high-income economies. In this context, tradables can create some jobs, but will be more important for growth, incomes, foreign exchange, productivity and technological learning. This feeds fiscal and intra-household transfers that support greater employment generation and a wider distribution of income.

Reliance on a labour intensive exports strategy – which appears to be the direction taken by national government - is unrealistic in a middle-income economy as it depends on low wage competition. To maintain this as a *dominant* employment generating strategy for any length of time, it would be necessary to continuously reduce the cost of living (through, for example, price controls on wage goods and the generous provision of a social wage as a proportion of incomes) or reduce real wages (either through exchange rate devaluations or some sort of wage control). Otherwise, it is unlikely that these goods would be competitive in international markets.

Workers in a middle-income country must earn wages that reflect the cost of living. Otherwise, the human resource is undermined. In a country with a small domestic market, this requires that the production structure and the export profile reflect this cost structure. High productivity industries generally pay workers with the same educational attainment more than lower productivity sectors. A greater reliance on higher value-added exports should raise national income and reduce business cycle volatility, with important knock-on effects for domestic firms generally. A longer-term strategy can focus on expanding the number of investments that fall within this category. However, with high productivity and strong local linkages, these sectors are unlikely to generate substantial net new employment in the medium term.

The most likely avenue for creating more employment is by increasing effective domestic demand for more employment-absorbing, low labour productivity non-traded goods and services. 'Non-traded' is distinct from non-tradable: most goods and services can practically be traded, but some are more oriented toward the local market, such as construction, or social services. Some products, such as maize and wheat, are traded, but here we refer to its domestic distribution.

In the context of a relatively small productive base, and a large un- and under-productive sector, the balance between high productivity, income generating sides of the economy and sustainable transfers to socially useful lower productivity activities is quite critical, particularly if sustained for a lengthy period of say 10 to 15 years. Over this period, it is expected that the higher value sectors would expand, and that net new entry to the labour force would diminish due to falling birth rates and HIV/Aids.

4 The role of provincial government in economic development

4.1 Introduction

Having analysed the KZN economy and its labour market, this section turns to an analysis of the role provincial government should play in the region's economic development process. Economic development involves a range of actors, with government, the private sector and organised labour generally occupying a pivotal position in the process. The three tiers of government – national, provincial and local – have distinct roles and policy instruments for promoting economic development.

This section sets the parameters within which the KZN government can intervene in the provincial economy to realise a set of defined objectives. To that end, a brief survey of international experience with respect to regional development (as distinct from local economic development which is the domain of local government) is provided to elicit the key issues confronting practitioners tasked with fostering economic development at a provincial level.

In order to demarcate the role of provincial government in relation to national and local government, an overview of the roles and responsibilities of the three tiers of government is presented. Finally, the instruments available to the KZN province, in the form of the existing institutional framework to drive regional development are surveyed.

4.2 International experience

Historically, the global trend has been for regional development policy - in the form of measures to shift economic activity away from metropoles and towards depressed areas – to be driven by central governments. Over the past two to three decades, however, there has been a shift to the decentralisation of decision-making with respect to local and regional development, underpinned by the devolution of power to provincial and local governments and fiscal decentralisation.

This has given rise to a new paradigm for economic development as evidenced by the centrality of local economic development and regional development as instruments of development policy. In South Africa, this trend emerged relatively late, after the democratic election of 1994, and hence is in its infancy relative to global trends and experience.

The removal of trans-national boundaries to the movement of capital, goods and labour – i.e. globalisation – has reinforced the central role of second and third tier government in promoting economic development. This is because "[A]s world market integration proceeds, all cities and regions must specialise and trade to maintain employment and growth" (Markusen, 1995:12).

Consequently, a development model in which provincial and local governments wield greater discretion over infrastructure provision and economic development incentives is currently in vogue the world over. Moreover, the marginalisation of geographical factors in mainstream economic analysis has been redressed by a recent body of research. This was made possible by an improved understanding of factors that influence the spatial concentration of economic activity. In essence, it is posited that if average production costs decline as the scale of production increases, either at the firm, industry or regional level, then it will be beneficial to concentrate production in particular locations (Lall *et al*, 2001).

The manner in which provincial governments can reduce production costs through fostering agglomeration economies and other measures to reduce the cost of doing business (such as the provision of efficient infrastructure and the elimination of bureaucratic red-tape) in order to attract economic activity to their jurisdictions had become a preoccupation of scholars and practitioners in the sphere of regional development. Hence Begg (2002) argues that regional policy has focused at times on inward investment, but has also had phases where small firms or 'clustering' have been in vogue. In addition, attempts to promote science-based industry or to develop retailing, financial services or tourism have also featured prominently.

Shankar and Shah (2001) in an empirical analysis of 8 industrial and 17 developing countries find that countries experiencing divergence in regional per capita incomes have adopted interventionist policies to foster regional development. In contrast, countries experiencing convergence have had a hands-off approach to regional development. Instead, they have focussed on the removal of barriers to factor mobility and ensuring minimum standards of basic services across the nation. This finding is not surprising, as the uneven performance of regional and local governments empowered to drive development is likely to result in an uneven spatial allocation of economic activity.

4.2.1 Agglomeration economies

Agglomeration economies, occupy a central role in the literature on regional development. This is because decentralised policy may be more efficient in determining industrial location, as it is difficult for central government to gauge scale and agglomeration economies and diseconomies in specific regions (Markusen, 1995).

Market access, localisation economies and urbanisation economies are the key factors underpinning agglomeration economies. Access to markets - including to inter-industry buyers and suppliers - is a well-documented determinant of location as it reduces the cost of accessing inputs and transporting outputs. Localisation economies give rise to intra-industry benefits where firms locate in close proximity to firms in the same industry. Such benefits include access to specialised know-how (i.e. knowledge diffusion), the presence of buyer-supplier networks and opportunities for efficient sub-contracting. Employees with industry-specific skills will be attracted to such clusters giving firms access to a large specialised labour pool.

In contrast, urbanisation economies accrue from being located in close proximity to firms in *other* industries. These inter-industry benefits include easier access to complementary services (for example, publishing, advertising and banking), availability of a large labour pool with multiple specialisation, inter-industry information transfers, and the availability of less costly general infrastructure such as telecommunications and transport hubs.

Based on these mechanisms for enhancing competitiveness, the international literature identifies the creation of industrial clusters as a primary instrument of regional industrial policy. In this context, the role of provincial governments in unlocking economic potential is to identify industries that can be organised into clusters and facilitate their creation. The agglomeration economies that clusters generate become a cost-reducing (and hence competitiveness-enhancing) factor external to the firm, which is attainable through spatial location.

In relation to agglomeration economies, theoretical and empirical work on economic geography (Henderson *et al.*, 2001) suggests that the net benefits of industry concentration and location in dense urban areas are disproportionately accrued to technology intensive and innovative sectors. This is because the benefits of knowledge sharing and access to producer services are considerably higher in these sectors than in low-end manufacturing that employs standardised production processes. Hence these innovative sectors can afford the high wages and rents in dense urban locations and industry clusters. In contrast, low-end industry producing standardised products can be expected to move to smaller urban centres with lower costs.

Paradoxically, in developing countries there is a considerable range of standardised industrial activity in large cities. This is certainly the case in South Africa and in the KZN province, as evidenced by the concentration of manufacturing activity in the city of Durban. For Lall *et al* (2001) this is due to the lack of inter-regional transport infrastructure linking small centres to large urban areas. In the South African context it is probably also due to historical patterns of spatial development.

From a policy perspective, endeavours to create agglomeration economies through intra-industry and inter-industry clusters are a key challenge for KZN. The access and proximity to trans-shipment hubs offered by locating in the KZN province is a competitive advantage upon which to build. Moreover, the success of nodal developments (in the form of SDIs and IDZs) is dependent on the identification and promotion of clusters that harness agglomeration economies to enhance the competitiveness of the industry and locate it within global supply chains.

4.2.2 Investment promotion

The decentralisation of the role of the state in economic development to second and third tier government has been accompanied by increasingly higher levels of competition among provinces and localities for investment. Hence the promotion of inward investment has become a key policy objective of provincial governments the world over. It is widely acknowledged that attracting an investor may trigger virtuous circle effects by inducing further investment in complementary activity. This is why investment promotion is a central instrument of regional policy.

From the perspective of the investor, a more attractive location is one that facilitates productivity gains, with the source of these incremental gains being largely external to the firm or agency making the investment. Many facets of the business environment external to the firm will bear on investment decisions. These include the availability and quality of commercial or industrial property, the characteristics of the local labour market, social factors (including crime and personal security), transport and accessibility, regulatory and planning considerations, and the quality of local services. Hence, a strategy to induce a greater level of investment must first assess regional strengths and weaknesses and identify the most pressing priorities for improvement, relating these to the needs and expectations of different categories of investors.

From a policy perspective, the determinants of the attractiveness of a location may conceptually be divided into four areas: public capital, factor markets, social factors and governance factors (Aschauer, 1989; Lawless & Gore, 1998; Gordon & McCann, 2000). While some are amenable to policy action, many lie beyond the immediate control of provincial policy makers, though it is sometimes possible to influence them.

The role of publicly funded infrastructure in improving the productivity of firms has been extensively studied. The implication of much of this research is that public capital is often under supplied and thus that many areas would obtain sizeable increases in investment by devoting resources to enhancing infrastructure (Aschauer, 1989, Mikelbank & Jackson, 2000).

Of note is the fact that airport access is becoming increasingly important for many forms of activity, especially where the potential investor employs a high proportion of professional staff, and inadequate access to frequent air services may be a major deterrent. Indeed, it has been found that urban growth is correlated with per capita air traffic, suggesting that there may be an advantage in having adequate access to hub airports (Goetz, 1992). In addition, more specialised forms of infrastructure, notably advanced telecommunications, are especially relevant to high-tech industries or to advanced services, and can vary greatly in quality between locations.

The nature and development of markets for factors of production (labour, capital, land and premises) will affect the attractiveness of an area in diverse ways. Aspects of the labour market that prospective investors tend to focus on include the availability of crucial skills, the character of the workforce and prevailing wage rates. However, these are attributes of the local workforce that may be transitory or susceptible to changing economic circumstances. Hence Begg (2002) argues that flows into the labour market, the provision of training and the adaptability of the institutional structure to shifting skill demands will also matter.

Key determinants of flows into the labour market are the demographic make-up of the area and the scope for reinforcing the indigenous labour force either by drawing in commuters or by inward migration. Commuting relies on an efficient transport system and the presence of adjacent labour supply, while the opportunities for migrants will be affected by housing availability and social conditions, hence housing market decisions affect the supply of skills. Many of these dynamic elements of the labour market are amenable to policy actions.

Property rents or purchase costs, site availability and the quality of premises are important considerations for potential investors. Here too, however, the dynamics are important; if developers regard an area as promising, it is more likely to have the sort of renewal in the supply of property that will meet emerging investor demands.

Access to capital markets differs between classes of investors while the impact on prospective investors of variations in the character of national or sub-national financial intermediaries will depend on how easy it is to tap alternative sources of funding. Small firms typically face much more limited options, making them more dependent on local conditions than larger firms. The availability and terms of loans and start-up capital vary between localities, not just because of differing institutions but also because of the disposition of practitioners. Begg (2002) argues, for example, that venture capitalists often follow property developers by excluding entire classes of investment from consideration.

In addition to public capital (to finance infrastructure) and factor markets, social factors play an important role in attracting investment. While the links between social cohesion and competitiveness are widely believed to be crucial, they are poorly understood. The evidence suggests, however, that social cohesion in the sense of the 'togetherness' of a community helps to foster innovation and institutions that underpin competitiveness (Keeble & Wilkinson, 1999; Gordon & McCann, 2000). Clearly, crime (or the threat of it) is viewed as a deterrent to investment, in so far as it increases the costs of security and insurance, and has an adverse impact on staff.

Cultural attributes are increasingly being seen as important 'assets' that contribute to the ability of an area to pull in tourists and day-trippers, and to the broader appeal of the locality for residents and/or employees. This is evidenced by the galvanizing effect on the local economy of the development of a performing arts centre in Newark (Strom, 1999) and the ability of the new Guggenheim museum Bilbao to induce complementary investment (Plaza, 1999). At the same time, 'cultural industries' themselves are a growing proportion of economic activity as illustrated by two US cities – Memphis and Hollywood – where a coming together of creative and other forces led to an upsurge in innovation. (Hall, 2000).

The final factor that influences a region's ability to attract investment is governance. Clearly, it is an area over which provincial and local policy-makers have considerable influence. Regulatory factors impinge on the investor in several different ways. Planning decisions, for example, set explicit limits on what an investor is allowed to produce or the processes that can be used. Noise restrictions, curbs on working hours or controls on emissions are good examples. Such controls would be expected to add to operating costs because of the need to adopt more costly technologies or the loss of flexibility in operations. More subtly, regulatory signals, such as the stance of land-use planning offices regarding possible uses of sites, can be expected to percolate into perceptions of how suitable an area is for different sorts of investment projects. Similarly, decisions that discriminate for or against particular transport modes will alter the balance of feasible projects.

How rapidly the planning system functions, the responsiveness of government agencies in dealing with prospective investors and the fiscal arrangements in an area are just some of the relevant aspects of governance. Incoherence in governance, particularly between different tiers of government, will clearly deter potential investors and frustrate a region's economic development agenda.

Recent literature has focused on the role of different agencies in promoting inward investment. The capacity to assemble a package of support measures (which goes beyond site assembly and direct subsidies to include such 'extras' as the reconfiguration of training or mediation between the inward investor and potential sub-contractors) is seen as important. The speed and ease with which planning authorization for major sites is granted is central and may have tip the balance on certain high-profile location decisions.

In sum, the review of international literature has identified measures to foster industrial clusters in order to enhance competitiveness through agglomeration economies, and measures to promote inward investment as the cornerstones of regional development policy. The scope for regional governments to translate these policy imperatives into policy instruments will, however, be delineated by the resources and powers allocated to them within the intergovernmental system.

4.3 Regional development: the powers of provincial government in South Africa

South Africa has three spheres of government with significant decentralisation of powers, functions and budgeting between them. In the post-1994 period, the devolution of power from national to provincial government has been significant, as evidenced by larger proportions of the national budget being allocated to second tier government. As regards economic development, central government sets the parameters within which provincial and local strategies are framed.

In terms of the Constitution, national and provincial governments are concurrently responsible for functions like school education, health, welfare and housing. National government's role is primarily to determine policy, while provincial governments shape some policy and have a considerable role in implementation. Exclusive functions for provinces include provincial roads and traffic, abattoirs, provincial planning and provincial sport.

Most local government functions involve services with user-charges like electricity, water and sanitation, but they also provide public goods such as municipal and household infrastructure, streets, streetlights, and refuse collection. Related to the re-demarcation of municipal boundaries, processes are underway to decide on a final assignment of powers between district and local municipalities.

South Africa's intergovernmental fiscal system is based on a revenue-sharing model, with provinces largely dependent on transfers from the national government, while municipalities are only partially dependent on such transfers. The crux of the financial arrangements for provinces is that revenue raising is, by and large, reserved for national government. Their main source of revenue is from an equitable share of national revenue and other conditional grants from national government.

The most important source of revenue is the equitable share to which they are entitled under the Constitution to fulfil their executive obligations. The equitable share is an unconditional allocation to provinces. It is consistent with the notion of relatively autonomous provinces with the constitutional responsibility to govern in certain areas.

Expenditure patterns among the three tiers of government reflect the fact that in the realm of basic services, national government's role is one of policy making, with provincial and local governments play a central role in the provision of social and basic services. For example, in 2001 national government retained 40.5% of the R208-billion it had raised, allocating 56.4% to provincial government and 3.1% to local government (Budget Review, 2001).

Provincial governments have the largest spending budgets. They are responsible for the implementation of major social services, including school education, health (including academic and regional hospitals, as well as primary health care), social grants and welfare services, housing and provincial roads. Since these functions have limited or no cost recovery potential, provinces are largely dependent on transfers from nationally raised revenue. Indeed, in 2001/02, of the R121.4-billion provincial budget, only R3.9-billion (3.2%) was own revenue, while the balance was a transfer from national government.

Local government has more fiscal capacity than the provinces. Although there are large variances among municipalities, they raise on aggregate about 90 percent of own revenue. Municipalities can raise property tax and turnover/payroll regional levies on businesses, as well as user charges (and a surcharge) on the provision of electricity and water. However, although budgeting on the expectation of collecting all their revenue, many municipalities do not collect a significant portion of revenue due. This results in deficits at the end of the financial year.

Refinement of the intergovernmental fiscal system to improve national and provincial support to local government is currently being considered. There is a also a concerted attempt to enhance cross-sphere linkages in local planning and budgeting, through the Integrated Sustainable Rural Development Support Programme and the Urban Renewal Strategy.

In line with the Constitution, many national and provincial departments are deciding which of their functions are best performed in the local sphere, and should be devolved to local government. Functions under review include housing delivery, primary health care and the district health system, water and municipal policing. Decentralisation of management is also being considered, for functions like education (to regions), health (to districts and hospitals) and justice (cost centres at local court level.

In terms of promoting regional economic development, provincial governments have concurrent legislative and executive power with national government over matters such as agriculture, public transport, tourism, urban and rural development and trade and industrial promotion. In practice, their knowledge of the provincial economy places them in a strong position to provide strategic direction to its development in cooperation with national and local government.

In the case of industrial policy, national government's powers to alter customs duties (within the framework of the regulations of the World Trade Organisation) and design and administer supply-side measures means that the DTI effectively determines the parameters within which growth and development takes place. The translation of national-level industrial policy into concrete developments on the ground is, however, driven by provincial and local governments (especially those of the scale of Durban and Richards Bay).

The relatively recent devolution of power in South Africa away from the centre and towards the second and third tiers of government has meant that the institutional framework for cooperation between the three tiers is not well developed and the relevant role of each tier is not well understood.

This is illustrated in the case of the implementation of spatial development initiatives (SDIs), which together with industrial development zones (IDZs), are the only measures implemented by national government to influence the spatial distribution of economic activities. In an evaluation of SDIs, Altman *et al* (2001:2) find that although they were meant to fast-track processes, "some local and provincial officials feel that they may have inadvertently slowed processes down". Moreover, they argue that the national DTI's role in regional development may be more appropriately centred on strong national policies and programmes that can be utilised by regional institutions.

In sum, within the intergovernmental system, the scope for provincial government to drive economic development by providing strategic direction to the provincial economy is considerable. The DEDT's contribution to KZN's economic development lies in the fact that it is sufficiently far removed from the centre to focus on the specific needs of the KZN province, but has a macro view of the provincial economy and its potential synergies across space as it is not narrowly focussed on a particular locality (as is the case with local government). Once the strategic direction has been determined, it is necessary to cooperate with first and second tier government in order to maximise the range of policy instruments available to meet well-defined objectives. The institutional framework within which this cooperation is forged currently constitutes a critical challenge to the success of KZN's industrial strategy.

4.4 Institutions promoting economic development in KZN

A number of key institutions – including the DEDT, Ithala, Trade and Investment KZN (TIK) and Tourism KwaZulu-Natal (TKZN) – are tasked with promoting economic development in the KZN province. Their powers and functions, as well as the mechanisms at their disposal to execute their mandates, collectively represent the instruments available to the province for achieving its economic development objectives.

4.4.1 The department of Economic Development and Tourism (DEDT)

The Department of Economic Development and Tourism, KZN is the provincial government department responsible for economic and tourism policy. The strategy framework guiding the DEDT is that of the 1996 Provincial Growth and Development Strategy (PGDS), which is centred around seven core programmes elaborated upon below.

Programme one: building the winning province

The core objective of this programme is to open up KZN to the economic opportunities presented by trade and tourism by addressing four elements, namely:

- Improving the commercial, financial and service sectors of KZN through the integrated development of the ports and transport infrastructure, the facilitation of exports and development of the SMME sector;
- The promotion of KZN as a gateway province;
- The use of tourism as a lever for job and wealth creation; and
- The delivery of services and facilities as an economic activity.

Programme two: enabling local economic development

Provides a framework for the formulation of sustainable local strategies and linkage of service delivery to local economic activities.

Programme three: fuelling the powerhouse

Addresses the need for industrial expansion through the promotion of:

- Lead industries (including food and beverages, pulp, paper and wood, plastics and non ferrous metals) and labour intensive industries (textile and clothing, automotive and construction) and industrial restructuring;
- Support for agricultural production and processing;
- Encouraging export promotion;
- The development of a housing market; and
- Augmentation of bulk infrastructure networks.

Programme four: addressing the needs of the poor

Focuses on strategies designed to address sustainable alleviation of poverty and provide short-term poverty relief including support for the small farming and non-farming sector, as well as health and welfare support.

Programme five: the development and utilization of human resources

Addresses the development of a human resources strategy for KZN and support for labour market reform.

Programme six: the formulation of an appropriate spatial framework,

Identifies particular development corridors including those of the north south coastal corridor, and secondary metropoles, particularly along the N3 and smaller nodes.

Programme seven: the development of institutional and implementation capacity

Addresses the development of institutional capacity within all spheres of government and the building of partnerships with stakeholders to give effect to the PGDS.

During 2001 to 2002, the provincial government undertook a process of review of the PGDS. The outcome of the review process is detailed in the *KZN PGDS Research, Analysis and Concept Document* produced by Price Waterhouse in 2002. The document details shifts in economic and intergovernmental relations post the 1996 PGDS, and develops a concept, institutional framework and implementation process for giving effect to a revised PGDS. Critical issues flagged for attention in the formulation of a revised PGDS include that of increased co-ordination and improvement of Intergovernmental Relations at national, provincial, district and local council level in order to transform budgets and priorities to focus on the historically marginalised sectors of society.

The impact of changes in the global economy on KZN includes a continued tendency towards capital intensification, shedding of jobs, decline of key economic sectors, an increased role for Information and Communication Technology and the growth of a "New Economy". The revised PGDS should be utilized as a guiding framework for packaging of key projects and marketing KZN as a leading social, industrial, human and economic development hub in Sub Saharan Africa by balancing investment in urban and rural areas.

Finally, the report suggests that a key flaw of the 1996 PGDS is the weak institutional framework for managing and monitoring implementation. It suggests a holistic implementation strategy around Cabinet Clusters in Governance And Administration, Economics, and Social and State Enterprises.

4.4.1.1 The role of the DEDT

The role of the DEDT with respect to economic policy and interaction with public institutions has undergone a transition. The work programme of the DEDT during the period 1994 – 1999 was not primarily concerned with economic policy and strategy formulation or analysis of developments in key economic sectors. In this period, the central thrust of activities of the DEDT related to:

- The SMME Directorate and support for the SMME sector in KZN;
- The dispersal of RDP funds; and
- The provision of unconditional grant funding to public entities.

The organisational and human resources capacity of the DEDT was geared to fulfilling the above functions. Limited material and human resources were deployed to developing an economic strategy capacity within the department. The Ministry was responsible for making economic policy statements and for linking economic development with government delivery programmes. A period of consolidation and restructuring of the DEDT has since been undertaken.

The focus of the restructured DEDT is encapsulated in the department's vision:

> *To ensure that by the year 2020 KZN will be a thriving, globally competitive economy that will house dynamic industrial and service sectors, with a world class tourist destination characterised by excellent services standards. There will be a high level of employment, raising the quality of life, and an economic environment supporting empowerment and creating prosperity for all.*

The primary objectives of the DEDT are to promote industrial development and stimulate the international competitiveness of the KZN economy. The core business of the DEDT relates to its desire to:

- Be a one-stop economic information shop;
- Contribute to the formulation of economic policy development and articulate the economic development strategy for KZN;
- Facilitate local economic development and the regeneration of small towns;
- Promoting rural economic development;
- Develop tourism as a key sector of the economy;
- Facilitate the increase in trade between the province and other economic regions;
- Promote fixed investment into the province;
- Promote economic development through the championing of public-private partnerships;
- Promote and facilitate economic empowerment programmes;

- Promote SMME development;
- Promote technological innovation and increasing competitiveness in key sectors of the economy;
- Champion initiatives, which improve the province's logistics capabilities and enhance key supply chains;
- Provide integrated economic project support for key identified anchor investment projects;
- Developing and supporting an investment framework for KZN;
- Undertaking development planning;
- Effectively manage parastatals as instruments of delivery and economic co-ordination;
- Provide an effective and efficient consumer protection service; and
- Ensure effective and prudent business regulation in the province.

The DEDT has identified focus areas to stimulate international competitiveness which include:

- Encouraging development in identified economic sectors including clothing & textiles, agro-processing, metal & aluminium, automotive components, ICT embedded systems, chemicals and biotechnology and minerals.
- SMME development programmes that include Business Development Services and targeted sectoral initiatives.
- Supporting the development of agribusiness in identified niche commodities including honey, organic products, cut flowers, essential oils, medicinal plants and aquaculture.
- Supporting rural community-based projects.
- Supporting Local Economic Development and the regeneration of small-town economies through an operational Local Economic Development Initiative
- Implementing an integrated Black Economic Empowerment (BEE) programme which addresses government procurement and internal trade policy, identifies investment opportunities, develops sectoral strategies for BEE, provides support for emerging contractors, facilitates community equity participation, provides finance and community banking through the establishment of a Provincial BEE Fund.
- Support for the provision of Trade & Investment Services.
- Unlocking strategic investment projects including the implementation of the Dube Trade Port including logistics gateway, cyber zone, IDZ, airport, and related residential and commercial value added activities.
- Support for Tourism Development and Promotion.

- Effective consumer protection and prudent business regulation.
- Supporting business financing.

It furthermore is responsible for setting parameters for the operation and allocation of funding to public entities. Public entities with a direct reporting relationship to the DEDT include Ithala, TIK and TKZN.

4.4.1.2 Organisational capability

The DEDT's budget of R190-million for the 2003/4 financial year is allocated as follows:

- R96-million to public entities;
- R29-million administration;
- R16-million Local Economic Development and rural projects;
- R31-million to SMMEs;
- R3.7-million to economic policy; and
- R13.7-million to special projects, of which R10-million is allocated to the Dube TradePort SPV. (In addition, the Treasury is holding R50-million for the Dube airport).

4.4.1.3 Challenges facing the DEDT

The restructuring process initiated by the DEDT has resulted in the development of a more effective institution, with a clearly defined focus and improved capacity. However, areas that remain unresolved relate to the absence of a well-defined economic policy for KZN and the relationship between the DEDT and the parastatals.

The need to develop a comprehensive and articulate economic development strategy for the province is becoming more urgent. Such a document would build on the PGDS by identifying specific levers for growth, investment targets, developing sectoral strategies for encouraging exports, implementation parameters, lead agencies, performance measures, targets and time frames.

The KZN Cabinet operates an economic cluster, incorporating ministries impacting on economic development including the Premier, EDT, Agriculture and environment, Transport, Finance, Public Works and Housing. The DEDT could play a lead support role to this cluster through the necessary technical and policy support to the Cabinet Economic Cluster. This would include interaction with the agencies required to give effect to particular project requirements, for example, to facilitate interaction with the Department of Transport in regard to the road infrastructure requirements of the Dube TradePort.

The Department of Finance is building an information base and undertaking an audit of planned infrastructure spending in order to develop management competence to prioritize strategic infrastructure spending in line with the economic and development imperatives of KZN. The Department is, however, constrained by the fact that there is no economic strategy in place to utilize as a yardstick to guide decision-making.

In the post 1994 period it was assumed that it was the responsibility of national government, most particularly the Department of Trade and Industry, to develop economic and industrial strategy. As the functions and powers of different spheres of government have developed, it is becoming increasingly evident that concurrent powers exist between national and provincial government in regard to economic policy formulation.

Thus the priority for the DEDT – in collaboration with the DTI - is to undertake an audit of economic development and co-operatively define national and provincial competencies and roles and the respective powers of various agencies and bodies. This role definition will need to be translated into a delineation of responsibilities in concrete programmes and activities such as those of the implementation of the IDZs. For example, the DEDT could play a particular role in respect of addressing policy to alleviate the developmental blockages and location specific problems facing the southern industrial basin of Durban.

The DEDT has increasingly engaged in a process of refining and detailing its responsibilities in respect of economic policy development and the facilitation of economic strategies for KZN. The current strategic plan of the DEDT notes that the Department needs to strengthen its policy mandate, partnership building and leadership role in regard to economic strategy development for KZN. The DEDT does not intend to play an on-the-ground project implementation role, but will rather focus its resources on defining project feasibilities/ businesses cases of projects, building partnerships with stakeholders in order to develop project implementation and strategies and increasing its ability to gather and disseminate economic information. Thus the DEDT intends to shift its role from that of a disperser of funds to play a greater role in economic strategy development and economic information management.

A proposed role for the DEDT would thus relate to:

- Economic policy formulation and interaction with public entities in terms of implementation.
- Acting as the first stop for economic information management resources in KZN with the necessary research and economic information management capacity.
- Developing a broad set of parameters to encourage investment into identified strategic priority projects critical to giving effect to the Economic Strategy of KZN. The role of the DEDT in this regard would be to consider project feasibility, and play a facilitation role in regard to strengthening logistics

competencies and the ability of public entities and stakeholders to implement projects.

4.4.1.4 The role of public entities

The DEDT's relationship with public entities has improved as a result of a process initiated by the former to clarify the roles of provincial institutions vis-à-vis the department. Monthly meetings are held between the CEOs of the DEDT mandated parastatals and the Head of Department. However, duplication between institutions persists and they are sometimes unaware of their core competencies and the specific role they should bring to particular programmes. To overcome this the DEDT will be encouraging closer relationships between TIK, TKZN and Ithala.

Clear lines of authority between the DEDT and the public entities need to be developed to ensure that policy parameters emanating from national and provincial government can be communicated and implemented. In this regard the DEDT must be acknowledged as the primary economic policy generator for KZN, with public entities responsible for implementation of programmes and strategic initiatives that give effect to policy imperatives. At the same time, open avenues of communication must be secured between the public entities and the DEDT to ensure that economic trends and issues arising from the research and programme operations of the public entities are able to impact on the policy priorities of the DEDT. A proactive relationship with public entities must thus be pursued. Interaction must take place in a formal institutional manner with clearly defined line function authority, regular meetings and full reporting.

The DEDT needs to strengthen its ability to monitor and evaluate the impact of the performance of public entities. To that end, the DEDT must develop the necessary capacity to assess the proposals and business plans of public entities against its economic policy imperatives, in order to develop proactive monitoring and evaluation procedures in partnership with the public entities. Public entities must, in turn, be fully accountable to the DEDT for any monies disbursed to them in terms of detailed performance targets, which should be open to public scrutiny through the publication of annual reports that include audited financial statements.

In regard to attracting investment into KZN, the DEDT has requested that the TIK develop an investment protocol, which would provide guidelines for investment promotion in KZN. In particular, it should develop guidelines as to institutional co-operation and partnerships and define the responsibilities of the respective spheres of government, address the necessary leverage required and chains of support available to give effect to potential investments.

Ithala has potentially a very valuable role to play in support of the implementation of key projects, particularly in so far as technical support and financing is concerned. The potential role of Ithala as a strategic investor needs to be explored further where Ithala has the capacity to provide leverage and equity in particular priority projects, programmes and strategic investments.

By adopting an approach which identifies and delineates the particular competencies of public entities and the DEDT, yet at the same time encourages co-operative interaction between the respective bodies, there is an opportunity to institutionally strengthen linkages between economic strategy and resources by utilizing the financial and property management acumen of Ithala, the technical capacity of TIK, and government leverage.

In order to play these roles both the DEDT and the public entities need to be equipped with the necessary human resources and financial capacity to perform their respective mandates. The DEDT, in particular, needs to strengthen its capacity to develop policy and economic strategy for KZN, communicate with public entities regarding the implementation of policy and monitor and evaluate the outcome of programme delivery. In this respect consideration should be given to strengthening the DEDT's Business Plan to incorporate the need for more highly skilled staff, greater economic management skills, focused policy and monitoring role and a larger budget.

4.4.2 Ithala Development Finance Corporation

The powers and responsibilities of the Ithala Development Finance Corporation (commonly known as "Ithala") are determined by Section 3 of the KZN Ithala Development Finance Corporation Act, No. 2 of 1999. Ithala's objectives are:

- To mobilise financial resources and to provide financial and supportive services to the people of KZN;
- To plan, execute, finance and monitor the implementation of development projects and programmes in the Province;
- To promote, assist and encourage the development of the Province's human resources and its social, economic, financial and physical infrastructure;
- To promote, encourage and facilitate private sector investment in the Province and the participation of private sector and community organisations in development projects and programmes, and in contributing to economic growth and development; and
- To act as the Government's agent for performing any development-related tasks and responsibilities that the Government considers may be more efficiently or effectively performed by a corporate entity.

In line with the mandate defined by the KZN Cabinet, the core business of Ithala relates to:

- Promoting and encouraging private sector participation in economic growth and employment creation;
- Promoting entrepreneurship by acting as a Development Finance Institution operating within the context of the Banking Council Code and providing a range of business and personal financial products. Sectors targeted for business products include Agriculture, Industry, Commerce and Tourism; and

- Acting as a property portfolio holder and developer, providing industrial, service and SMME sectors with rental premises such as factories, shopping centres and office complexes

The strategic direction of the organisation is incorporated in its Vision, which emphasises three areas: socio–economic development (particularly with respect to fulfilling its mandate in regard to the development dividend), financial sustainability of the organisation and the building of partnerships.

The mission of Ithala is to be:

> *"a financially sustainable organisation, representative of and identifying with the community we serve, promoting economic growth and socio-economic development by:*

- *Identifying and implementing development opportunities;*
- *Providing a range of products and services that meet the needs of our clients; and*
- *Complementing Government and private sector initiatives.*

> *We will achieve this by growing our organisation and actively seeking out partnerships in socio-economic development".*

The legal and regulatory framework governing Ithala includes the Corporations Act No 2 of 1999, and the Public Finance Management Act SA Banks Act (Ithala Ltd). The institution attempts to abide by the King Code of Corporate Governance SA and the Banking Code of Conduct. Despite the fact that Ithala does not have a banking licence, it nevertheless complies with the provisions of the act. The Technical Service Department is ISO 9001 compliant. A fully-fledged Internal Audit Unit is in operation and external audits are conducted annually. The institution has furthermore established a Fraud Tip-Off Service

4.4.2.1 Institutional framework

Ithala's Board of Directors, comprising one Executive Director and 10 Non-Executive Directors, are appointed to hold office for a maximum of three years by the MEC for Economic Development and Tourism in consultation with the Premier in Cabinet. Board Committees include the Credit Committee, Assets and Liability, Audit, and Human Resources.

Ithala comprises a number of corporate entities including:

- Ithala Development Finance Corporation Ltd (Group);
- Ithala Ltd (Full Subsidiary);
- Other subsidiaries (SPVs and JVs) such as:
    - Dube Trade Port Ltd
    - Albert Luthuli Hospital (Cowslip); and
- Other property joint venture companies.

4.4.2.2 Programmes

Strategic focus areas for the new financial year include the following:

- Improving the efficiency of IT Systems;
- Addressing non-performing & non-productive assets (PIPs);
- Accessing donor funds in order to give effect to the Black Economic Empowerment Fund;
- Proactive involvement in Strategic Projects such as the Dube Trade Port and Albert Luthuli Hospital;
- Effective arrears management, client service excellence, regularisation of deposit-taking;
- Developing the capacity of staff;
- Maximise non-interest income – new products (bank assurance);
- Addressing Black Economic Empowerment; and
- Review lending and pricing policies.

The organisation's activities are undertaken by a number of strategic business units:

The Business Loans department is responsible for Ithala's small, medium, and micro enterprise (SMME) development programme and its agri-business development programme, providing loan packages to cover building finance, plant and equipment finance, working capital, land and fixed improvements finance, and empowerment equity capital. Ithala further actively seeks business partnerships, which will benefit clients. Ithala business partnership with the World Bank, through its wholly owned subsidiary, African Project Development Facility (APDF), is designed to bring direct benefits to small and medium enterprises active in KZN. APDF specialises in the provision of business advice, management technique interventions and skills development. APDF will contribute 50% of the cost of its business support.

The Properties department promotes private sector investment in industrial, commercial and tourism development. Ithala acts as a property portfolio holder and this division is responsible for the management of various Ithala owned industrial estates and parks in KZN. It promotes inward investment to these nodes through a range of financial packages including building finance, working capital, equipment, furniture and vehicle finance, plant and equipment finance and empowerment equity capital, offered via the Business Loans Department. Ithala also develops one-stop shopping centres in primarily rural areas. Ithala provides tourism investment support and tourism development services, specifically in the field of tourism development funding, focussing on eco-tourism facilities, game lodges, back-packer operations and guesthouse ventures. Ithala supports joint ventures in commercially oriented tourism development and facilitates community-based tourism projects.

Ithala Limited, is a ring-fenced wholly owned subsidiary of Ithala, and provides home loan and home improvement loan financial packages and related information services primarily aimed at the low-income end of the housing market.

In addition, Ithala provides a savings service including savings accounts, fixed deposits, target and club save products provided through a branch network to particularly rural communities and first-time savers not generally catered for by commercial financial institutions.

The five main categories of operation include savings products and services, homeowner financial packages, business loans, property portfolio, strategic projects (DTP, IDZs) and bank assurance.

The Black Economic Empowerment Fund (BEEF) was established as a partnership between Ithala and DEDT. The purpose of the Black Economic Empowerment Fund (BEEF) is to:

- Accelerate authentic BEE;
- Promote entrepreneurship;
- Improve access to capital by, inter alia, relaxing security requirements for qualifying loan applications;
- Improve business management skills by providing technical assistance to successful applicants; and
- Reduce and manage high-risk levels.

Ithala is responsible for the operational management within an agreed set of guidelines, with quarterly reports provided to the DEDT. The DEDT is responsible for policy frameworks and funding. Economic sectors targeted include those that will maximise benefits for BEE. Currently the focus of the fund is on tourism projects. It is intended to further extend institutional arrangements for the fund to involve partnerships between multiple partners. This may take the form of a Section 21 not-for-gain company.

The fund provides assistance in the form of loan finance, technical assistance and guarantees. Qualifying criteria for accessing the fund include:

- Basic: Persons from previously disadvantaged communities with specific emphasis on PPGs in which the enterprise should be owned/managed or sufficiently influenced by individuals from previously disadvantaged communities, especially PPGs; and
- Business: Financially viable, with security requirements constraints, and requiring technical assistance. Applications between R250,000 and R2.5-million are considered.

The fund is at present sourced from the DEDT, with R10-million received to date. Further funding is being sought from donor agencies and relevant institutions. The target for funding drives is set at R25-million to R50-million.

4.4.2.3 Organisational capability

Ithala employs approximately 1000 employees and has in place effective mechanisms for staff development and performance management of all activities. The impact of Ithala programmes is evidenced by the following results:

Table 4.1 – Ithala savings

Amount	Number	HDI %
R852-million	471,650	95

[Source: Ithala]

Table 4.2 – Business loans

Sector	Amount (Rm)	Number	Arrears %	HDI %
Agriculture	216	1,450	13	88
Commerce	357	1,653	14.5	69
M & L	237	403	7	29
M & S	120	1,250	30	82
Total	573	3,103		

[Source: Ithala]

Table 4.3 – Home loans

	Amount (Rm)	Number	Arrears %	HDI %
Bonds	801	14,669	11	65
Progress	2	221	4	95
Home improvements	61	5,192	1	98
Total	864	20,082		

[Source: Ithala]

Ithala plays a fundamentally important economic developmental role in KZN. The financial and property services offered to investors targeting emerging markets have supported the development of numerous initiatives throughout KZN. The provision of an extensive range of services to clients within a market historically ignored by the banking sector has assisted the development of a culture of savings in marginalised and poor communities.

Their remains, however, potential for further maximizing the financial, technical and developmental role of Ithala in KZN. The DEDT should engage with Ithala around extending its developmental role to further support the economic policy imperatives of KZN. The potential role of Ithala as a strategic project implementer and investor needs to be explored further. Ithala has the capacity to provide leverage and equity in particular priority projects, programmes and strategic investments thereby acting as a catalyst to support an economic strategy of KZN. Such a role is beginning to emerge with the role being played in respect of the Dube TradePort and could be extended to other areas of attention. This may require that the DEDT provide the necessary finances and resources to capacitate Ithala to fulfil this additional responsibility.

4.4.3 Trade and Investment KwaZulu-Natal

Trade and Investment KZN (TIK) is the provincial trade and investment promotion agency, established and funded by the DEDT, following the merger of the KZN Economic Council and the KZN Marketing Initiative, and the subsequent amendment of the articles of association of the Economic Council, in 2001.

The mandate of the organization is to promote, support and facilitate trade, investment and economic development in KZN. Its vision is to:

> *"make the province of KZN the premier investment destination and a leader in export trade. Within an agreed policy framework for trade and investment identify and package investment and export trade opportunities in KwaZulu-Natal; provide a professional and comprehensive service to potential and current exporters; ensure success to investment and export trade opportunities and sustained after care; brand and market provincial investment opportunities and link opportunities to the development needs through the facilitation of strategic partnerships".*

TIK operates within the policy parameters set by the DEDT. Its primary responsibility is to act as an implementing agent responsible for encouraging trade and investment into KZN. The primary target is Foreign Direct Investment, followed by domestic investment. The TIK is required to provide the DEDT with performance measures against which the organization's progress - in terms of encouraging investment, creating jobs and facilitating trade - may be measured.

The TIK further aims to support the development of a broad economic strategy for KZN, particularly by giving consideration to government procurement policies and encouraging procurement and service delivery to be sourced from companies located in KZN.

4.4.3.1 Institutional framework

TIK is an association incorporated under section 21 of the Companies Act of 1973. It is accountable to the MEC for EDT and the DEDT. The Accounting Authority is the Board comprising non-executive directors, which meets on a quarterly basis. Board members include representatives from the private sector, parastatals, provincial and local government and trade unions. Board Committees include an Executive Committee, Human Resources and Audit Committees.

4.4.3.2 Programmes

The six main programmes of the TIK are outlined in the strategic plan, which is currently under review. The programmes include:

- Expansion of local fixed investment and export trade. Programme activities include interaction with local business, assisting exporters with export marketing incentives, lobbying for local incentives, promoting skills development, the establishment of beneficiation projects, and the hosting of an exporters database. Sectors identified for priority attention include the textile industry, agriculture, tourism, automotive industry and components, arts and crafts, aluminium, and ICT.
- Increase foreign direct investment and international trade. Programme activities are directed at undertaking trade and investment promotion missions, hosting business delegations, participation in trade and investment delegations, monitoring investment trends, gathering and disseminating information pertaining to trade and investment opportunities in KZN, providing project support and aftercare services to investors, assisting existing and new investors with applications for investment incentives, linking investors with appropriate service providers including the securing of project and operational financing and assisting foreign investors with applications for work permits.
- Integration of public / private sector input. Programme activities include encouraging public private partnerships, developing and strengthening relationships with local companies and strengthening the provinces international economic linkages.
- Promotion of Black Economic Empowerment (BEE) and the establishment of appropriate institutional arrangements. Programme activities relate to the facilitation of joint ventures, facilitating business linkages between small and big business, the development of appropriate equity arrangements, encouraging beneficiation, the identification and packaging of investment opportunities and monitoring progress achieved by black owned businesses through the BEE database. BEE is a dominant theme in all the sectoral activities undertaken by the TIK.
- The creation of an investor friendly climate. Programme activities are concentrated on developing effective relations with strategic partners, influencing empowerment and investment policy. A memorandum of understanding has been secured with TISA, which addresses areas of co-operation including those of staff development, project management systems with respect to the EMIA scheme, and co-operation around investment promotion activities. Interaction with the Durban and Pietermaritzburg Chambers of Commerce is undertaken as is with the Durban Investment Promotion Agency (DIPA), Richards Bay and Midlands investment Initiatives.

Specific services offered within the various programmes of the TIK include:

- Provide assistance to emerging international traders;
- Assist with international trade enquiries; and
- Assist investors.

4.4.3.3 Organisational capability

The TIK has undertaken a phased appointment of staff, with an initial appointment of 18 members (14 operational and 4 support staff). It is intends to build its staff complement to include a full staff capacity of 29. The organisation has an annual budget of R16-million, with phased increases over a three-year period.

Customer orientation, and performance measurement systems are currently under review. A Staff skill audit is being undertaken to address skill gaps in terms of fulfilling the operational activities of the organization.

The TIK has the capacity to play a fundamentally important role in promoting investment and exports in KZN. As a fledgling institution, its organizational, programme implementation and human resources capacity are in the process of development. The role of the TIK would be further strengthened by the development of an economic policy for KZN in order to provide the framework within which a focused trade and investment framework and implementation policy for KZN could be developed.

4.4.4 Tourism KZN

Tourism KZN is the official agency through which tourism in KZN is promoted, developed and marketed. The institution receives its mandate from the KZN Tourism Act passed in 1996 by the KZN legislature.

The primary purpose of the act is to:

> *"Provide for the establishment of bodies to develop, promote and market tourism in KwaZulu-Natal within the framework of national and provincial tourism policy and Legislation, and to provide for matters incidental thereto"*.

The KwaZulu-Natal Tourism Third Amendment Bill of 2002 governs the relationship between different spheres of government and provincial institutions responsible for tourism promotion, marketing and development. The recently revised KZN Tourism Act governs the TKZN, sets out legislative parameters, determines powers and details the form that the representative structures (including the reconstituted board) are to take.

With the appointment of the first Board of Tourism KZN in mid-1999, a three- year strategic plan of action, *Tourism Strategy 2000*, was launched. In order to realize the vision of the organization – which is for KZN to be recognized nationally and internationally as Africa's premier tourism destination - *Tourism Strategy 2000* identified five core strategic elements – a strategic marketing framework; an international marketing strategy; a domestic tourism strategy; the implementation of a tourism product development strategy and a corporate governance strategy. Consistent throughout the implementation of these programmes is the branding of KZN as "*The Kingdom of the Zulu.*"

4.4.4.1 Institutional framework

The TKZN has a direct accounting role to the MEC for Economic Development and Tourism (EDT) and the provincial DEDT. The board appointed in terms of the KZN Third Amendment Bill in 2002 by the MEC Economic Development and Tourism, governs the TKZN. Board Committees include a Development, Marketing, Audit and Corporate Services Committees.

Additional stakeholder liaison committees include:

- Research and Information Advisory Services Committee;
- Investment Advisory Forum;
- CEO and Municipal Managers Forum; and
- Charters and Aviation Steering Committee.

Co-operation with SA Tourism, South Africa's national marketing organisation has improved since 2001. Regular meetings and workshops are held with the DEDT KZN and co-operative structures have been established with other provincial and national departments and public entities including district councils and the Durban unicity.

In addition TKZN co-operates actively in the following national co-ordinating structures:

- Ministers and MECs Tourism Meeting (Tourism MINMEC);
- MINMEC Interprovincial Steering Committee (MIPTECH);
- Development Working Group of MIPTECH;
- Research Working Group of MIPTECH;
- SA Tourism and Provincial CEOs Meeting; and
- Tourism Transformation Forum.

TKZN launched a voluntary registration system for the KZN tourism industry in July 2001, with over 1800 establishments having registered. Registered establishments benefit from recognition as a registered KZN tourism establishment and access services such as the TKZN database and partnership programme. Regulations to make registration mandatory have been drafted and are currently with the MEC for Economic Development and Tourism and the Parliamentary Portfolio Committee.

4.4.4.2 Programmes

Domestic tourism marketing strategy

The TKZN domestic tourism marketing strategy is designed to provide a generic marketing platform to market KZN as a domestic tourist destination under the "Kingdom of the Zulu" brand. Activities include the undertaking of year-round promotional campaigns, advertising in various print and electronic media, and participation in domestic trade shows and exhibitions. This includes a cooperative drive with local travel and tourism operators to sell KZN destined holiday packages to boost occupancy during low seasons. Key cultural, sporting events and news events are given exposure, in order to attract tourists and include previously excluded areas into the tourism mainstream.

International tourism marketing strategy

The major focus of TKZN's international marketing efforts is in co-operative marketing ventures with major outbound tour operators in key source markets including Germany and the United Kingdom. This includes the hosting of trade workshops and trips for media and South African inbound operators to expose them to KZN-based product owners and operators, and participation in numerous international shows and exhibitions.

TKZN has adopted a charter flight policy for tourism in the province. The need to secure charters to Durban arose partially out of aviation policies that favour the hub and spoke practices of South African Airways, which encourages international airlines to fly to Johannesburg and have their passengers transported domestically by SAA. Research indicates that this policy has impacted negatively on arrivals to the region.

Strategic product development

In order to ensure the effective transformation of the tourism industry within KZN, the Department of Economic Development and Tourism identified areas for specific attention by all provincial departments including community based tourism development and Black empowerment in the tourism industry.

TKZN provides assistance to small business in the following areas:

- Training and accreditation of small and emerging businesses, such as tour guides;
- Marketing Assistance programme for marketing materials to promote their businesses;
- Assistance with participation at domestic and international trade and consumer shows; and
- The procurement policies of TKZN.

TKZN has managed Poverty Relief Projects with more than R30-million accessed from the National Department of Environmental Affairs and Tourism for projects that benefit historically disadvantaged communities during 2002. A dedicated Community based tourism unit is responsible for the promotion of community based tourism product.

The product development strategy aims to:

- Broaden ownership in the industry, particularly amongst the previously disenfranchised sectors;
- Compliment and improve the existing tourism product mix by identifying key tourism development projects and sites for private sector investment;
- Give support to the strategic marketing framework and brands;
- Facilitate new investment/funding in areas of low economic activity and provide a strategy for tourism in rural areas; and
- Establishes a spatial framework for future product development;
- Identifies key nodes and sites for public sector funding including that of infrastructure requirements;
- Provides a funding and investment strategy; and
- Identifies core institutional, functional, and legal and policy issues.

The strategy highlights 12 projects as areas for priority attention:

- Zulu Heritage & cultural trail;
- King Shaka Tourism Route within the Limber District Council area;
- Emakhosini Heritage Park: Valley of the Kings;
- Isibaya: Royal Zulu House at Nongoma;
- Richards Bay Cruise Ship Passenger Terminal;
- Coastal Resort Development: Tongati River Mouth;
- Durban beachfront: strategic tourism development plan;
- Repositioning of the Valley of the 1000 Hills;
- Development of the Mnweni Valley Development within the Ukhahlamba Drakensberg Park;
- uKhahlamba-Drakensberg Park: access roads and signage;
- Development of Oribi Gorge and Mzimkulu Nature Reserve on the South Coast; and
- Marina Resorts Development on the KZN coast.

4.4.4.3 Information services

TKZN maintains a tourism information management system and research programme. This includes a website, Fax on Demand service, Tourism Asset Database, undertaking of market research and monthly survey, the dissemination of research brochures an information resource centre, and various tourism information offices established at locations such Durban international airport and V & A Waterfront.

The image-marketing component of the TKZN strategy comprises Corporate Communications (strategies undertaken to promote Tourism Strategy 2000 and TKZN), and Image Positioning strategy to reverse negative perceptions in relation to crime, disease and grime in KZN.

Service levels and performance measurement systems:

TKZN sets macro goals that relate to improving the performance of the tourism industry in KZN and micro goals for measuring the performance of TKZN. Quarterly reports are provided to the DEDT in respect of monitoring performance in reaching the macro and micro goals set.

Micro goals monitor:

- Consumer response to services offered, including brand recognition;
- Use of web site, e-mail, telephonic, mail enquiries and walk-in enquiries;
- Brochure distribution; and
- Trade response to services offered including recognition of slogan, awareness of campaigns, perceptions of performance, role recognition and registration rate.

It is estimated that Tourism KZN will reach the following economic targets with the following budgets*:

Table 4.4 – TKZN economic targets

	2001/2002 (Rm)	2002/2003 (Rm)
Budget	27	35
Direct expenditure	168	182
Impact on GGP	239	258
Total impact on employment: sustained jobs	2,623	2,758

The Tourism KZN budget influences 25% of KZN's domestic and 7% of its foreign tourists whose decision to visit was influenced by marketing media. These tourists are expected to spend at least R168-million in the province in 2002 and R182-million in 2003. Research has revealed that the economic multiplier for tourism in KZN is in the order of 1.42, which implies that the total impact of this spend will be in the order of R239mn in 2001 and R258mn in 2002. The employment multiplier for tourism is estimated to be 15.6 jobs for every R1mn of direct tourism expenditure in 2001 and 14.6 jobs in 2002.

4.4.4.4 Organisational capability

TKZN's human resource development programme has four core areas:

- Education, training and capacity building on community based tourism projects;
- Bursary scheme for students studying travel and tourism;
- Teacher training support programme in partnership with the University of Zululand;
- Student internship programmes; and
- Tour guiding assistance programmes.

TKZN has undergone some limited internal restructuring during the course of 2002. It has streamlined various divisions to ensure that they remain focused around their core areas of competence and restructured the management team. It employs approximately 45 staff members. Currently staff and operational costs constitute less that 25% of the provincial grant and around only 10% to 14% of annual turnover.

TKZN has developed into an efficient organization. However, it appears that the organization needs to give greater attention to marketing the diversity of its tourism product and increasing advertising both nationally and internationally.

4.4.5 Dube TradePort Special Purpose Vehicle

Initiatives to establish the Dube TradePort were outlined in section 2. A special purpose vehicle (SPV), which falls under Ithala, has been established to manage its implementation. The project was initially driven by the provincial Ministry of Economic Development and Tourism, and is currently managed by an interim Board comprising the DEDT and Ithala. It is intended to expand this to include the unicity and the provincial Department of Transport staffed through secondments.

4.4.5.1 Development and implementation milestones

A Passenger Airport Feasibility Analysis for the project was completed in January 2001, together with a logistics concept and master plan. The national cabinet has granted in principle government approval of the project concept. Current initiatives are focused on the finalisation of the detailed business plan / structured finance packages and project commercialization.

The implementation phase of the project, including detailed design and construction, is set for 2003 to 2005. The IDZ / Cyberport operations are mooted for 2004 to

2005. It is intended to commence commercialisation of land on the Southern Industrial Basin in December 2005, with the passenger terminal operations of the Trade port operational by 2006.

4.4.5.2 Cost

The proposed deadline for completion of the initiative is 2006. The total start up phase budget for the initiative amounted to R1.250-million at September 2001 prices excluding escalation (this includes R980-million for the airport and runway facility and R270-million for the IDZ and cyberport).

The successful implementation of the project requires further attention to securing stakeholder acceptance of the project including that of ACSA, and ensuring that attention is paid to developing the economic imperatives to give effect to increased logistics requirements in KZN.

4.5 Conclusion

The successful implementation of a provincial industrial strategy that prioritises employment creation and skill formation, while being cognisant of the deleterious economic impact of HIV/Aids, is dependent on the efficacy of the instruments utilised in its implementation. The range of instruments at the disposal of provincial government is spread over many institutions, including national and local government.

In addition to the provincial-level institutions identified above, the resources and programmes of the DTI, IDC, DBSA and National Treasury will play an important role in promoting industrial expansion in KZN. Hence a key challenge is to mobilise the resources of these institutions in support of KZN's industrial strategy.

The overarching priority for DEDT is to develop a detailed policy framework for the province's economic development that prioritises particular sectors and geographic areas. This will focus the resources and programmes of the public entities that are mandated by DEDT on defined outcomes. The absence of an overarching policy framework is clearly inimical to sustainable economic development.

5 Future economic prospects for KZN: challenges and opportunities

5.1 Introduction

KZN is the most populous province in South Africa, with the highest level of unemployment and a severe incidence of HIV/Aids. Moreover, it has a disproportionately high share of South Africa's manufacturing sector and is home to the most important logistics platform for South Africa's trade. The province's economic fortunes will therefore clearly have a significant impact on the broader South African economy.

While KZN has a number of weaknesses, it also has many strengths. The province's strengths are related to its geographic position, resource endowments and logistics infrastructure. The structure of the economy, which differs from the broader South African economy in that the mining sector is much less dominant, may be interpreted as a source of strength in the context of the decline of the mining sector and its uncertain future within the global economy.

Key weaknesses of the KZN economy are related to its high levels of unemployment and high incidence of HIV/Aids. The evidence also suggests that skill formation is not taking place at the desired pace and that KZN's education institutions are not responsive to the skill demands emanating from industry. In terms of the structure of the KZN economy, the higher share of manufacturing enterprises has meant that the province has been more vulnerable to the negative impact of trade liberalisation as South Africa becomes integrated with the global economy. For this reason, the clothing, textile and industrial chemical industries have been experiencing decline and face an uncertain future.

5.2 Opportunities

Opportunities for economic growth and development abound within the KZN economy. The structural shifts within the economy that have emerged over the 1995 to 2001 period suggest that the provincial economy is undergoing the structural adjustments necessary to specialise in its areas of strength (for example, aluminium, paper and pulp, transport and communication) in order to become a global player. While the decline of certain industries (for example, textile) will have a negative impact on KZN's growth prospects, it is a necessary adjustment to global competition.

The buoyant growth of a number of industries in the secondary and tertiary sectors in a context of trade liberalisation, suggests that they have made the necessary adjustments to their cost structures to become players in the global arena. Opportunities for expansion and the development of backward and forward linkages in the business and financial services, transport and communication, paper and paper products, non-ferrous metals and petroleum sectors should therefore be actively sought. In this regard, the potential to develop clusters should be more actively pursued.

As regards smaller industries that have demonstrated expansion, their potential for further expansion and potential for cluster development as well as their current position within global supply chains should be investigated. Within this grouping, the motor vehicle and parts and wood furniture industries have been the preoccupation of policy-makers and researchers in KZN. Recent developments with respect to Toyota (including ownership changes and plant-level restructuring to gear up for production for the global market) bode well for the future expansion of this industry. It also has potential for cluster development, particularly in the supply of components which are currently being imported from Japan.

Other industries that show signs of occupying a more dominant position within the KZN economy include printing & publishing, beverages, non-electrical machinery and iron & steel. The printing and publishing industry, for example, enjoys backward linkages with the dominant paper and paper products industry which is currently experiencing buoyant growth. This suggests that there may be opportunities for enhancing the competitiveness of both industries through clustering.

Initiatives currently underway to restructure South Africa's port system, and the decision to fast-track the process of concessioning the Durban Container Terminal presents an important opportunity for the KZN economy. The removal of the obstacles presented by a poorly-managed and inefficient container terminal will not only reinforce Durban's position as Southern Africa's largest container terminal (hence removing the threat of competition from Maputo and Ngqura), it will also provide a catalyst for the development of 'back-of-port' operations, which will provide a substantial boost to KZN's manufacturing capability.

The expansion of the Durban Port through the enhancement of its container handling capacity and the creation of an additional multi-purpose terminal will also have positive spin-offs for the KZN economy as higher volumes of cargo moves through the port. While these two restructuring initiatives will be driven by the Department of Public Enterprises and the National Port Authority, once they are in place the extent to which their benefits are fully exploited is dependent on the KZN government and the Ethekwini Metropolitan Council. In this regard, the identification of industries that could develop or expand existing operations and the facilitation of such endeavours will be key to unlocking these opportunities.

In terms of initiatives that are under the direct control of provincial government, the three spatial development initiatives (Lubombo, Richards Bay and Pietermaritzburg-Msunduzi) and two industrial development zones (Richards Bay and Dube Trade Port) present an opportunity to greatly enhance the growth rate of the provincial economy, while at the same time enhancing its ability to integrate within the global economy. There is, however, a range of challenges associated with the successful implementation of these initiatives.

In a context where the skill of the labour force is becoming a more important determinant of competitiveness than resource endowments, KZN has significant institutional capacity to develop a skilled labour force. Indeed, KZN has the highest proportion of further and higher education and training institutions in the country. If they are able to be responsive to the demand for skills from industry, rapid skill formation is attainable.

5.3 Challenges

The challenges confronting the KZN government in its efforts to promote economic development emanate from both structural weaknesses within the economy, and the national institutional framework within which instruments of industrial policy can be accessed and implemented.

As regards structural weaknesses within the economy, the most critical challenge is the high and growing level of unemployment in the province. In terms of the expanded definition of unemployment (which includes discouraged workers) 46% of the labour force is unemployed. This amounts to in excess of 1.6 million unemployed people for whom jobs must be created. In fact, entrants to the labour market (net of those who exit) averaged 155 000 per annum during the 1996 to 2001 period, in terms of the expanded definition of unemployment.

This means that merely to maintain the status quo of a 45% unemployment rate, 150,000 jobs have to be created each year. To make any inroads into the unemployment rate, far more than 150,000 jobs must be created. KZN's unemployment problem is exacerbated by the structural shifts that are emerging within the economy. As is the case in the national economy, as a consequence of trade liberalisation labour-intensive industries (for example, clothing and footwear) are declining, while capital, technology and skills intensive industries and sectors are expanding. In such a context, unemployment among the semi-skilled and unskilled mushrooms, while the economy's ability to grow is constrained by skill shortages.

Hence alongside employment creation, a human resource strategy that fast-tracks skill development – in a manner that is responsive to the demand for labour emanating from growing industries – is essential. It appears, however, that KZN's tertiary education institutions remain unresponsive to the skills required by its economy. Moreover, the decline in the matric pass rate and number of university exemptions suggests that the primary and secondary education system is not performing well. As South Africa's integration into the global economy proceeds, the skill base of its provinces will become much more important than their resource base as a driver of growth. Hence the KZN government must reform its education institutions as a matter of urgency.

As regards employment creation, Appendix A has argued that at this juncture of South Africa's development trajectory, labour-intensive exports do not provide an avenue for job creation. In a context where the majority of the unemployed are semi-skilled and unskilled, the expansion of economic activity in the non-tradables sector represents and avenue for job creation. Moreover, these sectors can be stimulated through government expenditure. In the construction sector, for example, the development of infrastructure will create a demand for unskilled and semi-skilled labour. In the context of KZN, phase 2 will provide a more comprehensive approach to tackling unemployment.

A further formidable challenge confronting KZN is the high prevalence of HIV/Aids. From the perspective of labour markets, while it will reduce unemployment it will also negatively impact on productivity as workers become symptomatic and will add to skill shortages when skilled workers afflicted by HIV/Aids exit the labour force. While the treatment of affected people remains the responsibility of the KZN Department of Health, the DEDT must be cognisant of its negative economic impact and develop a strategic framework for mitigating such impacts.

The high prevalence of HIV/Aids in KZN will, however, continue to create a growing demand for health services. Hence the sector must be capacitated, in terms of capital and skills, to grow in tandem with the demand for these services. This will not only provide a humane way of dealing with the victims of the HIV/AIDS epidemic, it will also create employment and generate multipliers.

The role of the informal sector within the KZN economy must be addressed if incomes and productivity within this sector are to be enhanced. Related to this is the challenge of facilitating entry of small, micro and medium enterprises into a range of sectors in the KZN economy. This is, in turn, related to black economic empowerment through both the creation of new economic opportunities and the transfer of ownership stakes in existing enterprises to empowerment companies.

While nodal developments have the potential to act as a catalyst for economic expansion, they may not yield the anticipated benefits if they are poorly conceived or inadequately implemented. In this regard, the Lubombo initiative appears to be on the wane as the expected investment has not been forthcoming. Hence it is imperative that the KZN government facilitates the inflow of such investment.

As regards the Dube Trade Port, while it holds enormous potential for positioning KZN within global supply chains the precise nature of the industries that will render it a success remains vague. If the KZN government is to secure national support for this initiative, the economic logic that will guarantee its success needs to be spelt out much more clearly. The identification of industrial clusters that could find a place within global supply chains is essential both for securing national support and ensuring that investment flows into the IDZ.

Of relevance to the two proposed IDZs is that there is a strong possibility that existing domestic and international firms will relocate to IDZs to enhance their export competitiveness. The net effect is therefore likely to be diversion of existing economic activity to IDZs: mostly, the best-case scenario in a low-growth economy is probably one where firms relocate and expand their business into export markets.

This will unleash a range of economic, social and political dynamics – including competition among provinces – with potentially undesirable outcomes. Clearly, there is a limit to the quantum of export-oriented firms that will locate in IDZs and the timing of their implementation, together with the locational advantages they offer in terms of access to inputs and transport nodes - will be a critical determinant of their spatial location. Hence there is some urgency to secure the designation and operators licences for the Richards Bay IDZ and Dube Trade Port.

In terms of institutional capacity to promote economic development, the key issue is that there is currently no overarching economic development policy to focus the activities of the various public entities that get their mandates from DEDT. It is clearly imperative that this vacuum in strategic orientation is remedied as a matter of urgency.

The lack of cooperation between provincial and national government (in particular, the DTI) currently acts as a constraint to the realisation of KZN's policy objectives. It is essential that the DEDT and its agencies facilitate the take-up of the incentives offered by DTI (for investment, competitiveness, innovation and SMMEs) by firms located at the provincial level. This is not only key to the expansion of existing enterprises, but to the promotion of greenfield investments. To accomplish this, the challenge is to build a functional relationship with DTI.

5.4 Conclusion

The KZN province, on the basis of its resource endowments and productive capacity, as well as the emerging structural changes within the provincial economy, has the potential to achieve much higher growth rates in the future. With effective government interventions, a number of latent opportunities can be unlocked. The critical challenges are employment creation, a more effective skills formation strategy and finding ways to mitigate the negative impact of HIV/Aids. A further challenge is to align national, provincial and local institutions and policy instruments to realise sustainable economic development in KZN.

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6 Appendix A: The national context: the impact of industrial policy

Provincial development strategies are located within the framework of national Industrial policy, over which provincial-level institutions such as the DEDT have little influence. Indeed, as highlighted in section 2, the role of provincial government is to implement these policies by utilising the instruments created by national government (for example, preferential market access and investment and incentives). Provincial level institutions are best placed to do so because of their superior understanding of the dynamics of the provincial economy.

To effectively steer the regional development trajectory, provincial government must be cognisant of the complexities of industrial policy and the rationale underpinning it. From a strategic perspective, it is essential that the institutional interface between national and provincial government enables the latter to effectively utilise its instruments to promote targeted industries within the regional economy.

This section sets the context within which the KZN economy has performed in the post-1994 period. To that end, an overview of South Africa's industrial development trajectory is provided. In addition, the shift in industrial policy in the post-1994 period is surveyed and its impact on the economy analysed.

6.1 Industrial development in historical perspective

South Africa's industrial development trajectory has been driven by import-substitution industrialisation. Due to the small size of the local market (a small economy and poor distribution of income) it is believed that import substitution opportunities were largely exhausted by the late 1970s. This fact substantially contributed to poor productivity, high levels of industrial concentration and slow growth throughout the economy.

There is widespread consensus that since the 1980s, failure to shift to export-oriented industrialisation policies has constrained the development of the manufacturing sector. This is because lack of exposure to international competition is inimical to enhanced efficiency and innovation. The critical factor underpinning South Africa's industrial development trajectory is, however, the fact that it is a "minerals economy".

As a "minerals economy", South Africa's industrial development has been driven by all the attendant complications associated with a 'resource curse' (Auty 1993, 1994, 1994a, Davis 1995, Ostensson 2000). In general, minerals economies tend to grow and to experience structural shifts more slowly than non-minerals exporters. They also tend to have a more capital-intensive structure of production. This can be explained by a number of characteristics that are common to these economies.

Other developing countries go through a phase of low wage, low productivity manufacturing development that has the impact of mopping up the labour surplus (Syrquin and Chenery 1989,). The pattern of development experienced by labour surplus developing economies usually follows along a familiar path, where under-productive labour moves off the farms, and into labour intensive manufacturing traded sectors. As there is a labour surplus, wages are low, and the sectors can therefore be highly competitive internationally. As the labour market becomes tighter, wages rise, and there is a shift to investment in more capital-intensive activities.

Only once there is a tighter labour market do wages begin to rise and the economy moves into the development of more capital and skill intensive industries. The emphasis on labour intensive tradables is a necessary step in an economy that is capital and foreign exchange constrained. Ultimately, the more successful newly industrialised countries are those that simultaneously invested in human capital development, so that the skills base developed alongside these structural shifts.

In contrast, the minerals economies tend to leap-frog from the resource base into heavy and chemicals industries (HCI) development, by-passing the development stage of labour intensive manufacturing. This is made possible by large resource rents. The mass creation of jobs in labour intensive tradables is not really viable in a context of high domestic cost structures: overvalued exchange rates caused by minerals exports earnings render labour intensive agricultural and manufactured exports uncompetitive. Nor is it a requirement of manufacturing development, as it is in developing economies that do not have ready access to capital and foreign exchange. This means that the benefits of the minerals economy do not tend to spread widely and high levels of income inequality and unemployment result, since the HCI sector is capital intensive. Moreover, domestic demand may not expand as much as in other economies.

In accordance with the experience of other minerals economies, South Africa bypassed the phase of development where large numbers of workers are absorbed into low cost, low skill labour intensive tradables. The ideal period for this phase arises where there is a labour surplus in a context of low economy-wide cost structures. In other words, the context of a less developed country where labour is cheap, but so is the cost of living. The low cost structures are often maintained by an agriculture sector that supports large numbers of under-employed workers.

The low growth and high levels of unemployment that characterise the South African economy today are a consequence of the development trajectory that is peculiar to minerals economies. The attendant price distortions were amplified by the political agenda of the Apartheid regime. These two factors inhibited role of the manufacturing sector as an engine of growth.

6.1.1 Early attempts at trade liberalisation

In the context of a stagnant and uncompetitive manufacturing sector, the movement towards more open global trade began in the late 1980s. A key factor constraining international competitiveness was the anti-export bias that the protectionist tariff regime had created. Anti-export bias is a disincentive to export, relative to producing for the domestic market, created by tariffs and other measures that protect domestic industries. This raises the profitability of selling into the domestic market, relative to exporting, because the price is higher. Domestic industry therefore has no incentive to export and hence no means of becoming internationally competitive.

The most far-reaching measure to redress anti-export bias was the General Export Incentive Scheme (GEIS), which was introduced in 1990. It was meant to help offset the competitive disadvantage experienced by South African firms as a result of inflation, exchange rate fluctuations and the price of local inputs. The amount of cash assistance offered by GEIS was varied by an inflation and exchange rate adjustment factor.

Even the most generous combination of incentives (the GEIS and duty rebates), however, did not equalise the price received in domestic and in export markets, so that an anti-export bias persisted. GEIS and the duty rebates both had the effect of raising the profitability of exports by reducing associated costs. However, the high rates of effective protection meant that there was still a price advantage in the local market, linked to import parity pricing. Since the GEIS incentive contravened World Trade Organisation (WTO) rules governing export subsidies, it was phased out by the end of 1997.

In combination with punitive welfare costs incurred by South African consumers - in the form of much higher prices relative to imports - and high and growing levels of unemployment, the structure of South Africa's manufacturing sector was clearly unsustainable when the democratic government took power in 1994.

6.1.2 Small firms and limited spread effects

Legal exclusion from vertical mobility severely limited the expansion of entrepreneurial or artisanal skills among the black population. Small clothing firms, regardless of race, have stagnated over the period studied. In the South African context, black firms have experienced even greater difficulty as a result of exclusionary legislation, insufficient availability of credit, market access and higher input costs (Nattrass and Nattrass 1988; Rogerson & da Silva 1986). Such shortages have had an impact on the supply of small businesses and on the organisation of production.

African traders had experienced discriminatory legislation since as early as the 1920s. Yet, the restrictions intensified from the mid-1950s with the evolution of the Separate Development ideology. Fundamentally, "...Africans resident in the townships and locations... (were)... regarded as 'temporary sojourners' in white South Africa" (Southall 1980). The restraints became particularly severe in 1963 when a circular was issued to local authorities by the Department of Bantu Administration and Development.

The implications of these controls are threefold: first, the restrictions on black business raised the cost of inputs and hindered their access to markets. Inputs for black businesses had to be bought from the White centres; transport costs raised the price of these goods. Moreover, the majority of township dwellers worked and spent a large part of their day in White areas. Yet, the Group Areas Act stipulated that Africans could operate businesses in black residential areas only (Nattrass & Nattrass 1988).

Second, access to credit constituted a major barrier to the development of African businesses. There had never been many sources of capital available to small business. The lack of freehold rights in urban areas precluded the possibility of using real estate as collateral against loans (Southall 1980).

Finally, an artisanal class was not developed during the period of industrialisation, as Whites were moving out of industry into higher paying jobs. This partly contributed to a concentration of production in large plants with relatively little subcontracting: small firms would have not developed the skills to supply the market. Moreover, the supply of skilled staff would have limited the ability of producers to expand horizontally.

6.2 Industrial policy in the post-1994 period

The democratically elected government faced a formidable challenge in reversing the stagnation of the manufacturing sector. The range of policy instruments at its disposal were more limited than during the apartheid era as a consequence of South Africa's re-entrance into the global economy after nearly two decades of isolation. In particular, accession to the World Trade Organisation occurred at a time when a number of measures (including export subsidies such as GEIS) were prohibited and developing countries were required to reduce their tariffs irreversibly.

In this context, the key challenge was to dismantle the protectionist tariff regime that had kept South Africa isolated from the global economy without bringing about deindustrialisation. In 1994, the key objectives with respect to the manufacturing sector were to open up the economy, improve international competitiveness, improve access to economic opportunities and foster greater geographical equity.

To that end, the ANC-led government implemented a range of measures that marked a radical departure from previous industrial policy. Far-reaching trade liberalisation (in the context of broader macroeconomic reform and liberalisation) was associated with South Africa's democratisation and re-integration into the global economy. In addition, supply-side interventions – targeted at specific industries, spatial locations and exporting sectors – replaced demand-side interventions as the key instruments of industrial policy. They were utilised to meet the central challenge: to reverse the psychology of protectionism and isolation that permeated the manufacturing sector.

6.2.1 Trade liberalisation

The structure of international trade and its influence on industrial structure has been quite dramatic over the 1990s, with many unexpected effects. The key changes in the trading environment were related to the system of protection, export promotion, and trade arrangements with key partners.

South Africa's offer of tariff bindings to the WTO in 1994 represents a decisive break with the highly protectionist nature of previous trade regimes. The salient elements of the offer were:

- A 5-year tariff reduction and rationalisation programme;
- The reduction of tariff categories from more than 100 to 6;
- Tariff category rates to range between 0% and 30%, with no discretionary changes permitted;
- Average import duties to be reduced from 34% to 17% for consumption goods, 8% to 4% for intermediate goods, and 11% to 5% for capital goods;
- A one-third reduction of the simple average tariff for industrial tariffs; and
- An 8-year extended time frame permitted for clothing, textile and automotive sectors.

After an initially rapid pace of tariff liberalisation between 1990 and 1996, with a reduction in the number of tariff lines from 12,500 to 8,250, a fall in the maximum tariff rate from 1,389% to 61%, and a reduction in the number of different tariff bands from 200 to 49, progress slowed considerably, with only marginal further reductions between 1996 and 1999. The number of tariff bands numbers still numbers more than 40, in comparison with the WTO commitment of 6, and the system remains complex with over 7000 lines.

As a central instrument of industrial policy, trade liberalisation, by dismantling a range of protectionist tariffs, has induced a far-reaching structural change in the economy. In the context of industrial policy it is necessary, however, to highlight that while trade liberalisation has been significant, anti-export bias persists. The persistence of anti-export bias after trade liberalisation is explained by a context in which a fall in tariffs did not compensate for reduced export incentives.

On the one hand, the most generous export incentive, GEIS, was dismantled due to its incompatibility with WTO export subsidy rules (Altman, 1995). On the other, while official tariffs have fallen, the actual amounts paid at customs are about the same. Indeed, Fedderke and Vaze (2000) after calculating average effective protection rates for the 1988-93 and 1994-98 period respectively, conclude that half of South Africa's GDP is produced in sectors where effective protection *rose* between the two periods, while only 15 percent comes from sectors where protection has fallen. The clothing sector is one important example of a trade sensitive industry, where the tariff paid at customs rose from 20% to 24% between 1991 and 2000, despite the dramatic fall in official rates (Altman 1995, van Seventer 2002).

6.2.2 *Securing market access*

During the immediate post-1994 period, the centrepiece of trade policy was securing market access to the economies of South Africa's main trading partners. Accession to the WTO, which necessitated an offer of tariff bindings, was a pre-condition for South Africa to benefit from the MFN tariff bindings of other WTO Member States. In addition, the government actively pursued Free Trade Areas (FTAs) with the European Union (EU) and the Southern African Development Community (SADC).

The EU-SA FTA, has not yet entered into force because it has not yet been ratified by a sufficient number of EU Member States. In contrast, the SADC FTA has been ratified by all Member States and entered into force in 2000.

An additional source of preferential market access is through the Africa Growth And Opportunities Act (AGOA). The Act extends the Generalised System of Preferences (which, in terms of the WTO's rules, allows developed countries to provide preferential access to developing countries for specific goods) for qualifying African countries to September 2008. It extends the existing list of 4,650 products by 1,837. Thirty-four sub-Saharan African countries, including South Africa, qualify for AGOA.

6.2.3 *The impact of trade liberalisation*

The reduction of tariffs and preferential market access has had a profound impact on the structure and development of industry. On a positive note, Cassim *et al* (2002) demonstrate that despite significant import penetration in previously protected sectors, there has been no evidence of de-industrialisation as a consequence of trade liberalisation.

At the aggregate level, exports have grown by 5.5% per annum during the 1991 to 2000 period. A disaggregation of this data reveals that exports emanating from the primary sector (agriculture and minerals) declined by -1.5% per annum, while manufacturing and services exports increased by 11.2% and 9.9% per annum respectively. This represents a significant structural change in the composition of exports, reflecting more closely trends in other middle-income developing countries.

A disaggregation of manufactured exports reveals that most sectors have experienced an increase in exports. The highest weighted average annual growth in exports occurred in furniture (28.9%), television and communications equipment (27.6%), transport equipment (23%) and plastic products (22%). In contrast, exports emanating from the mining sector declined over this period at an annual rate of -3.7% for gold mining, -1.9% for other mining and -0.9% for coal mining. This demonstrates a marked departure from South Africa's traditional export profile, which has historically been dominated by minerals.

Of note is the rapid growth of exports in the automotive industry, which averaged 20% during the 1991 to 2000 period. This occurred in the context of targeted policy interventions within the framework of the motor industry development programme

(MIDP), and therefore cannot be attributed to trade liberalisation alone. The impact of the MIDP is analysed in detail later in this chapter.

6.2.4 The African market is driving export growth

Although South Africa does not enjoy preferential access to SADC (because of the asymmetrical nature of the FTA), it is the growth of manufactured exports to these countries that has underpinned the structural changes within the manufacturing sector. Exports to Africa have grown by 480% over the 1992 to 2001 period. Moreover, approximately 80% to 90% of manufactured exports are destined for SADC markets. If SACU markets are included, Africa becomes the second largest export market after the EU.

While South Africa imports manufactured exports from the EU and exports primary commodities to that market, the exact reverse is true of the African market. For example, almost 70% of South Africa's trade with Africa comprised: machinery and equipment (16%), base metals and metal articles (10%), chemicals (12%), transport vehicles and equipment (9%), prepared foods (10%), plastics (7%) and pulp and paper (5%). In contrast, half of South Africa's exports to the EU were in the categories of mineral products (19%), base metals (11%), precious and semi-precious stones and metals (15%) and vegetable products (5%). Hence the stimulus to higher value growth in South Africa is clearly driven by exports to the African market.

6.2.5 Trade liberalisation and unemployment

South Africa's high and rising unemployment has recently been attributed to globalisation and the increasing openness of the South African economy, leading to shifts in the skills composition in the demand for labour. The demand for lower skill labour has fallen, in the context of a very large oversupply, and the demand for higher skill labour has risen in the context of a severe skills shortage (Bell and Cattaneo 1997, Bhorat and Hodge 1999, HSRC 1999).

Table 6.1 summarises trends in employment during the1991 to 2000 period. The data starkly illustrates the "jobless growth" that has characterised the South African economy in the post-1994 period. In a context of buoyant export growth – averaging 5.5% per annum in aggregate and 11.2% per annum in the manufacturing sector – the absence of employment growth appears to be a perverse outcome.

Table 6.1 – Trends in employment, 1991 – 2000 (%)

Sector	1991-1995	1996-2000	1991-2000
Primary	-2.5	-5.2	-3.5
Manufacturing	-1.2	-3.0	-1.5
Services	0.3	-0.7	0.1
Total	-0.5	-1.9	-0.9

[Source: TIPS standardised industrial database (2002)]

An analysis of the factors driving the growth of exports and the concomitant demand for labour reveals, however, that it is consistent with declining employment. Trade liberalisation has two distinct impacts that affect employment levels: structural changes at the level of the firm to enhance international competitiveness, and import penetration into previously protected sectors.

Edwards (2001), in an analysis of structural change, trade liberalisation and employment, finds that since 1984 – and particularly between 1993 and 1997 – there has been an increase in the capital intensity of exports as a consequence of technological change. It has therefore resulted in rising skills intensity in manufacturing and services.

Indeed, unskilled labour-intensive exports declined from 8.9% to 6.8% of total exports between 1992 and 1999, while human capital-intensive exports increased from 49.5% to 58.5% during the same period (Lewis 2002). Moreover, an analysis of factor intensity in exports finds that South Africa has a remarkably low, and declining, share of exports that use unskilled labour, and a relatively high share of exports using more skilled labour (Lewis, 2001). This explains why the manufacturing sector has not created jobs despite the rapid growth in exports.

The DTI (2002) acknowledges that there is a correlation between industries that have become increasingly export-oriented and high rates of investment in capital equipment and capital and skills-intensive technology. This is seen as a necessary structural change to gear up for international competition and partly accounts for the 26% increase in labour productivity that has occurred since 1994. Moreover, many of the sectors that have rapidly increased their output are less labour intensive than the manufacturing sector in aggregate.

In sum, trade liberalisation has altered the structure of South Africa's economy, as evidenced by a contraction of exports emanating from the primary sector and buoyant growth of exports emanating from the manufacturing and services sector. This has, in turn, altered the nature of the demand for labour and exacerbated high levels of unemployment.

6.3 Supply-side policies

Trade liberalisation was implemented in tandem with a range of supply-side policies to promote the international competitiveness of the manufacturing sector and encourage its expansion through investment. The shift from demand to supply-side policies as the main instrument of industrial policy represented a decisive break with the policies pursued during the Apartheid era.

The following supply-side measures were pursued in the post-1994 period:

- The Motor Industry Development Programme (MIDP);
- The Duty Credit Certificate Scheme (DCCS) for the clothing and textiles sector;
- A range of measures to promote exports across all sectors (including duty drawbacks for inputs utilised in the manufacture of exports, export marketing assistance, a number of schemes to promote technological advance and competitiveness and the development of export councils);
- Investment promotion;
- Black economic empowerment;
- The development of the small, micro and medium enterprise (SMME) sector; The restructuring of state-owned enterprises in the transport, energy and telecommunications sectors; and
- Spatial policies to redress geographical inequities, in particular, spatial development initiatives and industrial development zones.

6.3.1 The Motor Industry Development Programme

The MIDP is a concrete example of the successful application of industrial policy to re-position an uncompetitive industry in the face of declining tariff protection. It was initiated in recognition of the problems besetting the domestic automotive industry in a context of trade liberalization: its high-cost structure and low volume production that resulted from the various local content programmes that had protected it for over three decades. Its objective was to entrench the outward orientation of the automotive industry, thereby restructuring it to achieve global competitiveness, whilst at the same time maintaining its employment and output contribution to the South African economy (Black, 1998).

The key policy instrument of the MIDP is the encouragement of higher volumes of exports by allowing exporting firms to earn rebates that can be used to offset automotive import duties whilst exposing the industry to greater global competition through tariff reductions. Import Rebate Credit Certificates (IRCCs) are issued to exporters of qualifying built-up vehicles and automotive components based on the value of the exports less the foreign content of those particular exports. In essence, the programme rewards firms that export by enabling them to reduce their input costs through duty drawbacks on imported components.

As alluded to earlier, exports emanating from the automotive sector averaged 20% during the 1991 to 2000 period. This buoyant export performance from a sector that risked collapse as a consequence of exposure to international competition is a clear indication of the success of the policy. Its success may be attributed to the fact that government was able to position the domestic automotive industry within international supply-chains in cooperation with multi-national corporations. This has highlighted the imperative of positioning South Africa's manufacturing sector within global supply chains as a key to its expansion and international competitiveness.

6.3.2 Clothing and Textiles: The Duty Credit Certificate Scheme

In the clothing and textile sector, the DTI utilised a similar policy instrument in the form of the Duty Credit Certificate Scheme (DCCs). It was introduced on 1 April 1993 to replace two schemes that had been the pillars of state support to this industry: GEIS and the structural adjustment programme (SAP). As alluded to earlier, these schemes were dismantled because they were not compatible with WTO regulations.

The DCCs is a system of earning duty credits based on exports of textile and clothing products. It provides a duty rebate to the value of 30% of the value of exports for clothing, 20% for household textiles and 10% for fabric and other textiles.

In aggregate, the clothing and textile sector has improved its export performance as evidenced by an annual average growth rate of exports of 5% for textiles and 7% for clothing, during the 1991 to 2000 period. Whether the DCCs contributed towards this outcome, or whether other factors such as declining tariffs and better market access to the EU and US markets, remains a moot point in the absence of definitive evidence. It is, however, reasonable to surmise that it is a combination of these factors. Despite its improved export performance, this sector has, however, grown very slowly since 1994 and has been shedding jobs.

One reason for limited programme impact may be due to the policy approach. Unlike the motor industry programme, clothing industry policy has not attempted to strategically position the sector within global supply chains. This may be partly due to the more dispersed character of the clothing industry.

6.3.3 Export promotion

A further supply-side intervention introduced by the DTI in the post-1994 period was economy-wide export promotion. This measure targets all export-oriented firms in the manufacturing sector. It utilises a range of policy instruments that are outlined below.

The 470.03 rebate scheme is a duty drawback that allows firms in any sector to import inputs for production of exports duty-free. It is a continuation of the pre-1994 duty drawback scheme alluded to earlier, but is more generous in that it allows exporters to a rebate equivalent to 100% of the cost of imported inputs. It's objective is to redress anti-export bias by lowering input costs.

The Export, Marketing and Investment Assistance (EMIA) scheme partially compensates exporters for costs incurred in respect of activities aimed at developing export markets for South African products and services and to recruit new foreign direct investment into South Africa. It provides exporters with financial assistance to showcase their products and services internationally and assists in their matchmaking process to secure exports and foreign direct investments. It also assists in offsetting the exporters' marketing costs.

Emulating the New Zealand model, the DTI promotes the formation of industry-based export councils. In partnership with the DTI, many export-orientated firms in various industrial sectors have already organised themselves into 20 sector Export Councils whose main objective is to tackle the global market place as a collective force. Executives appointed by the exporting firms serve on these Export Councils.

In addition, the DTI has developed a range of schemes to promote the competitiveness of the manufacturing sector. These include the competitiveness fund (which provides companies access to knowledge about new technologies, production processes and markets to improve their competitiveness), the sector partnership fund (which provides financial assistance to partnerships of five or more firms/organizations in the manufacturing, agro-processing or ITC industries to define and implement collaborative projects related to production and marketing that will enhance their productivity and international competitiveness), the support programme for industrial innovation (which promote manufacturing of technologically innovative products or processes in South Africa that are globally competitive), and the technology for human resources for industry programme (which is an incentive where industry and government contribute financially to the research efforts of academic partners, specifically in the area of training of students).

Collectively, these export promotion measures have played an important role in permeating the psychology of protectionism that characterised the manufacturing sector in 1994. They have also served as a platform for government to forge cooperation with the private sector in its pursuit of an internationally competitive manufacturing sector.

6.3.4 Investment promotion

Low level of aggregate savings in South Africa poses a critical constraint to growth. In such a context, the ability to attract foreign direct investment (FDI) can accelerate growth by expanding potential investment beyond the limits set by domestic savings.

To that end, the DTI has developed a range of incentives to attract FDI and channel domestic investment into export-oriented manufacturing sectors. Such incentives may be categorised as supply-side instruments of industrial policy. At present, they include:

- The Critical Infrastructure Programme provides subsidised support for economic infrastructure required for specific committed productive investment;
- The Foreign Investment Grant aims to encourage foreign entrepreneurs to invest in new manufacturing concerns in South Africa by compensating the

foreign entrepreneur for the qualifying costs of moving new machinery and equipment from abroad to South Africa;

- The Skills Support Program (SSP) is a cash grant for skills development with the objective of encouraging greater investment in training and creating opportunities for the introduction of new advanced skills. It is available for new projects or the expansion of existing projects;
- The Strategic Industrial Projects (SIP) scheme was introduced in 2001. It is an incentive programme designed to encourage investments into South Africa from both local and foreign investors. It provides industrial investment allowances, in the form of tax relief, to qualifying industrial projects;
- Direct financial contributions to the investor for travelling to South Africa to visit potential investment sites and companies; and
- The Small and Medium Enterprise Development Programme (SMEDP) offers a cash grant to cover initial capital expenditure in the start up or expansion of a company, over 2 to 3 years.

The incentives offered by the SA government are unlikely to shift the structure of production, nor attract foreign investment. Instead, they are designed to shift the risk-return ratio in investment decisions. For large firms, the incentive raises the return to investment, overcoming risk differentials in investing in SA as opposed to other middle-income economies. SA government has chosen not to offer extremely attractive incentives, as they were not seen to be sufficiently efficacious nor promoting of the desired forms of investment. Instead, the incentives are de

For small and medium sized firms, the incentives help bridge initial cash flow problems that often contribute to business failure in the first 3 years of a company's life. The SMEDP now also includes expansions, where many sustainable jobs are created. Finally, there is intention to move beyond manufacturing, to tourism, high value agriculture, cultural industries, ICT and recycling. Tourism is the first to be introduced. This is an important step for the DTI, in its move toward recognising the importance of services and labour intensive investment in the SA economy.

6.3.5 Black economic empowerment

In a bid to reverse the legacy of Apartheid, government has committed itself to pursuing black economic empowerment (BEE). The objective is to "redress the imbalances of the past by seeking to substantially and equitably transfer and confer the ownership, management and control of South Africa's financial and economic resources to the majority of its citizens" (BEE Commission, 2001).

The policy instruments created by government to realise this objective include its procurement policies, the restructuring of state-owned enterprises and a range of empowerment funds administered by the IDC. There is widespread consensus that government has made little progress in fostering BEE. This is evidenced by the fact that while the market capitalisation of black controlled firms rose from 3% in 1997 to 6.8% in 1998, it declined spectacularly to less than 1.5% by 2002.

Indeed, government has admitted that, "the significant broadening of black ownership that was hoped for has not materialised" (DTI, 2002:19). Hence a process to develop a strategy to more effectively implement BEE is currently underway. Indeed, at a Cabinet Lekgotla held in August 2002, Cabinet resolved to "take decisive action to bring black South Africans into the economic mainstream. The central thrust of the BEE strategy is the setting of clear targets for government and the identification of key instruments that will be used to promote BEE" (DTI, 2002).

6.3.6 Small micro and medium enterprises

Related to BEE is government's policy of promoting the SMME sector. A myriad of complex regulations effectively prevented the entry of firms of this scale to many industries during the apartheid era. More to the point, the Apartheid government made most forms of black business ownership illegal. In a bid to reverse this legacy, government has dismantled these regulations and provided a range of financial and non-financial instruments to promote this sector.

Indeed, the SMME sector is viewed as a panacea. It is expected to fulfil a number of roles, ranging from poverty alleviation and employment creation to international competitiveness. Despite the creation of an array policy instruments and institutions to promote SMMEs, the DTI (2002:18) has acknowledged that "the survival rate of small business remains low by international standards, and we have failed to develop a vibrant critical mass of small entrepreneurs that are effectively integrated into the mainstream operations of all sectors."

The National Small Business Act, promulgated in 1996, legalised the establishment of new institutions to promote the SMME sector, in particular Khula (to provide wholesale finance), and Ntsika Enterprise Promotion Agency (NEPA), to provide non-financial support. In addition, the DTI and Industrial Development Corporation (IDC) have a range of specific programmes to encourage the competitiveness of SMMEs.

These policies have, however, largely failed as evidenced by the small number of SMMEs that use them. Berry *et al* (2002:34) estimate that a mere 6% of SMMEs use support programmes and argue that this is "due to distrust of external agencies among SMMEs and incapacity to raise awareness about their existence and efficiency". Moreover, the poor coordination of service providers results in a replication of services and clustering of institutions in urban areas (Ntsika, 1999).

In the context of high and growing levels of unemployment, the SMME sector remains an important source of job creation. This is because SMMEs are generally more labour-intensive than larger firms and hence have a higher labour-absorption capacity. The evidence suggests that employment growth in the SMME sector is not from the expansion of existing SMMEs, but from the formation of new micro and survivalist enterprises (Berry et al, 2002). This suggests that the employment created is of the low-wage, low-productivity variety, which is inimical to redressing poverty and inequality.

As the majority of SMMEs operate in the non-traded sector, its growth is dependent on domestic demand. It is therefore unlikely that the SMME sector will act as a catalyst to growth. Instead, its growth or decline will reflect what is happening in the broader economy. This is partly why – after six years of SMME promotion – government has failed to transform the SMME economy into a vibrant small business sector.

6.3.7 Restructuring of state-owned enterprises

The inefficiencies and high costs associated with state-owned enterprises that provide infrastructure in the areas of transport, energy and telecommunications has been identified as an impediment to the competitiveness of the manufacturing sector. Hence, in 1999 the Department of Public Enterprises developed a policy framework to fast-track the restructuring of Telkom, Transnet (in particular Spoornet and Portnet) and Eskom. This constitutes a supply-side measure.

While Eskom is widely regarded as an efficient energy utility and the low cost of electricity a competitive advantage to the manufacturing sector, Transnet is notorious for its inefficiencies and high cost structures. The persistent congestion at the port of Durban, which houses the largest container terminal in South Africa is well documented. This is exacerbated by a pricing structure that is *ad valorem* and hence acts as a disincentive to the export of low-volume, high value goods. The inability of Spoornet to transport goods between Gauteng and the port of Durban in less than six days has long been a complaint of manufacturers. Consequently, many products are transported by road (as they arrive at their destination within ten hours) at a high cost to the South African tax-payer, because of the externalities generated by heavy vehicles.

In the case of Telkom, it must be acknowledged that telecommunications has improved since 30% of the enterprise was sold to a strategic equity partner. Telecommunications services, as the backbone of a knowledge-intensive economy, however, remain well below international best practice. Indeed, a recent study by DTI (2002) into the use of ICT in several industrial sectors, found that the lack of effective and affordable telecommunications services ranked as the most important impediment to ICT diffusion and a major competitive disadvantage in the global economy.

Government's intention of accelerating the restructuring of these enterprises has, however, failed to materialise. Conflicting political agendas within government, coupled with opposition from COSATU and the enterprises themselves, has effectively put a brake on their restructuring. Indeed, government has signalled its intention to slow down the restructuring process until after the 2004 election.

While there are a number of political difficulties surrounding the restructuring of SOEs - including the fact that in an economy with extremely high levels of unemployment it will result in more job losses – this supply-side intervention is probably the single most important means of improving South Africa's competitiveness, attracting FDI and realising the objectives of BEE.

6.3.8 Spatial development initiatives

Spatial policies are, in essence, supply-side measures that target particular geographical locations and provide a range of support measures to develop industrial capacity or build on existing capacity. In the context of industrial policy, spatial development initiatives (SDIs) and industrial development zones (IDZs) have been the key instruments to influence the spatial distribution of industrial activity. They are a means of achieving greater geographical equity in the spread of economic activities and investment. They are also a way of focusing resources on select locations, where opportunities are identified within this spread. These initiatives are discussed in detail in section 4, in relation to the 3 SDIs and 2 IDZs currently being implemented in KZN.

6.4 The impact of industrial policy

The objective of industrial policy in the post-1994 era – utilising trade liberalisation and supply-side measures as instruments – was to restructure the manufacturing sector in order to render it competitive in the international arena. This was expected to drive higher rates of growth and create sufficient employment to reverse the high levels of unemployment prevailing in 1994.

By 2000, only some of these objectives had been met. That industrial policy was successful in enhancing the international competitiveness of the manufacturing sector is unequivocal as evidenced by a marked increase in exports, despite persistent anti-export bias. The contribution of the manufacturing sector to growth and employment creation has, however, been disappointing. This outcome can be attributed to the fact that international competitiveness requires industry-level technological change that is biased towards skills and capital-intensive manufacturing processes.

Between 1997 and 2001 the average output of the manufacturing sector grew by a mere 1.8% per annum (DTI, 2002), well below economy-wide growth rates. This growth appears to be related to the expansion of manufactured exports, which grew from 39% to 51% of total exports (in the context of an aggregate growth in exports of 5.5% per annum) between 1994 and 2000. The fact that exports have grown in skills-intensive sectors accounts for the failure to create employment. It also constrains the continued growth of these sectors in a context of skills shortages.

Weak capital formation has contributed to slow economic and employment growth. Gross capital formation as a percentage of GDP had started to rise from about 15% to 17% in 1998, but then fell back to original levels thereafter. This rate of investment is only enough to keep up with depreciation, and will not support GDP growth higher than current rates in the region of about 2.5% per annum. At these rates, and average capacity utilisation at about 80.5%, there may be little incentive for firms to invest. Unsurprisingly, it is the more export-oriented firms that have added capacity, seemingly to take advantage of the Rand depreciation and new trade arrangements.

A positive impact is that industrial policy has led to a more competitive environment. This refers not only to import competition, but also enhanced opportunities for business entry generally with, for example, the demise of single channel marketing in agriculture, the deregulation of bread (and the entry of small bakeries and millers), and greater opportunities in retail and wholesale trade and finance. This new environment has, in some cases, resulted in greater ease of entry, improved flows of information, and greater expectations of knowledge intensity in production and trade.

The unintended consequence from an employment perspective was the important hand of industrial policy in shifting the structure of the economy to one that is even more capital and skills absorbing. On the one hand, manufacturing industries have shifted toward more capital and skills-using technologies. On the other, many of the resource-based industries, particularly mining and agriculture, that had been the main employers of low and semi-skilled labour, shed substantial numbers of jobs. While the production profile now better represents one associated with a middle-income economy, these shifts have exacerbated structural unemployment.

6.5 Industrial policy post-2000

The failure of industrial policy and broader macro-economic reform to yield sufficient economic growth or investment to enable government to meet its aims of alleviating poverty, redistributing wealth or eradicating structural unemployment, led policy-makers back to the drawing board. A critical review of the policies that had been implemented between 1994 and 2000 prompted government to augment and refine the instruments of industrial policy. The new policy approach is articulated in government's over-arching micro-economic reform strategy and DTI's integrated manufacturing strategy.

President Mbeki unveiled the microeconomic reform strategy in early 2002. It is a response to the fact that the emphasis on macroeconomic reform (including trade liberalisation) between 1994 and 2000 has not yielded sufficient economic growth to enable government to meet its aims of alleviating poverty, redistributing wealth and eradicating structural unemployment. Hence government has recognised that the long-term development of the South African economy is contingent on a more thoroughgoing reform programme to tackle its structural deficiencies. Government proposes to do this through a systemic approach to eliminating constraints in the economy and improving efficiency.

Such constraints include appropriate and efficient economic and social infrastructure, access to finance for productive activities, investment in research and development, innovation and the take-up of new technologies, as well as investment in human capital and an adaptive, flexible workforce.

In the manufacturing sector, DTI's integrated manufacturing strategy (IMS) articulates government's policy approach. It is premised on the view that reliance on traditional bases for competitiveness – in particular, abundant natural resources and cheap unskilled labour – will not create a modern, outward looking economy that is essential for growth.

Instead, competitiveness should be built on increased knowledge intensity and value addition. New sources of competitiveness are located in the development of the ICT sector, the impact of technological change on production processes and the importance of time and efficiency to production costs. The emergence of integrated supply or value chains – in many cases trans-national and influenced by the operations of multinational corporations - is seen as a hallmark of modern production processes.

In such a global context, government believes that "the challenge for emerging economies such as South Africa which have a resource-oriented legacy is to ensure the opportunities within the domestic economy are developed and integrated advantageously into both domestic and trans-national value chains, in order to meet national socio-economic objectives" (DTI, 2002).

To that end, five sectors of the economy have been targeted because government believes they have considerable potential for increased outputs, exports, and employment creation. These sectors are export sectors, agriculture, tourism, ICTs, and cultural industries. Export sectors targeted by government include clothing and textiles; auto, auto components and transport; agro-processing; mining, metals and minerals beneficiation, chemicals and biotechnology; crafts; and information and communication technology. In the context of a low growth economy it is not surprising that exports have been targeted as a growth sector, given that the growth in global exports has been significantly higher than the growth of global GDP during the 1990s.

Government has signalled its intention to play a proactive role in developing value chains by mobilising infrastructure development and directing investment (both public and private) to these activities. The measures for the DTI to achieve this comprise the championing of competitiveness within government (suggesting that there is currently no unity of purpose), customised support measures (i.e. targeting specific sectors or value chains), and broad-based support measures that address generic areas that affect competitiveness, for example, market access.

Whether the broadening and reconfiguration of industrial policy set out in government's microeconomic reform strategy and the DTI's IMS will accomplish the objectives of higher growth in the manufacturing sector and lower levels of unemployment in the broader economy is uncertain. There is still an uneasy and unspecified relationship between the objective of creating a modern, outwardly focussed economy with the imperative of reducing unemployment among the unskilled and semi-skilled.

The IMS relies on a rapid increase in the skills base, in order to meet the demands of a knowledge-intensive development trajectory. This begs the question as to where the unskilled and semi-skilled workers that currently comprise the vast majority of the unemployed will be absorbed. Moreover, how will the pool of skilled labour be exponentially expanded? While the DTI (2002) identifies this as a central challenge of the IMS, an exposition of how this will be tackled at a policy level is conspicuously absent.

6.6 Conclusion

The central issue in relation to industrial policy is redressing an unemployment level that is economically, politically and socially unsustainable. The expansion of manufactured exports has created a sense that the economy is finally moving onto the right track and that it will start generating more employment. National policy is premised on the idea that employment growth will depend on expansion into global markets. This makes intuitive sense, except that the development path that generates substantial numbers of jobs through labour intensive exports is more associated with low income, non-minerals exporting economies.

Minerals economies tend to have different development trajectories from other economies. As alluded to earlier, like many other minerals exporting economies, South Africa leap-frogged this stage of development, investing at an early stage in heavy industry. This has generated path dependence in the economy, due to both resource curse and Apartheid legacy, resulting in many structural biases to capital intensity, alongside a low proportion of skilled workers.

Given international experience of minerals exporting economies, it appears that policy to promote employment, especially in the medium term, may be somewhat distinct from that to promote other economic objectives such as technological learning, foreign exchange and government revenues. They are not *competing* objectives, but rather *complementary* ones: it will not be possible to promote the employment absorbing non-traded goods and services sectors, and further underpin welfare schemes for the long term unemployed, unless there is an expansion in the higher value traded sectors as these latter sectors support less productive members of the population.

7 Appendix B: Ithala's property portfolio

Name	Locality and market	Description	Management	Tenant mix	Size
Eminent Rail Centre	Tanner Road, Empangeni Rail with linked taxi rank and an adjacent bus rank.	Comprising land and fragmented buildings, including kiosks, factory shops, an anchor tenant, managed vendor stalls and retail outlets. It includes a taxi rank office. Acquired by Ithala in August 1997 and upgraded in 1999.	Ithala Development Finance Corporation Limited.	Bank, bottle store, supermarket, pharmacy, fast-food outlets, hairdresser, phone shops, funeral parlour and other specialty stores.	9,187m^2 for 60 individual shops.
Eshowe Centre	Situated in Osborne Road, Eshowe, on the Northern Coastal belt in area central to the surrounding districts of Inkanyezi, Ongoye, Mtunzini, Nkandla and Ntumeni.				
Estcourt Centre	Near Estcourt's main trading area, serving mainly bus and taxi commuters.				
Eston Shopping Centre	Situated at the crossroads to Eston and Mpumalanga/ Hammarsdale, the main arterial route from Pietermaritzburg to Kingsburgh and the South Coast and the sugar cane/game farm country on the Sakabula Tourist circuit. The centre's primary market area is the Beaumont/Eston/Mid-Illovo region.	Comprises 10 shops in a Natal Verandah strip formation.	Ithala.	Liquor store (wholesale and retail) and other businesses.	2,250m^2 trading area to 10 shops ranging from 40m^2 - 800m^2.
Harding Shopping Centre	Situated in the centre of the town and serves communities as far afield as the Eastern Cape.				

Name	Locality and market	Description	Management	Tenant mix	Size
Isithebe Commercial Centre	Corner of Blue and Yellow Streets in the heart of Isithebe Industrial Estate on KwaZulu-Natal's north coast	Double storey face brick building.	Ithala	IT and office equipment rental companies and national and individual service providers who provide support services to the industries in the Isithebe Industrial Estate.	Ground floor includes 12 retail commercial units from $25m^2$ - $100m^2$. First floor has 32 offices from $15m^2$ - $25m^2$.
Jozini Shopping Centre	On Main Road, Jozini, a small town in North Eastern KwaZulu-Natal, on the main route to Mozambique	The centre comprises facebrick buildings opened for trading in August 1995.		A supermarket, clothing and shoe shops, a branch of Ithala, a bakery and confectioners, hardware and motor spares, and specialty outlets.	2,200m^2 centre with 16 shops, ranging from $18m^2$ - $780m^2$ including a $675m^2$ office complex.
KwaMashu Shopping Centre	On Site P, Malandela Road, KwaMashu, 10km north of Durban.	It comprises a one-stop shopping centre opened for trading in1980, upgraded and extended in 1994.	Ithala	Major national retail chain store groups and private owners, includes fast-food, clothing, furniture, a supermarket, bottle store, banks, specialty outlets, a post office and doctors' consulting rooms.	Approximately 9,500m^2 with 34 shops from $10m^2$ - 4,000m^2.
Madadeni Shopping	In the CBD of Madadeni, a suburban township on the outskirts of Newcastle, KwaZulu-Natal. It serves an urban catchment population of more than 200 000.	Includes an open and enclosed mall-type design with a bus/taxi rank, a formal promotional area with public address and hi-tech security system. Operating since 1980 and upgraded in 1995.	Ithala	Supermarket, branch of Ithala, post office, clothing and bottle store, butchery and various small shops and offices	Total lettable area of 9,381m^2 divided into 56 shops from $13m^2$ - 2,500m^2.
Makhathini Shopping Centre	Situated on Main Road, Jozini, in North Eastern KwaZulu-Natal on the main road to Mozambique	L-shaped single strip face brick buildings an on site petrol filling station and convenience store. Opened for trading in June 2000,		Supermarket, clothing shops, doctor's surgery, franchised fast food outlet and national furniture retailers.	4,256m^2 centre with 19 shops, from $24m^2$ to 1,139m^2.

Name	Locality and market	Description	Management	Tenant mix	Size
Manguzi Shopping	In the middle of Manguzi in KwaNgwanase, along the main road to Kosi Bay, near the Mozambique border.	The centre comprises a facebrick U-shaped open shopping mall with customer parking bays in the middle. Behind the centre are seven houses for management and staff of the tenants' shops, rentable from Ithala, a taxi rank and Taxi Association offices.	Ithala	A supermarket, pharmacy, doctor's rooms, furniture and clothing shops, a liquor store, bank and a takeaway.	The centre offers a 7,975 m^2 trading area to 29 shops and two warehouses. These shops range in size from 50 m^2 - 2 800 m^2.
Nongoma Plaza	Situated in Main Street, Nongoma, one of the busiest towns in rural KwaZulu-Natal.	Nongoma Plaza Limited, a subsidiary of Ithala, built in three wings, owns a one-stop shopping centre. Opened for trading in November 1992.	Ithala manages the centre in terms of a Management Agreement with Nongoma Plaza Limited.	Major national retail chain store groups and private owners and includes food, clothing, furniture, supermarket, bottle store, butchery, banks and specialty outlets, a post office and a garage/filling station.	
Ondini Plaza	Princess Magogo Road, Ulundi, operating as the centre of business activities in the town.	Facebrick property comprises an open mall-style shopping complex, providing a one-stop shopping centre, which The property belongs to Ithala. Adjacent is a taxi rank and informal market stalls. Operational since November 1988.	Ithala	Major national retail chain store groups and private owners and includes food, a number of clothing, furniture, supermarket, bottle store, post office, micro-lenders, hairdressers, banks and speciality outlets.	14,903 m^2 trading area to 51 shops, ranging in size from $50m^2$ – $2,200m^2$.
Power Centre	On the site of the old power station off Otto Volek Road, New Germany, The centre's primary market area includes the total Pinetown/New Germany functional region.	The centre is a value-type centre, offering customers a factory shop experience. The centre provides 24-hour security, 348 parking bays, promotional activities, and cleaning and centre management team.		Factory outlets comprising air conditioning, fabrics, clothing, printing works, plastic furniture and packaging, as well as retail outlets comprising restaurant and pub, liquor store, book store, take-away, coffee shop, pets' parlour.	$5,900m^2$ in lettable space, with shop sizes ranging from $49m^2$ - $310m^2$.

Name	Locality and market	Description	Management	Tenant mix	Size
Sundumbili Plaza	On the farm Amanda, Inkanyezi District, adjacent to the Sundumbili Township, near the industrial town of Isithebe, on the border of Mandini, KwaZulu-Natal North Coast.	A supermarket and the Post Office anchor the facebrick U-shaped open mall shopping centre. It provides a one-stop local shopping centre, informal market stalls and taxi rank areas. Sundumbili Plaza Limited, a subsidiary company of Ithala, owns it. Opened for business in October 1991.	Ithala manages the centre in terms of a Management Agreement with Sundumbili Plaza Limited.	Comprises some of the major national retail chain store groups and private owners and includes food, clothing, furniture, supermarket, pharmacy, doctors' surgery, speciality outlets and a post office	13,809m² trading area to 41 shops ranging in size from 50m² – 5,000m².
Tugela Ferry Shopping Centre	Situated in Main Street, Tugela Ferry, between Greytown and Dundee. The complex is the CBD of the village and also the final destination of local taxi routes.	It comprises an open mall-style shopping complex, providing a one-stop shopping centre, incorporated provision for micro (small) traders - informal traders and taxis. Opened for business in 1997	Ithala	The tenant mix comprises a number of major national retail chain store groups and private owners and includes fast-food, clothing, furniture, supermarket, doctors' consulting rooms as well as a branch of Ithala.	4,333m² trading area to 23 shops, ranging in size from 10m² – 1,200m².
Umlazi Shopping Centre	Forms the core of the Umlazi CBD, together with the Government offices of Amawele, the Durban Metro Library and electricity and water offices. It is approximately 12 km from the DIA & 25 km from the Durban CBD.	Two-level enclosed mall, which incorporates informal traders' stalls and a stand-alone Post Office. A number of outside line shops operate beyond normal trading hours.	Ithala	Supermarket, furniture store, shoe and clothing stores, pharmacy, take-away, liquor store, butchery and financial institutions, the Post Office and a TAB.	10,850m² with 38 shops ranging from 27m² - 2,571m².
Umlazi 'V'	Situated at the intersection of Umlazi 'V' main road and Mangosuthu Highway, adjacent to a BP Service Station.	Double-storey U-shaped facebrick office-park service centre, with an ATM facility	Ithala	Includes a bakery, superette butchery, the medical services of general practitioners, a dentist and medical specialists.	1,200m² with 10 shops, ranging from 78m² - 200m².