In pursuance of the CONTRACTING PARTIES' Decision of 12 April 1989 concerning the Trade Policies Review Mechanism (BISD 36S/403), the initial full report by the Republic of South Africa for the review by the Council is attached.
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I. INDUSTRIAL TRADE POLICY

A. TRADE POLICIES AND PRACTICES

(1) Introduction

Due to a new political dispensation taking shape in South Africa and as international trade sanctions against the country are being lifted, South Africa’s trade policy is, of necessity, undergoing certain changes.

In this regard the South African Minister of Finance and of Trade and Industry has during March 1993, announced a comprehensive economic restructuring programme. This programme is contained in a document entitled, "A Normative Economic Model", the aim of which is to serve as a discussion document in order to facilitate the formulation of future policies. Amongst others, the Model quantifies the available resources for economic development, identifies the constraints that inhibit more rapid economic growth and also contains an indication of the probable eventual outcome of alternative policy options. The more important aspects which are addressed in the said Model are summarised in a document called "The key issues in the Normative Economic Model". A copy of this document is attached as "Annex A".

Furthermore, the Director-General of the Department of Trade and Industry, for purposes of a conference that was held in Johannesburg during October 1992, formulated certain general guidelines pertaining to particular aspects of economic restructuring and growth. It also pertains to some elements of industrial and trade policy. These guidelines are outlined in a document entitled, "Conference: Blueprint for Prosperity". A copy of this document is also attached, marked "Annex B".

The South African Trade Policy Review should, in the light of what has been stated above, be regarded as a document containing trade policies that are being revised and could change over the medium and longer term.

(2) Objectives of South Africa’s Trade Policy

With its trade policy, the Government of South Africa strives to promote better living standards and quality of life for all South Africa’s inhabitants. In order to achieve this goal the present macro-economic policy, which includes national trade and industrial policy, strongly focuses on increasing the economic growth potential of the country.

For a considerable period of time South Africa’s trade and industrial policy has been characterised by the promotion of import substitution under the umbrella of extensive protective measures. This was mainly effected through the implementation of customs tariffs. This policy has contributed to the development of a high domestic industrial cost structure and the inhibiting of effective international competition. The application of international sanctions compounded the difficulties experienced in regard to this development. Consequently, South African manufactured goods are relatively uncompetitive in world markets. This relative uncompetitiveness, to a large extent, inhibited the development of an export culture amongst South Africans, especially in the manufacturing sector.
Moreover, since the mid-1970's, fewer import substitution opportunities occurred and gold exports diminished. The South African economy was, to a significant extent, unable to compensate for this state of affairs through sufficient industrial exports. The result is a declining trend in economic growth and stagnating industrial development. In order to rectify the situation and to reach the above-mentioned goal, various objectives are pursued.

The main objective is to restructure the South African economy. It is generally accepted that sustained long-term economic growth could mainly be accomplished through increased investment in internationally competitive exporting industries. Thus, to strengthen the supply-side of the economy, Government provides various investment incentives, including, amongst others, a comprehensive technology innovation programme.

A further objective is the fostering and expansion of the competitive environment by preventing the formation of monopolistic cartels and restrictive practices.

A policy based on market-orientated, export-led and investment-driven economic growth implies trade and import liberalization. Accordingly, the reformation of South Africa's industrial protection policy is being attended to and Government is currently considering certain proposals. These proposals include:

(a) a carefully managed, phased reduction of tariffs;
(b) the removal of formula duties and tariff peaks;
(c) a more uniform, simplified and stable tariff structure;
(d) the removal of tariffs on product groups not manufactured in South Africa; and
(e) the lowering of tariffs on raw materials and intermediate goods that are still subject to duties, with a view to lowering cost structures.

The reduction of import tariffs is also under review, especially in view of the requirements of the Uruguay Round.

International financial sanctions against South Africa and the country's commitment to repay its debt in terms of the Interim Debt Agreement which was concluded with foreign creditor banks, forced the South African authorities to implement particular economic measures in order to maintain a surplus on the current account of the balance of payments. This was achieved by:

(a) suppressing domestic demand;
(b) promoting exports; and
(c) maintaining fiscal disciplines.

Apart from the above, fairly stringent monetary and fiscal policy measures aimed at achieving financial stability, have been maintained during the past three years.

Finally, a committee on financial policy and strategy also convenes regularly to ensure that trade, industrial and macro-economic policies are properly co-ordinated. This committee consists of the different Ministers involved in economic policy-making, senior officials of the relevant government departments as well as officials of the South African Reserve Bank.
(3) Description of the Import and Export System

(a) Import system

The South African Tariff Schedule contains approximately 12,500 tariff lines. Import control on about 10,500 of these has already been phased out. Quantitative import control measures thus still apply to roughly 2,000 tariff items, half of which fall within the category of agricultural products. These measures are currently in the process of being phased out and are replaced by tariff measures in those cases where it is appropriate and necessary to do so. As far as the utilization of customs tariffs as an instrument of protection is concerned, this falls within the purview of the Board on Tariffs and Trade.

As regards tariff protection, an arithmetic mean average nominal tariff protection of 22 per cent is afforded to the manufacturing sector in South Africa. This excludes the import surcharge which, on average, is less than 5 per cent. The levying of the import surcharge is controlled by the fiscal authorities and was introduced, primarily, for balance of payments protection.

The above-mentioned average nominal rate of protection of 22 per cent, incorporates estimates of the ad valorem equivalent of formula duties and conceals sharp variations across tariff lines. For instance, in 5 per cent of the South African tariff lines, nominal tariffs exceed 100 per cent. The South African tariff structure could be outlined as follows:

<table>
<thead>
<tr>
<th>South African Tariff Structure</th>
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<tbody>
<tr>
<td><strong>Industry</strong></td>
</tr>
<tr>
<td><strong>Product basis</strong></td>
</tr>
<tr>
<td>I * Capital goods</td>
</tr>
<tr>
<td>* Consumer goods</td>
</tr>
<tr>
<td>* Intermediate goods</td>
</tr>
<tr>
<td><strong>Stages of production basis</strong></td>
</tr>
<tr>
<td>II * Primary products</td>
</tr>
<tr>
<td>* Beneficiated primary products</td>
</tr>
<tr>
<td>* Material-intensive products</td>
</tr>
<tr>
<td>* Manufactured goods (excluding capital goods)</td>
</tr>
<tr>
<td>* Capital goods</td>
</tr>
</tbody>
</table>

Import tariff protection is also utilised to promote industrial development. Consequently, the Board on Tariffs and Trade, BTT, will, on application, consider the imposition of import duties or the increase of existing import duties. In its deliberations in this regard, the Board considers both the need for protection, which need is manifested by the cost-disadvantages which are being experienced by the applicant, as well as the justification for such protection in view of the particular
industry's contribution to the economy. In this regard the Board takes the following factors into account:

(a) strengthening of the balance of payments position;
(b) industrial cost structures;
(c) efficiency in the employment of capital and labour;
(d) growth prospects;
(e) technological dynamism; and
(f) export potential.

In view of Government's declared intention to reduce tariff protection, increases in customs duties are not granted lightly by the Board and where such increases are recommended, these are normally only granted for a limited period of time.

The BTT is furthermore deputed to consider the imposition of anti-dumping, countervailing or safeguard duties. The levying of such duties could be recommended by the Board where evidence of unfair or disruptive competition resulting in material injury to a particular industry is presented to the Board. The duties recommended by the Board may be imposed if such conduct is considered to be in the national interest.

The BTT also regularly considers applications for the reduction of duties and the creation of rebate provisions with a view to the lowering of cost structures and increasing the competitiveness of industries. Tariff adjustments on a regular and an ongoing basis have been identified as a problem and South Africa intends to move to a more stable tariff structure.

Another matter of importance in this respect is the question of rebates of customs and excise duties. Details of such rebates are provided for in Schedules 3 through 6 to the South African Customs and Excise Act of 1964. The following is a brief summary of the contents of these Schedules:

Schedules 1 and 2: General provisions with respect to customs and excise duties.

Schedule 3: Industrial rebates of customs duties:
Part 1: Goods used in the manufacture of other goods.
Part 2: Goods used in the manufacture of other goods for export.

Schedule 4: General rebates of customs duties:
Part 1: Specific rebates of customs duties.
Part 2: Temporary rebates of customs duties.
Part 3: Goods temporarily admitted under rebate of customs duties.

Schedule 5: Specific drawback and refunds of customs duties and fuel levy:
Part 1: Specific drawback of customs duties.
Part 2: Refunds of customs duties on goods exported in the same condition as imported.
Part 3: Miscellaneous refunds of customs duties.
Part 4: Refunds of fuel levy.

Schedule 6: Rebates and refunds of excise duties:
The rebates and refunds, contained in the above-mentioned schedules are applicable to the goods detailed under each rebate item and are administered by the customs and excise authorities. In terms of certain provisions, rebates and refunds could be subject to the issue of a permit by the Director-General: Trade and Industry and could also be subject to a recommendation by the Board on Tariffs and Trade. Important rebate provisions are the following:

Rebate item 470.00 of Part 3 of Schedule 4 of the said Act, provides for a rebate with respect to the duty imposed on goods temporarily admitted for processing, repairing, cleaning, reconditioning or for the manufacturing, processing, finishing, equipping or packing of goods exclusively for export.

Furthermore, Part 1 of Schedule 5 to the Act provides for a refund or drawback of the customs duties on materials used in the manufacturing, processing, finishing, equipping or packing of goods for export purposes. Part 2 of Schedule 5 provides for a refund or drawback of the duty on goods exported in the same condition as the condition in which it was imported.

(b) Export system

The General Export Incentive Scheme, GEIS, is an export promotion system which replaced the old Category A and B schemes with effect from 1 April 1990. The elimination of previous export incentives and the replacement thereof with GEIS is essentially a step towards the consolidation and eventual elimination of export subsidies which are not consistent with the General Agreement on Tariffs and Trade. GEIS was implemented to promote the export of value-added South African products. The benefits under GEIS are determined by the value added to exported goods and is calculated according to the following formula:

\[ Z = U(M+/-E)(P) \]

Where:
- \( Z \) = Tax-free value of export assistance.
- \( U \) = Export value (Free on Board).
- \( M \) = Manufacturing level factor determined by the category of export goods*
- \( E \) = Exchange rate factor based on information furnished by the Reserve Bank which takes into account exchange rate and inflation fluctuations.
- \( P \) = Factor related to the local content of the exported product.

* The manufacturing level factor is determined as follows:

<table>
<thead>
<tr>
<th>Category</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - Raw materials</td>
<td>0</td>
</tr>
<tr>
<td>2 - Beneficiated raw materials</td>
<td>7.5</td>
</tr>
<tr>
<td>3 - Basic manufactured products</td>
<td>12.5</td>
</tr>
<tr>
<td>4 - Other manufactured goods</td>
<td>25.0</td>
</tr>
</tbody>
</table>

South Africa has over many years experienced problems due to a relative high rate of inflation, continued deficits on the current account of the balance of payments and inflationary
financing of capital expenditure. These difficulties became progressively worse as a result of unstable monetary and trading conditions. This situation, inter alia, necessitated the institution of various export incentive measures which were designed to help South Africa's export community to overcome some of the more important drawbacks which they were experiencing in the international markets. The original export assistance measures which became known as the Category A, B, C and D schemes, have now been withdrawn. In their place two new schemes were introduced on 1 April 1990 namely, the above-mentioned General Export Incentive Scheme, GEIS, and the Export Marketing Assistance Scheme, EMA.

As far as an export tax is concerned, an export tax of 15 per cent may be levied in terms of section 62 of the Diamond Act of 1986. This tax applies to the export of rough diamonds, except when such diamonds have been offered to local diamond cutters at market-related prices. 

A so-called price preference scheme is administered by the Department of Trade and Industry in regard to scrap metal. In terms of this scheme, scrap metal produced by scrap dealers should first be offered to downstream domestic manufacturers of metal products i.e. the users of scrap metal, at a discount in relation to the export price. An export permit is only issued to the dealer concerned if such an offer is not taken up by manufacturers. The relevant discount amounts to 15 per cent in the case of non-ferrous scrap metal and 7.5 per cent in the case of ferrous scrap metal.

The administrative process pertaining to import and export licensing falls within the purview of the Department of Trade and Industry.

(4) The Trade Policy Framework

(a) Formulation of trade policy

The legislative arm of the South African Government consists of the State President and Parliament which approves, amongst others, all statutory provisions relating to South Africa's international trade.

South African trade policy is formulated on recommendations received from the Department of Trade and Industry, other public sector bodies such as the Board on Tariffs and Trade and the Industrial Development Corporation of South Africa, as well as from organised commerce and industry. The executive arm of government concerned with trade matters consists of the Ministers and Deputy Ministers of Finance and of Trade and Industry, their Directors-General and Commissioners and their officials.

(b) Application and co-ordination of trade policy

The Department of Trade and Industry is primarily accountable for the application and co-ordination of trade policy. The following Statutes, pertinent to industrial and international trade development, are administered by the Department of Trade and Industry:

(i) Industrial Development Act, 1940, in terms of which the IDC was established;
(ii) Import and Export Control Act, 1963;
(iii) Copyright Act, 1978;
(iv) Sugar Act, 1978;
(v) Patents Act, 1978;
(vi) Companies Act, 1973;
(vii) Board on Tariffs and Trade Act, 1992;
(ix) Merchandise Marks Act, 1941; and
(x) Trade Marks Act, 1963.
(xi) Geneva General Agreement on Tariffs and Trade Act, 1948.

Special mention should be made of the Board on Tariffs and Trade, which was previously known as the Board of Trade and Industry.

The Board of Trade and Industry Act, governing the conduct of the Board, was recently amended with a view to, among other things, defining the functions of the Board more clearly and modifying anti-dumping and countervailing duty procedures. These procedures were previously regulated by the provisions of the Customs and Excise Act of 1964. The Board was, prior to the said amendment to the Act, responsible for all investigations relating to anti-dumping and countervailing duties. Recommendations in this regard were at that stage made to the Minister of Finance.

In terms of the amended Act, the Board is still obliged to conduct the said investigations, but will henceforth make its recommendations to the Minister of Trade and Industry. The Minister has the option of either accepting or rejecting the recommendations of the Board. Should the Minister accept the relevant recommendations, he may then request the Minister of Finance to effect the necessary changes to the tariffs concerned.

Furthermore, the anti-dumping and countervailing provisions have been deleted from the Customs and Excise Act, with the exception of those provisions which regulate the implementation of the various duties provided for in that Act.

The Board on Tariffs and Trade Act of 1992, differs from the previous Act, in that it now defines dumping, subsidised export and disruptive competition. In order to achieve a relatively high measure of certainty in the business community, as to the implications of the new legislation, a guide on the policy and principles of anti-dumping and countervailing duty actions has been prepared, in consultation with the private sector.

As to the responsibility of the Commissioner for Customs and Excise, all matters pertaining to customs and excise are governed by the Customs and Excise Act of 1964. In terms of this Act, the said Commissioner has particular statutory powers, but is in any event, subject to the authority of the Minister of Finance.

Under the Customs and Excise Act, the Minister of Finance is empowered to amend the relevant Schedules to the Act, in order to impose, increase, reduce, withdraw or amend duties, rebates or other taxes. The Minister of Finance, and the Commissioner for Customs and Excise, may also prescribe regulations in connection with matters dealt with in the Customs and Excise Act.

With respect to the above-mentioned powers of the Minister of Finance, an important aspect of the South African legal system is that South African courts have inherent jurisdiction to review the decisions of administrative authorities. This implies that should the Minister of Finance or the Commissioner make regulations which are ultra vires in terms of the provisions of the relevant Act, such regulatory measures may be set aside by a court. In this regard it is also important to note that,
with respect to tariff and value determinations, the Customs and Excise Act also makes provision for appeals to the Supreme Court of South Africa.

(c) Process of trade policy formulation

As has been pointed out the Department of Trade and Industry, the Industrial Development Corporation and the Board on Tariffs and Trade are mainly responsible for recommendations in regard to the formulation of trade-related policies. The more important aspects of these policies are the following:

(i) tariff protection;
(ii) anti-dumping and countervailing action;
(iii) export promotion and investment incentives;
(iv) technology assistance;
(v) import and export control (directly);
(vi) multi- and bilateral trade agreements; and
(vii) industrial development.

On the other hand, the Departments of Finance and of State Expenditure together with the Commissioners for Customs and Excise and for Inland Revenue, are responsible for:

(i) fiscal policy;
(ii) tariff and taxation systems; and
(iii) state spending and budgeting.

The South African Reserve Bank on its part, is, inter alia, responsible for:

(i) exchange rate policy; and
(ii) monetary policy.

All matters relating to government procurement fall within the purview of the State Tender Board.

Apart from what has been set out above, advice regarding import and export control is also rendered by other government departments such as the Departments of Agriculture, National Health and Mineral and Energy Affairs.

(d) Trade Agreements

(i) Multilateral trade agreement

(aa) The Southern African Customs Union (SACU)

The Southern African Customs Union Agreement has been in operation since 1910. The members of this Union are South Africa, Botswana, Lesotho, Namibia and Swaziland.

The said Agreement has not been entered into for a specified period of time, but provides that should a contracting party wish to withdraw from the Agreement, that party shall give notice thereof
to all the other contracting parties. If, after such notice, the contracting parties fail to agree on the date and conditions of the withdrawal, the Agreement shall remain in force for twelve (12) months from the date of such notice and shall then cease to apply with respect to the withdrawing party.

The more important aims of SACU are to maintain the free interchange of goods between the member countries; to ensure the continued economic development of the less advanced members of the said Customs Union; the diversification of the economies of these countries; to apply the same tariffs and trade regulations on goods imported from outside the common customs area; to ensure the continued existence of the Union and to provide all members with the benefits arising out of the trade amongst themselves and with other countries.

A significant aspect of the Agreement is that it provides for the sharing of income derived from customs and excise duties according to an agreed formula.

An important matter as regards the practical functioning of the Customs Union is the fact that South Africa is currently classified as a developed country, but its customs union partners are classified as developing or even least developed countries. All contracting parties apply a common external customs tariff, namely the South African tariff. In terms of the Agreement, South Africa has to consult its customs union partners and has to take their development needs into account when considering and determining amendments to the common customs tariff. The needs of the other partners differ from those of South Africa because of their different stages of development. Customs as well as excise duties are pooled and shared annually amongst the contracting parties in accordance with the above-mentioned formula. The income derived from the common revenue pool represents an important source of state revenue for South Africa’s customs union partners.

The economic factors involved in the relationship between the Republic of South Africa and its customs union partners have to be kept in mind when South Africa’s trade policy is considered.

(ii) Bilateral trade agreements

(aa) Malawi

The bilateral agreement with Malawi, which came into force during 1990, provides for all products grown, produced or manufactured in Malawi, to be imported into South Africa free of customs duties. The importation of coffee, tea and sugar is, however, subject to import control. According to the said agreement, Malawi is obliged to allow all products grown, produced or manufactured in South Africa, to be imported into Malawi, but subject to the payment of the applicable customs duties.

This agreement may be terminated by either party by giving twelve (12) months written notice through diplomatic channels.

(bb) Zimbabwe

This bilateral trade agreement was entered into during 1964 and makes provision for tariff preferences on specific products. Consequently, both South Africa and Zimbabwe enjoy preferential tariff treatment with respect to specific products. Certain tariff preferences that South Africa grants to Zimbabwe are subject to quotas expressed in South African Rand.
This agreement was initially entered into for a period of five years, but after expiry of this period the parties agreed to continue with the agreement for an indefinite period on the same terms and conditions. However, the parties may, in terms of the agreement, give six months written notice of termination thereof.

The aim of the trade agreement with Zimbabwe is, amongst others, to ensure that trade between the two countries is as free and uninterrupted as is practicable.

(cc) Republic of China (Taiwan)

The trade agreement with the Republic of China (Taiwan) was entered into during February 1975. The aim of this agreement is to develop, extend and strengthen the commercial relations between the respective countries.

(dd) Other bilateral trade agreements

South Africa has also concluded bilateral trade agreements with the following countries:
- Hungary (August 1990);
- Romania (August 1990);
- Poland (September 1991); and
- Czechoslovakia (September 1991).

The agreements between South Africa and Hungary, Romania and Czechoslovakia have all been concluded for an initial period of three years. Should the contracting parties at the end of the initial periods wish to continue with these agreements, the agreements shall remain in force indefinitely, but could be terminated at any time by any party, by giving ninety days written notice. The trade agreement between South Africa and Poland, on the other hand, shall remain in force for an indefinite period and may be terminated by giving one hundred and eighty days written notice.

The aim of the above-mentioned trade agreements is to further strengthen the mutual trade relations between South Africa and the countries concerned. The said agreements also provide for the exemption from the import surcharge in South Africa of direct imports that are grown, produced or manufactured in the above countries. This concession was granted in return for their lifting of trade sanctions against South Africa.

(iii) Preferential tariff arrangements

(aa) Mauritius

The preferential tariff arrangement with Mauritius allows for the importation of tea into South Africa exempt from the payment of surcharge. This preferential treatment has been granted for an indefinite period and came into effect in 1992.

(bb) Mozambique

The preferential tariff arrangement with Mozambique, the aim of which is to promote Mozambican exports to South Africa, grants rebate of duties by South Africa on a limited number of products of Mozambican origin. Nonetheless, such tariff preferences are subject to quota limitations.
The list of products agreed upon is currently open-ended, with the result that additional products could be added to the list from time to time. The relevant tariff preferences have been granted by South Africa on a unilateral basis and could be summarily and unilaterally terminated.

(cc) Turkey

The trade arrangement with Turkey, came into operation on 1 January 1988, but is already earmarked for expiration on 31 December 1993. It provides for certain products of Turkish origin to be imported subject to a preferential ceiling duty of 3 per cent and further subject to quota limits in Rand. The list of products included in the arrangement has been changed several times, but the current list will prevail until the agreement expires.

Import permits, based on Rand-denominated quota limits, were initially issued and administered by the South African Department of Trade and Industry. However, on 1 January 1990 this responsibility was transferred to the appropriate Turkish authorities who now issue export permits to Turkish exporters.

(5) The Implementation of Trade Policies

(a) General trade policy measures

South Africa has for many years applied a policy of import replacement. Moderate and selective customs tariff protection was applied in cases of "normal" competition. Formula duties on the other hand, were applied to products imported at prices that were not considered "normal". To obtain the "normal price" with respect to a particular product, the domestic price of South Africa's main trading partners was taken into consideration. These formula duties were indiscriminate in that they were not specifically aimed at any one or group of countries.

In addition, specific sectors are from time to time selected for special investigation and treatment, for example, the motor vehicle industry.

Currently, and in response to the need for South Africa to improve both its growth potential through export promotion and its competitiveness internationally, an active debate is taking place concerning tariff policy. The Industrial Development Corporation was requested in March 1990 to prepare a report on the existing tariff protection policy and to recommend to Government any amendments the Corporation deemed necessary. The Corporation's report was handed to the Government in July 1990 and released for public debate in April 1991, with a view of achieving consensus for moving towards a more market-orientated industrial policy.

The Board on Tariffs and Trade, on its part, has in the meantime indicated its reluctance to continue applying the system of formula duties. In preference, the Board is working towards greater use of transparent anti-dumping and countervailing duties.

Although South Africa has embarked on an economic policy of export-led growth, it is clear that major changes will have to be effected, especially in view of the present round of negotiations of the GATT. Major restructuring of the tariff policy, coupled with a package of economic policy measures aimed at creating export-led industrial development, is needed.
A number of important steps have already been taken in this respect. The import surcharge on capital and intermediate goods has been scaled down, whilst capital goods and exports have been exempted from value-added tax. Other measures include a reduction in the rate of company tax and special rates on electricity, railage and loans from the Industrial Development Corporation.

(i) Investment policy

The South African economic system is based on the principles of a market-driven economy, private entrepreneurship and ownership of the means of production with minimum direct Government intervention. For all practical purposes no distinction is drawn between local and foreign investors as far as legal status and general treatment are concerned. The South African Government has always welcomed, actively promoted and facilitated foreign investment in South Africa, fully realising the important contribution such investment makes in the economic and social development of South Africa.

(ii) The rôle of the Industrial Development Corporation (IDC)

The IDC is a State Corporation, established to provide financing facilities to private entrepreneurs in order to establish and expand economically viable manufacturing industries in South Africa.

The Corporation was established in 1940 and its share capital is held entirely by the South African Government. Although it is not subject to South African company legislation, the IDC adheres to normal private sector company practices as to its operations, administration and reporting. Tax is levied at normal company rates.

The Act in terms of which the IDC was established, The Industrial Development Act, 1940 (Act 22 of 1940), specifically requires that its activities be conducted according to sound business principles. Its directors are appointed from the private sector on the basis of their ability and experience, particularly in the fields of finance, industry and economics.

Applications for financial assistance are considered by the IDC strictly on merit.

The main objectives of the IDC are:

(a) to provide finance to the private sector for the establishment of new industries, and the expansion and/or modernization of existing industries;
(b) to form partnerships with local and foreign suppliers of know-how and capital to develop new industries;
(c) to create employment opportunities and encourage the training and better utilization of labour; and
(d) to promote exports and regional development.

The IDC’s focus is currently directed at:

(a) financing of small to medium-sized independent undertakings that do not have access to the capital market as readily as larger entities;
(b) participation with the private sector in large industrial projects aimed at import replacement and exports, especially where value is added to local raw materials; and
(c) initiating projects which will contribute towards regional development, establish new technologies in South Africa, and create substantial new employment opportunities.

(iii) The Small Business Development Corporation (SBDC)

Since the small and medium-sized enterprise sectors in the more successful economies of the world have proved to be the most important and cost effective job creators in reviving economies, the further development of such sectors is of the utmost importance to South Africa today.

To assist in this development Government has, in conjunction with the private sector, established certain institutions such as the Small Business Development Corporation Ltd (SBDC) with a view of being of assistance to small businessmen. It should, nevertheless, be stressed that the SBDC is an independent public company and is being managed according to sound financial principles.

The mission of the SBDC is to harness the power of entrepreneurship by developing small and medium-sized enterprises and for this purpose it acts in the following four key areas:

(a) the provision of finance in both the formal and informal sectors;
(b) the provision of affordable business premises in selected areas;
(c) development of support services, for example advisory services, information and training for entrepreneurs, as well as marketing support; and
(d) development of promotion services which include community development and various projects promoting the wider interests of the small business community.

(iv) The local content programme for the motor vehicle industry (Phase VI)

The main objective of Phase VI of the local content programme for the said industry, is the reduction of foreign exchange usage by the industry through both import replacement and exportation.

An excise duty of 40 per cent ad valorem is levied on all passenger cars, busses and transport vehicles. This excise duty can be rebated up to 37.5 per cent ad valorem, depending on the local content, to a maximum of 75 per cent of the local content incorporated in a new vehicle. The remaining 2.5 per cent ad valorem excise duty is not rebateable and serves as a fiscal duty. Should a motor vehicle manufacturer participate in the local content programme, components for the manufacture of motor vehicles may be imported with full rebate of the customs duty.

Local content is calculated by subtracting the nett foreign currency usage of the motor vehicles manufactured, from the excise value of the vehicles. Nett foreign currency usage is the value of all imports, i.e. materials and components imported directly by the motor vehicle manufacturers and the imported content of locally manufactured components and materials, less the value of exported components and motor vehicles.

The previous phases (I to V) of the local content programme were based on measuring local content by mass and had the effect of fostering the local manufacturing of low-value, high-mass components. Employment, investment and to a certain extent foreign currency savings, were
promoted by these programmes. Phase VI seeks to promote economies of scale by including exports and also seeks to encourage the manufacturing of high-value, low-mass components. A number of projects have been established since 1989, such as the manufacture of catalytic converters, leather-covered interior trim components, engine management systems and engine plants. A further phase, Phase VII, is currently being investigated.

(v) Development programme for the industry manufacturing television receiving sets

The aim of this programme is to maximise the local content of television receivers which are manufactured in South Africa. The programme makes provision for a full rebate of the duty payable on imported components. In order to provide a favourable environment to a high-tech infant industry, a customs duty of 90 per cent ad valorem was imposed. This duty is being reduced at a rate of 10 per cent ad valorem per annum to a level of 50 per cent ad valorem, pending the outcome of the Uruguay Round negotiations. Should the Round be concluded, the duty will be reduced from the base rate of 60 per cent ad valorem on the implementation date and eventually to 30 per cent ad valorem.

Moreover, the programme makes provision for an ad valorem excise duty of 38 per cent on locally manufactured television receivers. This duty is then partly or wholly rebated depending on the local content achieved by a particular television manufacturer.

As a consequence of these measures, considerable investment flowed to the industry with the resultant creation of employment opportunities. A further result was that various industries, supplying materials and components to the television industry, were established.

(vi) Development programme for the industry manufacturing microwave ovens

This development programme is aimed at increasing the local content of microwave ovens. In the programme each component is allocated a specific percentage according to the value of such a component in relation to the total value of components incorporated in a microwave oven.

This specific programme has three stages of manufacture, with each stage being allocated a local content percentage as a target:

(a) Stage one: 27 per cent local content.
(b) Stage two: 47 per cent local content.
(c) Stage three: 55 per cent local content.

All manufacturers have to comply with these targets. A full rebate of the 30 per cent ad valorem duty is allowed on those parts which are imported in those instances where a target for each stage has been met. Due to the fact that certain components cannot be manufactured economically in South Africa, a permanent rebate provision might be considered after a manufacturer has reached the target for stage three of the programme.

These incentives have led to increased capital investment by the companies concerned and this has also assisted local manufacturers of materials and components in improving the utilization of their facilities.
(vii) Textile and clothing industries

A programme for the textile and clothing industries is in existence, which is aimed at encouraging manufacturers to limit their product ranges and to concentrate on areas of strength. Further aims are to develop the export potential and to increase the level of value added to local materials. In terms of this programme, products can be imported duty free. These duty free imports are based on the exportation of products manufactured from locally produced materials or from imports on which the full duty was paid.

Yarns and fabrics are also imported duty free, based on the level of purchase of locally produced materials. Clothing and textile manufacturers, yarn producers and trading houses who export at least 2.5 per cent of their turnover, qualify for the duty-free importation of products as has been outlined above. This programme is handled by way of a rebate permit system which is administered by the Department of Trade and Industry on the recommendation of the Board on Tariffs and Trade. The programme was introduced in 1989 and terminated in early 1993.

A new scheme, in terms of which exporters of clothing and textiles stand to earn duty credit certificates, has been approved for a period of one year as from 1 April 1993. This scheme is intended to provide a phasing out period of one year for the current programme in order to maintain current export levels until a long-term strategy to improve the competitiveness of the said industries has been devised and implemented. A Task Group is currently in the process of formulating such a long-term strategy for consideration.

(viii) Footwear industry

In order to allow for the restructuring of the footwear industry, by concentrating on areas of relative strength, a tariff of 60 per cent ad valorem was imposed in 1991 on all footwear with uppers of textile and of synthetic materials. This duty will be reduced annually by 5 percentage points until a rate of 30 per cent ad valorem has been reached.

(ix) Mineral beneficiation

The risk-return ratio in regard to mineral beneficiation is currently higher than normal, due to the uncertain political and social situation. This risk factor applies particularly to those industries requiring large capital investments which have to be recovered over the medium to long term. It is mainly due to this situation that South Africa’s fixed capital investment ratio has been declining steadily over the last few years to reach an all time low of 16 per cent of GDP. At this level it is estimated that the number of new machinery employed is extremely small and virtually no restocking of inventories is taking place. The present practice is rather to replace depreciated capital equipment.

In order to ensure adequate economic growth, South Africa’s gross fixed capital investment ratio needs to be increased to approximately 24 per cent of GDP.

Consequently, Government has introduced a tax incentive in September 1991 to be terminated in September 1993, in the form of section 37E of the Income Tax Act, 1962. This incentive provides for the early depreciation of machinery, plant and buildings used in a beneficiation process and the immediate deduction of any pre-production interest on the relevant costs. Depreciation on machinery and plant can be written-off in equal annual instalments over a five-year period, together with an
annual allowance of 5 per cent on the erection of buildings. The said write-off may be initiated from
the date at which the expenditure is incurred rather than the date upon which utilization of the assets
commences. A committee, established in terms of the said section 37E, evaluates all applications
according to particular criteria which, inter alia, includes that:

(a) during the beneficiation process, at least 35 per cent value is added to the value of
all intermediate inputs including that of the base material; and
(b) the beneficiation process be carried out on a scale which makes it internationally
competitive.

An important benefit of this scheme is that companies without a tax base may be issued
negotiable tax credit certificates.

(x) Government procurement

Government promotes local manufacture through a system of price preferences for locally
manufactured products. A general price preference of up to 10 per cent, depending on local content,
applies. However, for electronic equipment the price preference can be up to 20 per cent. This
percentage will be scaled down to 10 per cent as from 1 April 1994. Products bearing the
certification mark of the South African Bureau of Standards are allowed an additional 2.5 per cent
price preference. It is estimated that the South African Government annually and on contract
purchases goods to the value of between R 6,000 and R 8,000 million.

(b) Prospective changes in trade policies

Financial and trade sanctions, which resulted in the debt standstill of 1985, posed grave
problems for the South African economy. South Africa was forced to pursue strict monetary and
fiscal policies in order to maintain large surpluses on the current account of the balance of payments
with a view of financing debt repayments. This affected the growth rate negatively, causing the
creation of employment opportunities to come to a standstill. Since 1985, South Africa experienced
a massive flight of capital, as overseas investors, including large multinational corporations, began
to disinvest on a large scale. However, due to the strict monetary and fiscal policies that were
introduced, South Africa was able to meet its foreign debt repayments. The result was that total
foreign debt declined from US$23.7 billion at the end of August 1985 to $19.4 billion at the end
of 1990.

If South Africa is to successfully change its economic policy from import substitution to
export-led growth and greater liberalization, then it is imperative that entry into existing and new
external markets are ensured. This could be achieved if all participants will be adhering to the
obligations which are being negotiated in the Uruguay Round. To this end South Africa has
submitted its tariff offer in 1990. South Africa also intends to embark on a process of tariff reform.
This process will include, among other things, tariff reductions, over and above its commitments in
terms of the Uruguay Round, and a more uniform, simplified and stable tariff structure. However,
in view of the present severe economic recession and political instability, the tariff reform process
will have to be managed carefully and gradually to avoid sudden disruptions to the economy and cause
further large-scale retrenchments. The pace and extent of tariff reform will also be influenced by the
way in which the economy adapts to the changes as well as to the steps taken to assist industry in
order to increase its competitiveness.
The Department of Trade and Industry is responsible for tariff reform. Together with the Board on Tariffs and Trade and the Industrial Development Corporation, the Department will assist protected industries in adapting to international and national competition. Due regard will be given to limiting the rôle of the State in this process.

It is also intended to design stimulatory measures with a view of bringing about structural adjustment and not to artificially sustain non-viable industries.

Formula and specific duties will be phased out and dumping and subsidised exports will be countered by means of appropriate measures.

Import control still applies to roughly 2,000 tariff items of which 946 are agricultural items. Customs tariffs on paper products were recently revised by the BTT and import controls thereon were abolished in November 1992.

Government is in the process of phasing out import control as far as possible. The list of items still subject to control was published in 1992 for comment from all interested parties. Feedback received will be analysed by the Department of Trade and Industry’s Import Control Committee and the recommendations of this Committee will be submitted to the Deputy Minister of Trade and Industry for approval.

(c) Programmes in existence for trade liberalization

(i) Tariffs

When South Africa changed to the Harmonized Tariff System on 1 January 1988, an undertaking was given to contracting parties of GATT to the effect that tariffs on imported goods would not be increased as a result of the change.

To simplify and streamline the tariff book, various proposals have been made in terms of which the rates of duty would be equalised. In this process the creation of additional national subheadings would be obviated and existing subheadings reduced. An example hereof is heading No. 85.44, which previously consisted of 106 national subheadings, but now comprise of only four. The tariff structure of chapter 48 relating to paper has also been simplified together with the withdrawal of import control.

(ii) Customs valuation

The authority to implement the Agreement on Implementation of Article VII of the GATT, is embodied in Chapter IX (i.e. sections 65, 66 & 67) of the Customs and Excise Act, 1964 (Act 91 of 1964). In terms of section 74A of the said Act the interpretation of these sections of the Act is subject to the above-mentioned Agreement. Such interpretation is further subject to the Interpretative Notes, Advisory Opinions, Commentaries, Explanatory Notes, Case Studies and other Studies of the Customs Co-operation Council, of which South Africa is a member.
(iii) Rules of origin

South Africa's rules of origin are contained in section 46(1) of the Customs and Excise Act, which reads as follows:

"(1) For the purposes of this Act (excluding Chapters VI and IX), goods shall not be regarded as having been produced or manufactured in any particular territory unless -

(a) at least twenty-five per cent (or such other percentage as may be determined under subsection (2), (3) or (4) of the production cost of those goods, determined in accordance with the regulations, is represented by materials produced and labour performed in that territory;

(b) the last process in the production or manufacture of those goods has taken place in that territory; and

(c) such other processes as the Minister may, on recommendation of the Board of Trade and Industry*, by regulation prescribe in respect of any class or kind of goods, have taken place in the production or manufacture of goods of such class or kind in that territory."

* Now called the Board on Tariffs and Trade.

(iv) Anti-dumping and countervailing actions

Until 5 May 1992, the anti-dumping and countervailing duty legislation was embodied in the Customs and Excise Act, 1964. As from 6 May 1992, this legislation was incorporated in the Board on Tariffs and Trade Act, 1992. Only the enabling provisions, i.e. the authority for the Commissioner for Customs and Excise to collect anti-dumping and countervailing duties, were retained in the Customs and Excise Act.

The Minister of Finance imposes or amends the relevant duties in accordance with a request by the Minister of Trade and Industry who, on his part, acts on a recommendation by the Board on Tariffs and Trade in this regard.

(v) Privatization and deregulation

(aa) Deregulation

The background to South Africa's deregulation policy may be found in the 1985 report of the President's Council's Committee for Economic Affairs on A Strategy for the Development of Small Business and Deregulation. General guidelines on both deregulation and privatization are contained in the White Paper on Privatization and Deregulation which was published in 1987.

The White Paper, inter alia, states that regulating institutions should continuously ensure that the measures which they contemplate would have the effect of minimally restricting the healthy development of the economy. According to the White Paper, the following factors must be considered in respect of all new regulatory measures:
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The necessity of regulation;
the cost and convenience of complying with the regulations;
the appropriateness of the standards; and
the flexibility with which the measures can be applied in a differentiated economy.

The Competition Board has been instructed by Government to co-ordinate official deregulation policy and has the authority to conduct investigations as to possible deregulatory actions. Examples of the latter are the "Guidelines for the regulation of professional services" and the "Deregulation of the market for health services". In the application of general guidelines contained in the White Paper, the Competition Board attaches considerable importance to the promotion of competition.

Deregulation policy operates separately from the Government’s privatization policy.

(bb) Privatization

In an effort to decrease State involvement in the supply of products and services, the Government has embarked on a policy of privatization of State-owned enterprises. The principles in this regard have also been enunciated in the White Paper referred to above.

Commercialization or corporatization, is in many an instance employed as a forerunner to privatization. The reasons for this two-step privatization process include the placing of the to-be-privatised entity on a commercial footing with the view to establishing a "track record" for investors.

The commercialization/privatization process also most often has to be preceded by deregulation. The latter is often necessary to allow private companies entry into a previously regulated market and to provide for a soon-to-be privatised entity to operate in that market. In many instances the prospective privatised entities have their own Acts of Parliament which have to be abolished. It is also often necessary to "level" the so-called "playing fields" to ensure that the privatised entity does not enjoy advantages which are not available to other private sector participants.

(vi) Free trade zones, including in-bond manufacturing

No free trade zones exist at present in South Africa and South African legislation does not currently provide for in-bond manufacturing facilities in the generally accepted sense of the term. Provision is, however, made in the Third Schedule of the Customs and Excise Act for the importation of certain goods required for the production of certain manufactured goods by certain industries with rebate of duty to a specified extent. Furthermore, provision is made in Schedules 4 and 5 to the Act for the duty-free importation of goods required for the manufacturing, processing, finishing, equipping or packaging of goods exclusively for export. A permit, issued by the Department of Trade and Industry on recommendation of the Board on Tariffs and Trade is, however, required.

A study as to the feasibility and advisability of making provision for export processing zones has been completed and recommendations are being prepared for consideration by the South African Cabinet.
B. BACKGROUND INFORMATION PERTAINING TO THE ASSESSMENT OF TRADE POLICIES

(1) Wider Economic and Developmental Needs, Policies and Objectives

(a) General

According to the Economic Advisory Council of the State President, the implementation of a purposeful and coherent economic and socio-economic strategy is essential for formulating clear and valid policy guidelines to achieve the following complementary objectives:

(i) an increase in the long-term economic growth rate and the employment creating capacity of the economy;
(ii) a reduction in the inflation rate to a level comparable with that of our major trading partners; and
(iii) improving the standards of living of the poorest sections of the population through policies aimed at creating employment and addressing their basic needs.

The following factors would assist South Africa in improving its economic conditions:

(i) a return to steady growth rates worldwide;
(ii) inward foreign investment due to improved perceptions of South Africa’s future;
(iii) foreign development funding combined with increased domestic development expenditure;
(iv) freer access to foreign capital markets;
(v) access to IMF and World Bank loans;
(vi) lower corporate and individual tax rates;
(vii) lower inflation rate comparable to South Africa’s major trading partners;
(viii) fiscal prudence and accountability; and
(ix) strict monetary policy.

(b) Broad policy issues

To achieve higher economic growth, to create employment and to improve the standards and quality of life of the poor, the implementation of the following broad policy issues would be required:

(i) More effective use of scarce production resources

To improve productivity of all the factors of production is probably the single most important element which will contribute to higher economic growth. The following measures are required in order to improve the said productivity:

(a) increasing the supply of skilled labour and entrepreneurial talent considering the economic needs of the country;
(b) promoting vocational education over pure academic qualification;
(c) promoting affordable, but quality education for all;
(d) training, aimed at improving productivity;
(e) de-politicising the labour market;
(f) maintaining a positive real interest rate;
(g) maintaining strict monetary policy guidelines;
(h) removing distortive tax legislation;
(i) reducing government consumption expenditure;
(j) reducing public sector employment levels;
(k) deregulating control boards and certain State corporations;
(l) privatization and commercialization of State enterprises;
(m) encouraging private sector saving to create capital; and
(n) creating a favourable climate for investment.

(ii) Export promotion

Future economic growth in South Africa will be heavily dependent on the export of manufactured value-added products. Potential competitive advantages, therefore, have to be identified, developed and exploited to the fullest. Although the improvement of productivity and the application of cost-effective technology will enhance South Africa’s competitiveness and stimulate exports, attention should also be focused on the promotion of local beneficiation and processing, with the objective of exporting more value-added commodities. The maintenance of existing foreign trade relations in the Southern African context should also be borne in mind in this context. The collective export potential of the member countries of the Customs Union Agreement (Botswana, Lesotho, Namibia and Swaziland) should be exploited more effectively.

(iii) Industrial protection

South Africa’s current tariff protection policy requires fundamental reform. This requires that:

(a) excessively high import tariffs be lowered in a differentiated and non-disruptive manner in order to increase international competition, to lower inflation as well as inflationary expectations;
(b) import tariffs should not be permanent and should be revised; and
(c) the tariff structure arrived at must be simplified, stable and uniform involving less manpower to administer.

(iv) Urbanization policy

The main objective of the urbanization policy is to foster industrial development in those areas with comparative advantages via urban infrastructure, including housing and services. Further aims are to absorb people into the modern sector and to improve the socio-economic condition of the poorer section of the population.

(v) Rural development policy

More than 40 per cent of the total population is living in rural areas which are still underdeveloped and lacking in economic infrastructure. Unemployment in these areas is therefore high. Rural development forms part of the Government’s regional development strategy, which concentrates on both the expansion and economic development of existing sectors such as agriculture,
forestry, services and small business, as well as on the development of new opportunities through industrialization.

(2) **The External Economic Environment**

(a) **Major trends in imports and exports**

(i) Introduction

South Africa has a particularly open economy, where the level of exports determines the propensity to import, which on its part, has a direct bearing on economic growth. South Africa, a mixture of first world sophistication in several fields and third world standards in others, is susceptible to foreign economic and political developments. Traditionally an exporter of base raw materials and commodities to developed countries, and importing in return sophisticated manufactured products and capital equipment, South Africa is aware of the need to add value to its raw materials and to expand its manufacturing industry, geared towards world markets. A closer look at imports and exports over the last decade will reveal that this change is indeed taking place.

(ii) Exports

(aa) Agriculture

During the past ten years this sector contributed an average of 4 per cent of total exports, with a high of 6 per cent in 1982 and a low of 3 per cent in 1984, 1985 and 1988. Due to the volatile nature of South Africa’s weather patterns, alternating between severe droughts and destructive floods, high input costs and a deterioration in the terms of trade, it seems unlikely that agricultural exports could rise meaningfully.

During the same period, agricultural exports increased by R 341 million, or by 12.4 per cent to R 3,096 million. This increase is most gratifying when the devastating effects of the drought during 1992 are taken into consideration. Maize, wheat, sugar cane and sorghum crops were practically wiped out and the export performance was left to the country’s fruit growers. Agricultural exports, as a percentage of total exports increased from 4.28 per cent in 1991 to 4.58 per cent in 1992.

(bb) Mineral products

During the past ten years, this sector averaged 11 per cent of total exports, showing a high of 14 per cent in 1985, an increase of R 1.9 billion over 1984 and a low of 9 per cent in 1987. However, in 1987 exports amounted to R 3.9 billion, rising 32 per cent to R 5.1 billion in 1988, and further to R 7.8 billion in 1991. There has thus been a clear increase since 1987.

The upward trend in mineral product exports continued during 1992. Exports increased by R 278 million or 3.8 per cent to R 7,559 million. This was the sixth consecutive year in which exports of this sector have increased. The ratio to total exports remained at 11.2 per cent in 1992.
Although this sector averaged 2.6 per cent of total exports during the past ten years, it has shown meaningful increases, value wise, over the last five years. In 1987 exports totalled R 1.2 billion. In 1988 it increased by 36 per cent, or by R 409 million, in 1989 by a further R 415 million, or by 27 per cent and in 1991 by R 408 million to R 2.3 billion, or by 21 per cent. Chemical exports are set to continue rising as various large corporations, notably SASOL, Sentrachem, ENGEN and AECI continue to exploit this market.

Exports of chemical products continued to increase at a high rate during 1992. It totalled R 3,287 million, an increase of R 986 million or 43 per cent, in comparison with 1991. The high level of fixed capital investment in this industry will continue to ensure that annual growth in exports remains buoyant. As a percentage of total exports, chemical exports increased from 3.58 per cent in 1991 to 4.88 per cent in 1992.

This sector averaged 9 per cent of total exports over the last ten years with a high of 14 per cent in 1983 and a low of 7 per cent in 1985 and 1986 respectively. This indicates the volatility of this market and how vulnerable it is to international consumption trends. However, from a low of just over R 3 billion in 1986, exports more than doubled to R 6.8 billion during 1991, an increase of 123 per cent in five years or, on average, by 25 per cent per annum.

Exports of this industry increased by R 790 million to R 7,571 million in 1992, or by 11.7 per cent over 1991. It constituted 11.22 per cent of total exports, up from 10.53 per cent in 1991. The figure includes gems transferred by De Beers from its mines in Botswana and Namibia to the CSO in London. Although a volatile market due to the sensitivity to worldwide economic growth rates, this industry should show improved performance as the G7 countries, notably the USA, emerge from the current recession.

Although manufactured products as a percentage of total exports, averaged only 3.3 per cent over the last ten years, its share has been growing steadily. In 1988 it was 3 per cent growing to 5.6 per cent by 1991. Exports of machinery and mechanical appliances doubled from R 884 million in 1988 to R 1.6 billion in 1991, whilst exports of vehicles, aircraft, ships and parts thereof increased from R 456 million in 1988 to R 1.5 billion in 1991. This rising trend indicates that the South African industry is moving towards increased exports of beneficiated materials and manufactured goods. This change is both necessary and vital to ensure that export-led growth is not dependent on volatile and inconsistent international commodity prices which have caused South Africa’s economy either to boom or bust, but on the consistent and rising prices of manufactured goods and articles.

This sector of the economy continued to perform well in 1992 - exports rose by R 1,371 million, or by 38 per cent, to R 4,975 million from R 3,604 million in 1991. As a percentage of total exports it increased from 5.6 per cent in 1991 to 7.4 per cent in 1992. Exports of vehicles and vehicle components and accessories increased by R 836 million or by 55 per cent,
compared to 1991, whilst machinery and mechanical appliances, electrical appliances, and parts thereof, increased by R 456 million or 27 per cent over 1991.

The GEIS incentive scheme, phase VI of the local content programme and falling domestic demand in South Africa over the last three years, have all combined to help many businesses turn to export markets to survive or to expand. An export-orientated approach to business is being cultivated in South Africa which will ensure that manufactured products remain at the forefront of South Africa's structural economic changes.

(ff) Base metals and articles thereof

These exports averaged 12 per cent of total exports over the past decade, with a high at 15.5 per cent in 1989 and a low of 8.5 per cent in 1984. Although dependent on international economic trends and commodity prices, their share of total exports has increased since 1984. In that year it totalled R 2.1 billion, rising to R 9.6 billion in 1991. This gives an average growth of 43 per cent per annum over the last eight years.

Declining commodity prices worldwide due to the prolonged recession combined to depress export levels of base metals and articles thereof. Exports fell by R 135 million, or by 1.4 per cent to R 9,399 million in 1992 from 1991.

(iii) Imports

(aa) Agriculture

During the last ten years imports of agricultural products averaged 3.6 per cent of total imports with a low of 2 per cent in 1982 and a high of 6 per cent in 1984. Agricultural imports are seasonal and dependent on South African weather conditions.

The devastating drought of 1991/1992 cost South Africa R 1,775 million more in agricultural imports as they surged to R 3,457 million in 1992 from R 1,682 million in 1991. The percentage increase over 1991 was 106 per cent, and as a ratio to total imports jumped from 3.5 per cent in 1991 to 6.6 per cent in 1992. Imports of vegetable produce, (maize, wheat, etc) increased by R 1,411 million to R 2,553 million, while meat imports rose by R 127 million to R 229 million.

(bb) Chemical products

The average of chemical imports as a percentage of total imports was 10 per cent over the last decade, with a low of 7 per cent in 1982 and a high of 11.3 per cent in 1986. Since 1986 imports have grown steadily from R 3 billion to R 5.4 billion - an average annual growth of 13 per cent.

The average rate of increase in chemical imports continued at 6.8 per cent in 1992, rising to R 5,766 million, or by R369 million. The ratio of chemical product imports to total imports, remained constant at 11.2 per cent.
(cc) Manufactured products

These imports averaged 47 per cent of total imports during the last ten years. A low of 43 per cent was recorded in 1986 with a high of 51 per cent in 1988. Imports of machinery, mechanical appliances, and electrical machinery grew by an average annual rate of 15.2 per cent from R 7.3 billion in 1986 to R 14 billion in 1991. Imports of vehicles, aircraft and parts thereof grew at an average annual rate of 21.6 per cent from R 2.9 billion in 1986 to R 6.8 billion in 1991. This underscores South Africa's dependence on these imports to keep pace with international technological innovations.

Imports of these products during 1992 remained at 47 per cent of total imports, which is the average ratio since 1982. Imports of machinery and mechanical appliances, and electrical equipment, increased by R 983.4 million to R 14,966 million, or by 7 per cent. The import of vehicles, aircraft and associated transport equipment declined by R 261 million to R 6,505 million, or by 3.9 per cent. This underscores the severity of the recession in South Africa, particularly with regard to luxury durables such as motor vehicles.

(b) Developments in the terms of trade and commodity prices

Before analysing actual terms of trade figures as calculated by the South African Reserve Bank for the past 12 years, it would be useful to briefly consider how South Africa's imports and exports of goods developed over the last decade and what the trend is as to the trade balance.

South Africa's Trade Balance

<table>
<thead>
<tr>
<th>Year</th>
<th>Exports (R m.)</th>
<th>Imports (R m.)</th>
<th>Trade Balance (R m.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1982</td>
<td>19,239</td>
<td>18,433</td>
<td>806</td>
</tr>
<tr>
<td>1983</td>
<td>20,672</td>
<td>16,253</td>
<td>4,419</td>
</tr>
<tr>
<td>1984</td>
<td>25,109</td>
<td>21,689</td>
<td>3,420</td>
</tr>
<tr>
<td>1985</td>
<td>36,410</td>
<td>22,732</td>
<td>13,678</td>
</tr>
<tr>
<td>1986</td>
<td>42,171</td>
<td>26,892</td>
<td>15,279</td>
</tr>
<tr>
<td>1987</td>
<td>42,717</td>
<td>28,736</td>
<td>13,981</td>
</tr>
<tr>
<td>1988</td>
<td>49,724</td>
<td>39,484</td>
<td>10,240</td>
</tr>
<tr>
<td>1989</td>
<td>58,728</td>
<td>44,742</td>
<td>13,986</td>
</tr>
<tr>
<td>1990</td>
<td>60,929</td>
<td>44,125</td>
<td>16,804</td>
</tr>
<tr>
<td>1991</td>
<td>64,355</td>
<td>48,209</td>
<td>16,146</td>
</tr>
<tr>
<td>1992</td>
<td>67,457</td>
<td>51,917</td>
<td>15,540</td>
</tr>
</tbody>
</table>

It should be noted how South Africa's exports and imports reacted to the debt standstill in 1985. When the Government announced the standstill, due to adverse domestic political and economic circumstances, the effective exchange rate of the Rand, against a basket of currencies, depreciated sharply, especially against the U.S. dollar, deutsch mark, Japanese yen, British pound and
Italian lira. Thus, the Rand value of South Africa’s exports increased to R 36.4 billion in 1985, from R 25.1 billion in 1984, a 45 per cent increase. Conversely, import growth tapered off and only rose by 4.8 per cent as imports became much more expensive. However, the jump in the trade surplus from R 3.4 billion in 1984 to R 13.7 billion in 1985 was necessary for South Africa to meet its commitments negotiated in terms of the debt standstill. Since then, South Africa has maintained a substantial trade surplus, having had to forego economic growth in order to meet debt repayments. The trade surplus peaked in 1990 at almost R 17 billion, but has declined since then to R 15.5 billion in 1992.

The table above reveals how South Africa’s terms of trade declined during the eighties and early nineties. Note the effect of net gold exports on the terms of trade, indicating how South Africa’s economic fortunes have fluctuated with global demand for gold. Note, too, the precipitous depreciation of the Rand against a basket of currencies from 1984 to 1986. This corresponds with the sharp increase in the rand value of South Africa’s exports from 1984 to 1986, and the modest increases in the annual import bill during the same period.

The negative trend in the terms of trade during the period mentioned, is the result of a worsening of commodity prices as South Africa had to export greater volumes in order to import the same volume. South Africa had two major economic obstacles to deal with. Firstly, the declining terms of trade which led to a worsening of the current account of the balance of payments, and secondly, faced with the interim debt agreement, South Africa had to maintain a healthy trade surplus to meet the debt repayments. This situation, combined with strict monetary and fiscal policies, effectively ruled out economic growth. To compound the situation, South Africa faced severe trade
and financial sanctions during this period. These sanctions forced many South African exporters to lose traditional export markets, further damaging South Africa's terms of trade.

(c) **Important trends in the national accounts**

(i) **Balance of payments**

For eight consecutive years a surplus on the current account of the balance of payments was reported in the period up to 1992. During the past four years the surplus on the current account varied from R 3.1 billion in 1989, to R 5.8 billion in 1990, to R 7.4 billion in 1991 and to R 4.3 billion in 1992. The cumulative surplus during the past eight years added up to R 40.5 billion.

The maintenance of these surpluses was essential in view of the constraints imposed by financial and other sanctions. However, this occurred at a cost to the country in that economic growth was restricted. The low level of real economic activity dampened real gross domestic fixed investment and inventory accumulation, both of which have a relatively high import content. The import penetration ratio i.e. real merchandise imports as a percentage of real gross domestic expenditure, therefore fluctuated between 19.7 per cent and 24.6 per cent in the last eight years, compared with levels of more than 30 per cent in the early 1970s.

However, the share of capital goods imports to total merchandise imports remained relatively high. This ratio rose from 40 per cent in 1987 to more than 44 per cent in 1988, declining to 42 per cent in 1991. On the other hand, the share of intermediate goods to total merchandise imports declined sharply from 48 per cent in 1980 and 45 per cent in 1985 to only 37 per cent in 1991. This decline was largely due to South Africa's decreasing dependence on imported crude oil after completion of the new Sasol plant. Imports of consumer products to total merchandise imports fluctuated around 17 per cent reflecting changes in consumer demand.

The main driving force behind South Africa's exceptional current account performance since the beginning of 1985 has been a substantial growth in merchandise exports. From 1984 to 1992 the value of merchandise exports continued to advance strongly at an average annual rate of 20 per cent. Even more significantly, the volume of merchandise exports rose by 8.9 per cent per year over the same period, and the export of manufactured goods as a percentage of total exports rose from 14.4 per cent in 1987 to 22.4 per cent in 1992.

This export growth was achieved despite the introduction of sanctions and trade embargoes on South Africa by a number of countries on several categories of export products, and can largely be attributed to the following:

(a) a sharp decline in the real effective exchange rate of the rand, particularly during 1984, 1985 and 1988. In 1992 the average index value of the real effective exchange rate was still 18.5 per cent lower than the index value of 1983;

(b) relatively high growth in the volume of world trade; and

(c) the relatively low level of domestic economic activity and excess production capacity which encouraged domestic producers to find other outlets for their products.

Net service and transfer payments to non-residents declined over the last five years from 6.5 per cent of GDP in 1986 to 3.3 per cent of GDP in 1992. Repayment of South Africa's foreign
debts is reflected in lower annual interest payments to foreigners - the interest payments to total export earnings ratio declined accordingly from 10.8 per cent in 1985 to 4.1 per cent in 1992.

In contrast to these positive contributions to the balance of the current account, net gold exports performed relatively poorly. South Africa’s total gold production declined from 680 tons in 1984 to 599 tons in 1991 (1992 - 611 tons). This substantial contraction in production was mainly due to a decline in the grade of ore milled. In addition, the price of gold has only increased slightly since 1984. The average annual gold price rose sharply from US$360 per fine ounce in 1984 to $447 in 1987, but then declined again to $362 and $344 in 1991 and 1992 respectively.

At first, the improvement in the current account was accompanied by a moderate increase in the terms of trade at an average annual rate of 1 per cent between 1984 and 1988. However, international commodity prices declined sharply since 1988, and South Africa’s terms of trade deteriorated over the next four years. The average annual rate of decline amounted to 3.8 per cent.

Despite the further repayments on South African foreign debt, the net outflow of capital from the country decreased from R 6.2 billion in 1988 to R 4.2 billion in 1989, R 2.9 billion in 1990 and to R 1.4 billion in the first three quarters of 1991. This improvement in the capital account of the balance of payments prompted the South African Reserve Bank to cease quoting preferential rates on forward exchange contracts on 16 September 1991. These special rates were introduced in 1988 to encourage foreign trade financing. This move among other things, contributed to an outflow totalling R 4.7 billion in the last quarter of 1991 - bringing the total to R 6.1 billion for the year.

Underpinned by a substantial increase in public and private placements on international capital markets, a negligible small total net outflow of capital was recorded in the first quarter of 1992. Subsequent political developments and a strengthening U.S. dollar had a large negative impact on capital flows and led to a total net outflow of capital, not related to reserves, of R 6.5 billion in 1992.

The improvement in the capital account was due to a lower outflow of short-term capital not related to reserves; R 3.1 billion in 1989, R 0.9 billion in 1990 and an inflow of R 0.9 billion during the first nine months of 1991. Due to exceptional circumstances short-term capital of R 4.2 billion left the country in the fourth quarter of 1991; thus the net outflow for 1991 was R 3.3 billion. Political developments, the relatively favourable cost of domestic trade financing and the appreciation of the US dollar in international markets led to outflow of short-term capital of R 5.0 billion in 1992.

Long-term capital outflows remained fairly high during the past four years and rose from R 1.2 billion in 1989 to R 2.7 billion in 1991. In 1992 the outflow of long-term capital amounted to R 1.5 billion.

(ii) Foreign reserves

Despite the continued net outflow of capital, South Africa’s total net gold and other foreign reserves increased by R 2.9 billion in 1990 and by R 1.4 billion in 1991. The deterioration in the overall balance of payments position in 1992 however, caused the country’s net foreign reserves to decline by R 2.3 billion.

The total gross gold and other foreign reserves increased by R 0.4 billion in 1990, by R 2.5 billion in 1991, and by R 1.4 billion in 1992. The reserves at the end of December 1992
totalled R 11.2 billion, representing two months worth of imports of goods and services. This improvement, together with the unused credit facilities available to the Reserve Bank, represents a much healthier picture of South Africa’s reserves.

(iii) Exchange rates

The effective exchange rate of the Rand increased by 6.5 per cent from 18 September 1989 to 5 January 1990, after which it depreciated by 7 per cent during the rest of 1990. During 1991 and 1992 it depreciated further by 6.5 per cent and 4.2 per cent respectively. The decline of the nominal effective exchange rate of the Rand during 1992 was not sufficient to counter the inflation differential between South Africa and its main trading partners. The real effective exchange rate of the Rand during December 1992 was therefore, 0.3 per cent above its December 1991 level. The Financial Rand started to appreciate sharply from the end of 1990 and its discount to the Commercial Rand reached a record low of 7 per cent on 19 November 1991. It then began to depreciate again to reach a low of R 5.08 per dollar on 25 November 1992 and a discount of almost 41 per cent. At the end of March 1993 the Financial Rand was trading at the higher level of R 4.54 and a lower discount of 30 per cent.

(iv) Interest rates

The softening of most money market rates, which had started as early as February 1990, continued throughout 1991 and 1992. This was clearly reflected in the rate for three-month liquid bankers’ acceptances, which decreased from an average value of 18.57 per cent in January 1990 to 12.22 per cent in December 1992. This rate declined further to 12.15 per cent on 31 March 1993.

(v) Foreign debt

According to the latest available information, South Africa’s foreign debt was reduced from $23.7 billion in 1985 to $18.1 billion at the end of 1991. In Rand terms the debt decreased from R 65.8 billion to R 49.7 billion, despite the devaluation of the currency over the same period. Valued at constant US dollars at the dollar’s exchange rates against other currencies as on 31 August 1985, the total outstanding debt amounted to $15.6 billion on 31 December 1991, implying that $8.1 billion, or about a third of the outstanding debt has been redeemed.

Debt not payable in terms of the interim debt arrangement with foreign creditor banks also declined over this period, from $13.6 billion on 31 August 1985 to $6.0 billion at the end of 1991. The total debt outside the standstill net, however, increased from $10.1 billion to $12.1 billion over the same period.

The maturity structure of the debt has also improved substantially as loans have been re-negotiated. In August 1985, 57 per cent of the debt was within the standstill net; by the end of 1990 only 25 per cent was within the net.

As a result, South Africa’s debt ratios improved considerably over the past six years: foreign debt as a ratio to gross domestic product declined from 43 per cent at the end of August 1985 to 17 per cent at the end of 1991; foreign debt as a percentage of export proceeds declined from 128 per cent to 65 per cent over the same period.
(d) **International macro-economic situation affecting South Africa's external trade**

The global downturn has definitely affected an already weak economy. The lower economic growth rates in most industrialised countries resulted in weaker demand for primary commodities with lower prices following. The South African industries directly affected by these factors are the mining and beneficiated mineral exporters including, inter alia, the gold, coal, aluminium, copper, diamond, ferrochrome and steel producers.

(3) **Problems in External Markets**

South Africa's investment and competitive abilities are seriously hampered by the selective trade distortive measures of certain countries. Examples are the following:

(a) **UK cotton quota**

The United Kingdom selectively restricts South African cotton exports to an annual quota of 1,012,000 square metres. This figure remained constant since the beginning of 1984.

Only woven cotton goods that consist of 50 per cent or more by weight of cotton are included in the quota, which means that knitted cotton materials and garments are excluded. The annual quota of 1,012,000 square metres is apportioned in a 60:40 ratio between textiles on the one hand and clothing or other made-up articles on the other. The Department of Trade and Industry is responsible for the administration of this quota.

In view of the fact that there has been no increase in the quota since 1984, exporters receive their share of the quota at the beginning of each year, based on their past exports. New exporters only receive allocations where existing exporters do not utilise their allocations. A half-yearly review takes place to admit new exporters, whenever possible.

(b) **Canadian clothing and textile quota**

In December 1987 Canada alleged that South African textile and clothing exports were causing injury to Canada's textile and clothing industry. Consequently, on 1 January 1988 certain quotas were imposed.

South Africa then requested GATT Article XXII:I consultations with Canada. Canada defended her action as being in accordance with the provisions of the Multi Fibre Arrangement (MFA), and would not comment on the legality of its conduct in terms of the General Agreement. South Africa, however, reasoned that the Canadian action impaired its rights and was contrary to Canada's GATT obligations and that its reliance on the MFA, after the imposition of the quota, was not relevant to the case, as South Africa was not a signatory to the MFA.

The result of these discussions was that an annual quota for three years of 1,100,000 units was established, with the following sub-limitations:

(i) on trousers, shorts, overalls and coveralls, a quota of 230,020 units;
(ii) on blouses, shirts, other t-shirts and sweatshirts, a quota of 103,880 units;
(iii) on tailored collar shirts, a quota of 393,260 units; and
(iv) on other apparel, a quota of 372,840 units.

The quotas on the above products are subject to a 6 per cent increase per annum.

For worsted fabrics an annual quota of 80,000 kg was agreed upon, with an annual increase of 3 per cent.

The original Memorandum of Understanding between South Africa and Canada has been extended for a one year period till the end of 1993.

(c) EC apple quota

South Africa is the largest exporter of dessert apples to the EC and is part of a group of fruit exporting countries referred to as the "Southern Hemisphere supplying countries". The other major suppliers of dessert apples to the EC are, in order of volume, Chile, New Zealand, Argentina and Australia. South Africa, together with the other four countries mentioned, account for more than 95 per cent of all exports of dessert apples to the EC.

South Africa has a long tradition of disciplined apple exporting to the EC. In fact, in the past whenever the EC called for lower apple exports due to a better than normal European harvest, South Africa always complied by imposing a voluntary restraint, thereby preventing disruption of the EC market. Even at times when an annual quota system was implemented by the EC to prevent market disruption, South Africa strictly adhered to its quota.

However, the aforementioned disciplined action by South Africa over many years has resulted in the erosion of the country's market share as South Africa's allowed increase in the export of apples has been very modest in comparison with that of other apple exporting countries.

(d) The Republic of China (Taiwan) - ROC citrus and apple quota

(i) Apple quota

The ROC has granted South Africa a token quota of 100 tons per annum for apple exports. This is negligible when compared to quotas granted to other countries. South Africa's apple season is complementary to the ROC's and South Africa has repeatedly expressed its dissatisfaction with what it regards as blatant trade discrimination.

(ii) Citrus quota

Similarly, South Africa was granted a 100 ton citrus quota per annum by the ROC. This quota has recently been increased to 1,000 tons.

(e) USA State, county and city sanctions

Although the Comprehensive Anti-Apartheid Act of 1986, was lifted by President Bush in July 1991, an extensive network of state and city sanctions remains. In fact, several states and cities adopted their own sanctions legislation during 1992. These sanctions cover, amongst others, the following aspects:
(i) disinvestment;
(ii) partial disinvestment;
(iii) ban on new investment; and
(iv) selective contracting.

Selective contracting prohibits firms with South African connections from bidding for particular projects. An example is the so-called Shell-free zone by which trading between foreign enterprises and the Shell Oil Company or its subsidiaries, is prohibited because of Shell’s involvement in South Africa. Another example of selective contracting is the ban which prohibits the purchase of South African goods.

No tenders for public procurement are considered in certain states, cities or counties, in the event of the tendering firm having any ties with South Africa or with a South African firm.

These sanctions, maintained by certain sub-national entities of a federal state, seriously affect the competitiveness of South African exports and they are undue barriers to trade.

II. AGRICULTURAL TRADE POLICY

A. THE SOUTH AFRICAN AGRICULTURAL SECTOR IN PERSPECTIVE

Agriculture in South Africa has two distinct sectors: a well-developed commercial sector and a subsistence-orientated one. Approximately 12 per cent of South Africa’s surface area is utilised for the growing of crops.

On the basis of climate, natural vegetation, types of soil and the type of farming practised, the country could be subdivided into a number of farming regions. Agricultural activities in these regions range from intensive crop production, mixed farming in winter rainfall and in high summer rainfall areas, to extensive beef ranching in the bushveld, and sheep farming in the arid areas. By world standards, natural resources for agriculture are generally poor. Due to unreliable rainfall patterns, the country as a whole is subject to severe recurrent droughts, which are sometimes broken by devastating floods.

In monetary terms, agriculture’s share in the economy has long since been outstripped by mining and secondary industry. In 1960, agriculture contributed 12.5 per cent to the gross domestic product, as against 20 per cent in the 1930s. Currently it accounts for about 5 per cent of total GDP. However, 13 per cent of the economically active population is directly employed by the agricultural sector. Thus, a large part of the population relies directly or indirectly on this sector for its livelihood. Notwithstanding the agricultural sector’s declining share in the GDP, it remains vitally important to the economy and to the development and stability of the Southern African region.

Although a net exporter of agricultural products in prosperous years, in world terms South Africa is a minor player. As such it cannot influence international market trends and prices. Consequently, South Africa attaches great importance to the liberalization of world agricultural trade over the next decade.

Agricultural exports amounted to 8.4 per cent, of total exports in 1991, which is 23 per cent of the value of agricultural production. This illustrates the importance of international trade for the
agricultural sector. The most important export products are wool, sugar, maize, deciduous fruit, citrus fruit, hides and skins. In respect of several of these products 50 per cent or more of output, is being exported, with more than 90 per cent of total production in respect of certain products.

Although the agricultural sector is, to a great extent, export orientated, some sectors have to rely on imports to fully meet domestic demand. Rice, oil cake, vegetable oils, unprocessed rubber and cotton are the principal agricultural imports. In 1991, agricultural imports accounted for 4.9 per cent of total imports. In times of drought, grain is also imported, as was the case in 1992/93, when as a result of crop failures due to the drought, a considerable tonnage of maize had to be imported.

B. AGRICULTURAL TRADE POLICIES AND PRACTICES

(1) Objectives of Agricultural Trade Policies

(a) Introduction

Low prices paid to farmers during the depression of the early 1930s necessitated government intervention to ease the misfortunes of the time. Various relief measures were implemented and the domestic prices for farm products were raised above prices of equivalent foreign products. From 1930 to 1935, statutes for the control of industrial milk products, maize, tobacco, wheat and slaughter stock were enacted by Parliament.

When the depression ended, agricultural prices did not recover to the same extent as prices of industrial products. The conviction that permanent government intervention in the agricultural sector was necessary, was manifested by the enactment of the Marketing Act of 1937. This Act extended and consolidated all previous legislation pertaining to the control of agricultural products.

The first White Paper on Agricultural Policy was tabled in Parliament in 1946. Its aim was to identify policies in terms of which Government could maintain agriculture as a key industry in South Africa. Thus, the essence of the White paper was how Government could afford maximum protection to the agricultural sector. This was indeed achieved by a combination of price controls, demand and supply controls and price equilibrium between the prices of agricultural products and other products. The functions of the agricultural control boards were also expanded to cover many other products.

(b) Agricultural trade policies

The objective of the more recent White Paper on Agriculture, namely that of 1984, was to develop a policy for agriculture that would enable the factors of production employed to contribute to the economic upliftment of South Africa. Specific goals in terms of production, marketing, hygiene standards, quality control and general goals, are set out in the White Paper.

(c) Threats and opportunities

The cost effectiveness, efficiency and competitiveness of South African agriculture are dependent on free access to foreign markets and international trade. The effect of sanctions which restricted South Africa's access to international trade, caused a loss of export marketing opportunities.
for the agricultural sector and thus further depressed the economy. Despite this, the quality of South Africa's agricultural products, its marketing reliability, and stringent quality controls, enabled South Africa to maintain its position as an exporter to a discerning world market.

The political reforms and moves towards democracy in South Africa, have enabled the international community to forego sanctions and to trade more freely with South Africa. These developments have allowed South Africa to re-enter the realm of international trade, exposing our businessmen to new levels of competition, quality, standards and prices, but also providing them with many opportunities.

South Africa enjoys a comparative advantage in Southern Africa due to efficient commercial farming methods. As a result of fluctuations in climatic conditions, sporadic surpluses occur, resulting in these surpluses being sold on a depressed world market. Being a small player by world standards the comparative advantage is then lost.

(d) **Liberalization within the agricultural sector**

The international agricultural market is plagued by protectionism, especially subsidization. South Africa cannot compete against the assistance levels granted by others countries, especially by certain members of the OECD. Fiscal pressures have forced the government to phase out bread and maize subsidy schemes which were aimed at reducing the price of these items to consumers.

The recent formation/expansion of economic trade blocks, such as the EC and NAFTA, within which tariffs and other forms of protection are reduced and even abolished, while such measures are maintained and sometimes even intensified against the rest of the world, is cause for great concern in South Africa.

Although South Africa is a member of the Southern African Customs Union, its major agricultural markets remain Europe and the Far East.

During the 1980's reforms were introduced to improve the efficiency and responsiveness of various sectors to market forces. A change in the emphasis from the traditional production-orientated approach of the pre-1980's to a more market-related one, is currently being followed in agriculture. Farmers are now more aware of consumer trends, tastes and demands. The Government is committed to privatization and deregulation of Control Boards to improve efficiency. In line with the proposed obligations in terms of the Uruguay Round, South Africa is moreover in the process of replacing all quantitative import restrictions with tariffs.

A major structural adjustment programme in regard to agriculture, the land withdrawal scheme, was introduced on 1 October 1987. The objective of this scheme was to withdraw 1 million hectares of marginal cropland for grazing.

South Africa's erratic climatic conditions sometimes necessitates special disaster relief measures to counter the effects of drought, floods and hailstorms.
(e) **Importance of the multilateral trading system**

South Africa, a founder member of GATT, is committed to an open and free multilateral world trading system. South Africa has supported the objectives of the Uruguay Round of reforming agricultural policies.

(2) **Description of the Agricultural Import and Export System**

South Africa followed a trade policy of import substitution for decades. Re-adjustment to an export-orientated policy is currently being pursued. The legislation controlling agricultural imports and exports includes section 87 of the Marketing Act, 1968 (Act 59 of 1968), the Import and Export Control Act, 1963 (Act 45 of 1963), as well as a number of technical regulations.

(a) **Commercial measures**

The following legislation is currently applicable:

**Section 87 of the Marketing Act.** This legislation empowers the Minister of Agriculture to prohibit the importation or exportation of agricultural produce unless a permit therefore has been issued, either by the Director-General of Agriculture or the relevant control board. The Minister may also determine the total quantity of a controlled product to be imported or exported during a particular period.

The importation and exportation of products not prohibited by the Marketing Act, are controlled by the Import and Export Control Act. This Act is administered by the Department of Trade and Industry. Permits are granted and issued subject to recommendations by the Department of Agriculture. Products affected by this arrangement range from fresh and preserved fruit and vegetables to herbs, spices and animal feeds.

(i) **Imports**

Import duties are payable on a large number of agricultural products. These have seldom been adjusted to provide an adequate level of protection for local producers, as quantitative controls, either through the Marketing Act or the Import and Export Control Act, are the principal methods of control. The following control boards have the sole right to issue permits for importing their commodities: Wheat Board (wheat, barley, oats), Maize Board (maize and maize products), Dairy Board (butter, cheese, condensed milk, milk powder and skim milk powder), Lucerne Seed Board (lucerne seed), and the Grain Sorghum Board (grain sorghum and grain sorghum products). A permit is needed to import dried prunes, dried sultanas, raisins, dried currants, leguminous seeds, potatoes (except seed potatoes), chicory (including ground chicory and unroasted chicory), canary seed, cotton seed and cotton lint, coriander, soya beans, certain maize products and dry beans. Permits are issued by the Department of Agriculture.

Government policy, among other things, aims at the phasing out of quantitative control in favour of tariff protection. In 1988 tariffs for poultry and poultry meat were introduced and the quantitative control under the Import and Export Control Act was abolished. This is in line with the tariffication process required by virtue of the agricultural section in the text of the Draft Final Act.
of the Uruguay Round. Tariffs have subsequently been introduced for sugar, fish meal, vegetable oil, oil cake, tobacco, red meat and meat products.

In terms of Article 3 of the respective trade agreements between South Africa and Malawi and South Africa and Zimbabwe, permits are issued to allow the importation of certain agricultural products at preferential duties.

Levies, similar to those charged on local products, are imposed in respect of the importation of certain products in terms of the Marketing Act.

In order to improve the competitive ability of the agricultural sector, Government has requested the Board on Tariffs and Trade to conduct an investigation into input costs pertaining to that sector.

(ii) Exports

Section 87 of the Marketing Act, controls the export of potatoes, dried fruit, eggs, grain sorghum, lucerne seed, canned deciduous fruit, cotton (seed and lint), wheat, barley, oats, maize, groundnuts, sunflower seed, soya beans, vegetable oils, rooibos tea, deciduous fruit, chicory (unroasted), citrus fruit, tobacco (via co-operatives), red meat, live cattle, sheep, goats, pigs, karakul pelts, eggs, ostriches and ostrich products.

During the 1980s, incentives were introduced to promote exports. The variable export marketing allowances of section 11(bis) of the Income Tax Act, 1962 (Act 58 of 1962), were introduced. In 1990 it was announced that these allowances would be terminated on 31 March 1992. Some agricultural exports did, however, qualify for the General Export Incentives Scheme, GEIS, which was, in the mean time, introduced in April 1990. GEIS provides direct subsidies on the value added to products manufactured for export purposes. A number of agricultural products resort under category 1 of this scheme and therefore, do not qualify for export assistance. Other products fall under categories 2.3 and 4 which presently qualify for a subsidy of 7.5 per cent, 13.5 per cent and 25.0 per cent, respectively, of the export value.

A number of control boards subsidise the export of surplus produce by granting subsidies financed through levies on producers. In this case the domestic price will be higher than the export price. The effect is a two-tier price system. The Maize, Wheat, Dairy, Meat and Egg Control Boards have all sold surplus produce by subsidization.

South Africa is a member of a number of international commodity arrangements, such as the GATT’s International Dairy Agreement (IDA), the Agreement regarding Bovine Meat (IMC) and the International Wheat Council (IWC). Only the IDA enforces minimum export prices, while economic provisions are not applicable to the other arrangements.

(b) Technical measures

The following Statutes are applicable:

of animal diseases and parasites, promote animal health and public health service. The aim of these import and export control services is to facilitate the international trade in animals and animal products, and the movement of genetic and biological material without risking the health of the livestock industry and the public.

The Agricultural Pest Act, 1983 (Act 36 of 1983), aims to prevent harmful foreign organisms from entering South Africa, and to destroy them as and when detected. In terms of the Act, the import and export of agricultural products are regulated by the issue of permits and phytosanitary certificates. Phytosanitary requirements differ from country to country due to the regional distribution of harmful organisms.


The Liquor Products Act, 1989 (Act 60 of 1989), prohibits certain products from being imported into South Africa. Imported liquor must comply with certain minimum standards. In some cases permission should be obtained from the Wine and Spirit Board before liquor could be imported. This Act protects the domestic market from inferior imports, including brandy not made and matured according to local regulations, as well as pre-mixed drinks, fermented rice beverages and sacramental wine.

In terms of the Plant Improvement Act, 1976 (Act 53 of 1976), South Africa has a restricted plant variety list. This list controls the varieties which may be introduced to South Africa to guard against harmful materials.

The Fertilizers, Farm Feeds, Agricultural Remedies and Stock Remedies Act, 1947 (Act 36 of 1947), rules that no one may import and sell fertilizer, farm feed, agricultural or stock remedy in South Africa unless it is registered in terms of section 3 of the Act. The reasons for this are: to ensure that no harmful pathogens are introduced into the country; to ensure that no substandard items are imported; and to ensure that any remedy imported into South Africa has been tested for its adaptability to South African conditions. The registration requirements in South Africa conform to those of the EC and most other countries.

The Livestock Improvement Act, 1977 (Act 25 of 1977), regulates the genetic improvement of the livestock industry. Five national improvement schemes have been established in terms of the Act. Section 16 of the Act deals with control over the importation of genetic material. The importation of these materials must be authorised by the Registrar of Livestock Improvement and Livestock Brands, once the relevant breeders' society has recommended a particular application.

(i) Imports

Imports of live animals and animal products are inspected and the importers concerned are issued with import permits at the port of entry. The issuing of a permit depends on the general state of health of the animals in the country of origin.
South African legislation, with respect to the above, aims to:

(a) introduce animals and animal products without jeopardising the present animal health and environment of the country;
(b) prevent the introduction of new diseases and pests;
(c) detect, control and prevent the spread of new diseases and pests; and
(d) formulate and implement risk management policies.

All agricultural imports must comply with local standards, including standards pertaining to minimum marking; i.e. the name of the product, country of origin, a description of the contents and the name and address of the importer.

The Livestock Improvement Regulation, R.894 of 26 April 1991, the promulgation of which was requested by the Southern African Poultry Association, aims at protecting the local industry from falling prey to foreign diseases.

Bilateral agreements with South Africa's neighbouring countries, allow for the relative free movement of animal and animal products. A master veterinary permit, the granting of which depends on existing health standards is issued on an annual basis in order to facilitate movement of the relevant products. Moreover, import restrictions are also applied to protect animal health, public health and safety and not least, the environment.

(ii) Exports

Local and export standards are, as far as possible, harmonized with international standards which are prescribed by organizations such as Codex Alimentarius, the International Dairy Federation and the Economic Commission for Europe.

South Africa is internationally classified as a country infected by foot and mouth disease, African swine fever, blue tongue and African horsesickness. The export of products prone to these diseases have, in the past, been minimal. However, through relatively effective disease and movement control and by declaring some areas in the country as disease free areas, a number of countries do accept South African animals and animal products.

The export of animals is controlled in order to protect endangered species; conserve indigenous resources; honour agreements with overseas and neighbouring states; and to prevent trade in the commodities of endangered species, as for example, ivory.

(3) The Trade Policy Framework

(a) Domestic laws and regulations

Approximately 67 per cent of the gross value of agricultural production is marketed by the various control boards. About 11 per cent is marketed in terms of legislation that regulate the sale of sugar, lucerne, hay, wattle bark, wine and ostrich products. The remaining 22 per cent, chiefly consisting of vegetable products, is not formally regulated.
In 1937 The Marketing Act was passed by Parliament to introduce and amend marketing schemes which at that time related to all farm products. The idea was to have one piece of legislation which would cover all of the relevant products instead of having separate legislation for each specific product.

In 1968 a new Statute was enacted, the Marketing Act, 1968 (Act 59 of 1968). The objectives with this legislation were, amongst others, to ensure greater price stability and to reduce the margin between producer and consumer. The Act also aims at improving farming productivity and the efficiency of marketing and processing of the produce. The Act furthermore, provides for marketing schemes and other measures with which to control the marketing of agricultural produce. The Act also provides for the establishment of different control boards to administer the various schemes.

The Marketing Act also enables the Minister of Agriculture to exercise the powers of a control board in respect of those products which are not subject to a particular scheme.

There are presently 20 control boards administering 20 schemes. These schemes differ according to the nature and circumstances of each product. Perishability, geographic distribution, efficiency of processing and distribution, local consumption and the importance of each product to the community are some of the factors which influence the practical functioning of the schemes.

The present schemes in operation fall into four classes, as follows:

(i) Single channel fixed-price schemes

Producers are legally bound to sell their produce to the board concerned. Producer and local selling prices are fixed for a particular season. This relates to maize and wheat.

(ii) Single channel pool schemes

Producers pool their produce with the relevant board which makes advance payments to them. A final payment is made after all the produce is sold and expenses deducted. This method pertains to tobacco, oilseeds, wool, mohair, deciduous fruit, dried fruit, citrus fruit, chicory, rooibos tea and lucerne seed.

(iii) Surplus removal schemes

Producers sell their products on the open market. The board concerned intervenes when the price drops below a fixed level by purchasing the surplus. The surplus is either exported, redistributed or resold at a later date, for example red meat, dry beans, grain sorghum, eggs, milk and potatoes.

(iv) Supervisory schemes

The particular board acts in a supervisory capacity mediating between producers and buyers for contracts and prices, e.g. fruit canning and cotton.
The Co-operative Societies Act of 1939, was replaced by the Co-operatives Act, 1981 (Act 91 of 1981). This Act introduced co-operative single channel marketing schemes. The Act aims at regulating the marketing of agricultural products. A marketing scheme in terms of this Act is governed by private enterprise. The introduction of new schemes was terminated in 1981 when the new Act replaced the Act of 1939. A scheme could henceforth only be withdrawn with a majority vote of 66 per cent of the producers of the particular co-operative.

All members of a co-operative are obliged to sell their produce to the co-operative, usually on a pool basis. Currently only lucerne hay, tobacco, wine, ostriches and ostrich products are governed by schemes in terms of the Co-operatives Act.

(b) The policy formulation process

The Marketing Act also makes provision for any organised producer body to submit proposals to the Minister for a scheme that would regulate the marketing of its specific product. The proposal concerned first has to be referred to the National Marketing Council, NMC, which then conducts an investigation into the matter and thereafter reports to the Minister. If the Minister accepts the proposal, details of the scheme is published in the Government Gazette. The scheme becomes legally enforceable as from the date of such publication.

Control boards are supervised by the Minister of Agriculture, who is advised by the NMC. Many board decisions require Ministerial approval. The NMC consists of eight members who meet regularly to discuss the decisions of the existing control boards. Council members regularly attend meetings of the control boards. The NMC also investigates, inter alia, economic aspects of production and marketing, price levels, levies, marketing and processing costs.

Individuals may appeal to the Minister against a board decision concerning dealer registration, manufacturers and processors, agency appointments, and the issuing of permits for the importation or exportation of regulated products.

(c) Multilateral, bilateral and regional trade agreements

Such agreements have already been referred to above, but as regards the agricultural implications thereof, they need to be elaborated upon.

(i) Multilateral trade agreements

South Africa signed the International Dairy Agreement and the Arrangement regarding Bovine Meat.

The first Southern African Customs Union (SACU) Agreement was signed in 1910 after South Africa became a Union. The present SACU Agreement with Botswana, Lesotho, Namibia and Swaziland (BLNS-countries) is a continuation of the 1910 Agreement, and has been in effect since 1 March 1970. Articles 12 and 18 refer to agricultural products and their marketing within the common customs area.

The marketing policies of the various regions of the customs area are applied on an equal basis to commodities produced in some or in all regions of the customs area, where such commodities
are marketed in a particular region. The Agreement provides for consultations on matters affecting production, consumption and the improvement of marketing schemes of agricultural products.

(ii) Bilateral trade agreements

(aa) The Trade Agreement between South Africa and Malawi was signed on 19 June 1990. In terms thereof, South Africa allows all products grown, produced or manufactured in Malawi to be imported into South Africa duty free. The importation of certain products are subject to permits issued by the Department of Agriculture or Trade and Industry. These products include, inter alia, dairy products, potatoes, coffee, tea and unprocessed tobacco. South Africa, in turn, can export to Malawi all products grown, produced or manufactured in South Africa at the most-favoured-nation rate of duty. Import permits are issued for live animals, meat and edible offal, live fish, bananas and certain cereals.

(bb) The trade agreement between South Africa and the erstwhile Southern Rhodesia, now Zimbabwe, was signed on 1 December 1964. In terms of this agreement, goods produced in one country may not be imported into the other country unless an import licence has been issued. The agreement provides for preferential duties on imports covering a wide range of products.

South Africa exports certain products to Zimbabwe at the most-favoured-nation rate of duty, which is rebated to a specified extent. Zimbabwe exports to South Africa at reduced rates of duty depending on the percentage of local content up to a specified volume or value.

(cc) The Arrangement on Tariff Concessions by the Republic of South Africa to the Peoples’ Republic of Mozambique came into effect on 7 July 1989. In terms of this Arrangement, South Africa grants tariff rebates on imports of Mozambican origin subject to quotas (value/quantity) as specified in the arrangement. Goods imported in terms of this Arrangement can only be used/consumed in South Africa and Botswana. Agricultural products presently included in the Arrangement are fish, shrimps, citrus fruit, coconut oil, cashew nuts and cottonseed oil cake.

(4) The Implementation of Agricultural Trade Policies

(a) Agricultural trade policy measures

South African agriculture is not structured to meet the needs of the population in regard to all commodities. A policy of producing what is dictated by the national resources and the environment is generally followed. Consequently, those products that cannot be produced locally on a viable basis, are imported.

(i) Tariffs and tariff equivalents

The Board on Tariffs and Trade is responsible for customs duties on agricultural products. Requests for amendments to tariffs are published for comment in the Government Gazette. These comments are then taken into account by the Board and a recommendation is made to the Ministers of Agriculture and of Trade and Industry for approval. The Minister of Finance is then requested
to implement such amendments, which are then published in the Government Gazette, at which stage they become operative.

Import control in respect of the following agricultural products has been withdrawn and replaced with tariffs:

(aa) Poultry and poultry meat
Tariffs were introduced in 1988.

(bb) Tobacco
Tariffs were introduced in 1990.

(cc) Sugar
Tariffs were introduced in 1989.

(dd) Other products
The South African Agricultural Union applied for a 30 per cent ad valorem duty on a range of fresh, dried, frozen fruits and vegetables. The Board on Tariffs and Trade (BTT) is evaluating the application.

The Grain Traders Association has applied for the lifting of import control and the imposition of tariffs on peas, lentils and other pulses, except dried beans. This application is currently being considered by the BTT. The application for tariffs on dried beans will be submitted later in 1993.

Replacing quantitative controls with tariffs will continue as a matter of policy.

(ii) Quantitative restrictions

In terms of the Marketing Act and the Import and Export Control Act, import permits are the main instruments for controlling imports. This has resulted in customs duties not being updated in order to provide the correct level of protection on an ongoing basis.

Section 87 of the Marketing Act prohibits the importation or exportation of any agricultural product, unless a permit is obtained from the Director-General of Agriculture.

The Minister of Agriculture is deputed to confer on the Director-General of Agriculture or on the relevant control board, the sole right to import or export a regulated product to or from South Africa.

(iii) State trading enterprises

The following control boards market agricultural products in South Africa:

(aa) The Banana Board which was only concerned with the marketing of bananas on the domestic market has been abolished with effect from 1 April 1993.

(bb) The Rooibos Tea Board sells an indigenous type of herbal tea on behalf of producers at predetermined prices which are approved by the Minister of Agriculture. The
Board distributes the net proceeds on a pool basis. Exports are effected by the Board or a person authorised to export in terms of a permit issued by the Board.

(cc) The Chicory Board dries and then sells chicory root on behalf of producers to coffee roasters. An advance payment is made to producers and a subsequent payment is made depending on the ultimate realization for the crop at the end of the season. The Board is the sole importer and exporter of unroasted chicory, while roasted or ground chicory may be imported under a permit issued by the Department of Agriculture.

(dd) The Citrus Exchange, as agent of the Citrus Board, exports oranges, lemons and grapefruit on behalf of producers on a pool basis. Producers are responsible for the sale of their fruit on the domestic market, but the Board is responsible for market research and development and advertising. During the off-season imports may take place with the permission of the Board.

(ee) The Dairy Board operates a surplus removal scheme in terms of which minimum prices are determined for skim milk powder and butter. It, however, does not determine the price of fresh milk. The prices at which processors sell milk and other dairy products are likewise not controlled. The Board also imports or issues permits for the importation of butter, milk powder, condensed milk, condensed skim milk and cheese when local supplies are insufficient.

(ff) The Deciduous Fruit Board functions in a similar manner as the Citrus Board. The Board’s agent, Unifruco, exports apples, apricots, grapes, peaches, nectarines, pears, plums and prunes produced in the principal production areas on a pool basis on behalf of producers.

(gg) The Dried Fruit Board is the sole buyer from producers of dried prunes and dried vine fruits. A single channel pool scheme is in operation. After providing for the domestic market, the Board exports any surpluses. Producers receive advance payments and deferred payments are made from the pools after the crops have been sold.

(hh) The Egg Board, with the approval of the Minister of Agriculture, fixes minimum prices at which the Board is prepared to buy surplus eggs from producers. The Board’s purchases are processed and disposed of locally or exported. Exports take place either by the Board or by a person authorised to do so in terms of a permit issued by the Board.

(ii) The Meat Board, with the approval of the Minister of Agriculture, fixes floor prices at which it is prepared to buy dressed carcasses of cattle, sheep, goats and pigs at the auctions in the main urban centres, designated as controlled areas. The Board purchases all carcasses which fail to reach the floor price at these auctions. The Board further regulates the flow of animals to the main urban centres through the application of a quota or permit system. The Board is in the process of deregulating its scheme, with the purpose of freer movement of meat.
(jj) The Lucerne Seed Board administers a single-channel pool scheme for lucerne seed and appoints agents to handle the crop. The Board’s advance payments to producers, its selling price to lucerne seed cleaners and the latter’s selling price to the distributive trade are fixed annually with ministerial approval. The Board is the sole importer and exporter of lucerne seed.

(kk) The Maize Board operates a single-channel marketing scheme for maize. The Board buys all maize from producers through appointed agents at prices which it determines annually. The prices at which the Board buys and sells these cereals are fixed, but not the resale prices charged by the maize trade nor the prices of the products manufactured therefrom. The Board sells surplus maize on tender to independent exporters and, since 1982, exports also on a direct basis. Any losses sustained or profits made on such exports are met from or accrue to the Board’s stabilization fund, as the case may be, to which all producers contribute by means of a levy.

(ll) The Oilseeds Board is the sole buyer from producers of groundnuts, sunflower seed and soya beans and appoints agents to handle the crops. Depending on overseas prospects as well as the domestic selling prices to the trade, which are fixed by the Board with the approval of the Minister of Agriculture, the Board makes advance payments to producers according to grade. Subsequently, the Board makes one or more deferred payments from its pools depending on what it realizes on average from the sale of the crop. Although the Board undertakes exports of sunflower seed and groundnuts, it also sells a portion of these products to local traders for export purposes. A permit issued by the Director-General of Agriculture is required for the importation of soya beans, while in the case of groundnuts and sunflower seed, only a recommendation from the Department of Agriculture is required for the Department of Trade and Industry to issue an import permit.

(mm) The Tobacco Board fixes the minimum selling prices of tobacco for manufacturers, while the tobacco crops are handled by co-operatives. The Tobacco Exchange handles the export of leaf tobacco on behalf of the Tobacco Board. According to the preferential trade agreement with Malawi and Zimbabwe, a permit in terms of the agreement is necessary when importing from these countries.

(nn) The Wheat Board, through appointed agents, is the sole buyer of wheat and barley from producers, while in the case of oats, producers are authorised by permit to sell direct to consumers. The domestic prices of these cereals are determined annually by the Board with the approval of the Minister of Agriculture. The prices at which the Board buys and sells these cereals are fixed, but not the resale prices by the trade or prices of the products manufactured therefrom. The Board, or any person it authorises thereto by permit, is responsible for both imports and exports of wheat.

(oo) The Canning Fruit Board Scheme is primarily aimed at the promotion, and the orderly marketing of canned pears, peaches and apricots and contains provisions for proper grading and payment according to quality. The Scheme provides for seasonal contracts between canners and producers in respect of buying and selling of these products. Minimum prices are fixed annually between buyers and sellers of fruit for
canning purposes on a consensus basis. Any person authorised by a permit, issued by the Board, may export canned fruit.

(pp) The Mohair Board administers a single channel pool scheme whereby advance payments are made to producers on receipt of the mohair by the Board. At the end of the season, when the different pools are finalised, producers receive their final payments. The Board sells mohair through appointed agents by auction, subject to its reserve price.

(qq) The South African Wool Board administers a single channel pool scheme. Advance payments are determined at the beginning of each season and when the various pools are finalised, producers receive their final payment. The Board sells wool by auction through an agent subject to the reserve prices.

(rr) The Cotton Board operates a supervisory scheme. The producer prices for seed cotton depend on the prices at which ginners sell cotton lint to spinners. The latter prices are negotiated annually on a voluntary basis between the various interested parties. A permit issued by the Director-General of Agriculture is required for importing seed cotton and cotton lint.

(ss) The Potato Board, Dry Bean Board and Grain Sorghum Board were amalgamated into one administration, the PDG Boards, which operate the following schemes for potatoes, dry beans and grain sorghum:

(i) The potato scheme endeavours to stabilize prices through purchases when excessive supplies reach the market. Supplies thus purchased by the Board are redistributed to deficit markets, and to lower income groups, mostly at reduced prices, while small quantities of potatoes are exported by the Board or by a person so authorised by a permit issued by the Board. A permit issued by the Department of Agriculture is necessary for imports.

(ii) A floor price scheme is in operation for the main varieties of dry beans when local supply and demand conditions warrant such action. This action was seldom deemed necessary in the past years. The Board, in the light of crop prospects, may fix minimum prices at which it is prepared to buy beans from producers, should they not be able to obtain the equivalent or better prices on the open market. Purchases by the Board are sold for domestic consumption or for export by the private trade.

(iii) The Grain Sorghum Board operates a floor price scheme. Supplies which producers are unable to sell at higher levels on the open market are purchased by the Board at prices which are fixed annually for the different grades. Purchases by the Board are resold to the trade for use as stock feed. The Board, or any person it authorises thereto by a permit, is responsible for both imports and exports of grain sorghum.
C. RELEVANT BACKGROUND AGAINST WHICH THE ASSESSMENT OF AGRICULTURAL TRADE POLICIES WILL BE CARRIED OUT

(1) External Economic Development

(a) Major trends in imports and exports

During the 1980's, sanctions brought about changes in the structure of South Africa's international agricultural trade. Exports to the USA and Canada declined by 90 per cent and 53 per cent, respectively, during 1980 and 1987. Imports from the USA, as a percentage of total imports, declined from 20 per cent in 1980 to 10 per cent in 1990. However, imports from and exports to the EC increased during this period.

(b) Imports

Between 1980 and 1990, the value of agricultural imports from South Africa's major suppliers changed as follows:

<table>
<thead>
<tr>
<th>Country</th>
<th>Foreign currency change in rand terms</th>
<th>Rand terms</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Canada</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>EC</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>Australia</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>Japan</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Malawi</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>Mauritius</td>
<td>-</td>
<td>+</td>
</tr>
</tbody>
</table>

The following changes occurred in imports of major agricultural commodities over the past ten years:

<table>
<thead>
<tr>
<th>Percentage of total agricultural imports</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td><strong>1980</strong></td>
</tr>
<tr>
<td>Rice</td>
</tr>
<tr>
<td>Coffee</td>
</tr>
<tr>
<td>Rubber</td>
</tr>
<tr>
<td>Cotton</td>
</tr>
<tr>
<td>Oilseeds</td>
</tr>
<tr>
<td>Vegetable Oils</td>
</tr>
</tbody>
</table>
(c) **Exports**

The EC was the major export destination over the past decade (62 per cent of total agricultural exports in 1990). The UK, Germany, Belgium, Italy and France represented 89 per cent of all exports to the EC in 1990. Exports to Japan were 14 per cent of total agricultural exports in 1990.

Exports of wool, hides and skins, maize, sugar, wheat, citrus and deciduous fruit as well as preserved fruit and jams totalled 75 per cent of total agricultural exports during the past decade.

<table>
<thead>
<tr>
<th>Percentage of total agricultural exports</th>
<th>1980</th>
<th>1990</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wool</td>
<td>10.7 per cent</td>
<td>15.7 per cent</td>
</tr>
<tr>
<td>Sugar</td>
<td>19.3 per cent</td>
<td>13.8 per cent</td>
</tr>
<tr>
<td>Maize</td>
<td>20.7 per cent</td>
<td>11.7 per cent</td>
</tr>
<tr>
<td>Deciduous Fruit</td>
<td>6.3 per cent</td>
<td>11.3 per cent</td>
</tr>
<tr>
<td>Citrus Fruit</td>
<td>6.0 per cent</td>
<td>6.3 per cent</td>
</tr>
<tr>
<td>Preserved Fruit and Jam</td>
<td>7.6 per cent</td>
<td>8.8 per cent</td>
</tr>
<tr>
<td>Wheat</td>
<td>0.9 per cent</td>
<td>2.3 per cent</td>
</tr>
<tr>
<td>Hides and Skins</td>
<td>3.0 per cent</td>
<td>4.7 per cent</td>
</tr>
</tbody>
</table>

(2) **Barriers to External Markets**

(a) **Sanctions**

Sanctions against South Africa resulted in a marked change in agricultural exports. The industry was not only forced to rely more on the domestic market, but also had to establish new markets at great cost. The reform process in South Africa and the definite moves towards democracy, have led to a more relaxed attitude towards South Africa by the international trading community. However, in some cases South Africa still faces restrictions on its exports to certain markets such as particular US States and some Commonwealth countries.

(b) **Subsidies**

South Africa cannot compete with the massive subsidies paid to producers by other agricultural producing countries, notably by certain members of the OECD, on products such as maize, wheat, and oilseeds. The consequence of these subsidies is that it is often cheaper to import these products than to grow them locally.

(c) **Tariffs and quotas**

Other protectionist measures such as tariffs and quotas further restrict South African exports in many markets. With the global move to liberalise trade, the position may probably gradually improve as far as South Africa's agricultural products are concerned.
Other barriers, such as phytosanitary regulations in the USA and EC, have effectively closed markets to South African produce. Maize and potatoes are examples in this regard.

(3) **Regional Economic Development**

South Africa is currently classified as a developed country and therefore does not qualify for trade benefits afforded to countries classified as developing countries. These benefits include, *inter alia*, preferential rates of duty.

The South African government is currently studying the plausibility of having South Africa re-classified as a developing country in order to take advantage of the benefits offered internationally. The wars in Angola, Mozambique and Namibia, combined with droughts, malnutrition, poverty and economic stagnation have reduced Southern Africa to an economic cripple. Much needs to be done and South Africa can be the catalyst upon which the region begins to heal its wounds.

Against this background, South African agricultural trade policy will have to take into account the following two aspects:

(a) Subsistence farming which is part and parcel of Southern Africa's dualistic agricultural economy. This will need special support programmes to enable the agricultural industry to contribute to the socio-economic aims of the region; and

(b) The developing country status of the countries in Southern Africa, as classified by the GATT, is not similar to that of South Africa, a fact that may lead to unfair competition in the Southern African market.
ANNEX A

THE KEY ISSUES IN THE NORMATIVE ECONOMIC MODEL

March 1993
ERRATA

1. Page 16
   "..., the agreement on Trade Related Investment Measures (TRIMS), ..." under paragraph 4.6, second sub-paragraph on page 16, should read "..., the agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS), ...".

2. Page 17
   The figure for job opportunities under paragraph 5.2 on page 17, should read 1,300,000.
Preface

The main purpose of the present memorandum is to identify and briefly discuss key issues in the so-called "Normative Economic Model" constructed by the Central Economic Advisory Service under the direction of Mr Jan Dreyer. The model itself has been constricted with inputs from Dr Japie Jacobs, Special Adviser to the Minister of Finance, the South African Reserve Bank, several government departments, the Industrial Development Corporation and the Development Bank of Southern Africa. Its release has been delayed by the work involved in the collation of the many inputs and the time required to edit and prepare the lengthy document in both official languages.

The present memorandum focuses on the nature and size of the major objectives, constraints and available policy options. It does not discuss or demonstrate the "internal consistency" of the various quantitative results of the modelling exercise. Professional economists interested in this issue need to consult the main report.

This memorandum, which is a synthesis rather than a summary, deals with the issues in a sequence which may differ somewhat from the main report, Broader issues of socio-economic reconstruction in support of the envisaged growth process also receive somewhat greater relative emphasis in the present document than in the main report. Moreover, the model, and the policy framework largely derived from it, do not claim to be comprehensive. This is basically a macro-economic exercise for public discussion in its own right and to serve as a point of departure in public discussions of broader and more detailed issues in the political economy of the country. The strategies discussed are to be regarded as an internally consistent set of options, rather than a programme proposal from government.

The document was drafted by Professor Jan Lombard during February 1993 with the assistance of Dr Johan van den Heever (of the South African Reserve Bank) and Ms Lolette Kritzinger-van Niekerk (of the Development Bank of Southern Africa). They were also assisted in the first two weeks of the month by the following economists Dr Pieter Haasbroek (of Barlow Rand), and Messrs Jan de Jager (of the National Productivity Institute), Flip Kotze and Gerrit van Wyk (of the Industrial Development Corporation) and Dave Mohr and Dr Terence Moll (of The Old Mutual). These persons are not, of course, responsible for the final draft.

Ms Rina Viljoen and Ms Marietjie Pretorius did a sterling job in typing and typesetting the numerous drafts. The final document was printed in the Reserve Bank.

I wish to express my sincere thanks to everyone, including the South African Reserve Bank which provided valuable support services, for their contributions in producing the present document in a very brief space of time.

Derek Keys
Minister of Finance and of Trade and Industry
THE KEY ISSUES IN THE NORMATIVE ECONOMIC MODEL

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C/RM/G/37  
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The Normative Economic Model, and the framework for policy options based on it, deal with economic growth and development in South Africa in terms of:

- a feasible vision for the South African economy in the foreseeable future,
- the realities constraining its achievement, and
- a strategy framework for action to address the constraints and realise the vision.

The exposition is presented as a basis for public discussion and negotiation among the parties concerned.

The proximate roots of economic growth are perceived to be found in more investment and greater productivity of investment. Productivity, in turn, is perceived in terms of more real value added and more gainful employment of people.

Central to the strategy and the macro-economic consistency of the supporting normative model, is the need for the government sector to free national resources for more investment, mainly by the private sector, in growth and development. The model also shows the extent to which the attainment of the objectives also depends on a favourable turn in the capital account of the balance of payments.

THE VISION

What is envisaged is a process of structural adjustment in the developed market economy and a reconstruction of its less developed socio-economic framework, in particular the equitable access of all South Africans to all opportunities in the economy. The main product of this transformation is expected to be the generation of a growing, high quality income per capita, sustained by the beneficial participation of all South Africans. The market economy responsible for most of the performance in this regard, is expected to become much more efficient in its production functions, and more equitable in its distribution functions. Finally, economic activity is envisaged to take place in an environment of macro-economic stability.

Table 1 provides an overview of some of the main quantitative features of this vision:

<table>
<thead>
<tr>
<th>Table 1: The Vision Quantified</th>
<th>1992 %</th>
<th>1997 %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP growth</td>
<td>-2</td>
<td>4½</td>
</tr>
<tr>
<td>Per capita</td>
<td>-4½</td>
<td>2¼</td>
</tr>
<tr>
<td>Employment growth</td>
<td>-2</td>
<td>3</td>
</tr>
<tr>
<td>Average rate of inflation</td>
<td>14</td>
<td>5</td>
</tr>
<tr>
<td>Share of income enjoyed by poorest 40% of households</td>
<td>6%*</td>
<td>10</td>
</tr>
</tbody>
</table>

*1988
The new paradigm

The economic system of a reconstituted and integrated South Africa necessarily differs substantially in many respects from that which functioned under the policy of separate development. The new political understanding of the nature of the South African economy, accordingly, accepts that the process of economic growth must be seen as but a central feature of the broader process of economic development of the country and its people. The latter is also an end in itself. These two dimensions go together, although at the present juncture an early revival of economic growth must be emphasised.

Market effectiveness

Since these socially desirable objectives are to be achieved mainly through the market system of the South African economy, the broad network of relative prices and costs guiding market processes has to be sound. On the aggregate level this condition refers mainly to the relationship between major prices in the economy, namely the rate of inflation, interest rates, wage rates, the Exchange rate and tax rates.

CONSTRAINING REALITIES

At present, South Africa and its people face a number of realities constraining the attainment of the social objectives envisaged. The constraints are outlined in four fairly distinct categories as follows:

In the immediate future, economic revival is constrained by certain functional imbalances, which add up to the fact that a substantial revival of domestic investment may soon produce serious balance of payments problems and may also be thwarted by the crowding out effects of fiscal policy.

In the medium-term, and assuming that the aforementioned functional imbalances are removed, sustained economic growth will be constrained by certain domestic market inefficiencies, which would probably prevent or curtail a strong process of export-led growth.

In the longer run, and assuming effective diminution of domestic market inefficiencies, economic growth in South Africa may falter because of remaining defects in our socioeconomic system which would prevent the full participation in the growth process by the country’s large developing community.

In general, the economic renaissance of South Africa faces growing international economic complexities which call for energetic responses from our private entrepreneurs and vigilance from our policymakers.

1. FUNCTIONAL IMBALANCES

Prospects for a sustained revival of the South African economy are severely constrained by several functional imbalances that have emerged since the early 1980s. These imbalances are reflected most harshly in a large fiscal deficit, a persistent outflow of capital on the balance of payments, relentless wage and price increases, taxes perceived to be excessive and unfair, and a climate of general uncertainty about the future. These factors all undermine productive investment.
1.1 A large fiscal deficit on revenue account

Since the early 1980s a considerable shortfall has opened up between the current expenditure and current (largely tax) revenue of general government (central, provincial and local governments). This shortfall, or general government dissaving, reached some 4.8 per cent of GDP in 1992, and is illustrated in Figure 1.

![Figure 1: Saving/ dissaving by general government](image)

The widening deficit was largely the result of a sharp and sustained rise in current expenditure by government. The dissaving was tempered to some extent by a considerable increase in the tax burden, but this in its own light created disincentive effects detrimental to economic progress. Apart from unduly raising the government debt burden, such dissaving seriously reduced the amount of domestic savings available for domestic investment. Government curtailed its own expenditure on capital formation to limit its borrowing requirements on the capital market. In spite of this, the overall fiscal deficit (dissaving plus capital outlays) of the general government (all levels) grew from an average of 3.4 per cent of GDP during the period 1985 to 1991 to 6.2 per cent of GDP in 1992.

1.2 A persistent outflow of capital on the balance of payments

For a developing country, a deficit on the current account of the balance of payments may be considered desirable if it arises primarily from high imports of capital goods, as this may be expected to accelerate economic growth. An inflow of foreign capital, i.e. savings from foreigners, is required to finance the deficit on the current account. Were domestic savings to be used to finance a persistent outflow of foreign capital, as has been the case in South Africa since 1985, the potential for domestic growth and development is restricted.
On balance, South Africa experienced net inflows of foreign capital during the 1960s and early 1970s. Then the situation began to deteriorate. A series of political and economic events eventually culminated in a sharp deterioration in foreign perceptions and the foreign debt crisis of 1985. In spite of a succession of debt standstill agreements between the authorities and foreign banks, the economy experienced a considerable net outflow of foreign capital, equalling 2.8 per cent of GDP, between 1985 and 1992. Financing these outflows in a way that would not cause macro-economic instability, resulted in a restriction of the authorities' scope to pursue growth-orientated economic policies.

The accompanying graph illustrates the prolonged and sustained nature of the capital outflows from 1985. The reduction in foreign debt that has been accomplished in the process must, however, be viewed as one of the positive factors which may contribute to a renewed inflow of capital in the future.

**Figure 2: Net capital movements not related to reserves**

1.3 A persistent adverse movement in unit labour costs

Since the middle of the 1970s South Africa has been suffering from an escalation in the levels of consumer and producer prices as well as the costs of factor inputs. Average consumer price inflation rates increased from 3.3 per cent per annum between 1961 and 1972, to 11.2 per cent between 1973 and 1978, 13.5 per cent between 1979 and 1984, and 15.2 per cent between 1985 and 1992. The persistence of these trends imbed consumers and employers with a passive acceptance of inflation. An informal system of inflation indexation consequently arose in price and wage determination which distorted the efficiency of the market economy, leading to a persistent adverse movement in unit labour costs, and accommodating a marked structural movement towards investment in capital-intensive industries and technologies.
Real wages tended to rise more or decline less than productivity in general, as measured by an index of multifactor productivity, or MFP. During 1979 to 1984, for example, real wages increased by 1.29 per cent per annum compared to 0.1 per cent per annum in MFP. During 1985 to 1991 the respective figures were -0.13 per cent and -0.5 per cent per annum. This resulted in rising unit labour costs, which made South African exports less competitive on international markets and imports more competitive on local markets. It also resulted in greater domestic unemployment.

1.4 Tax burden perceptions and entrepreneur uncertainty

A crucial prerequisite for the achievement of the envisaged high rate of economic growth is a substantial improvement in the level of private real investment (capital formation). Among the variables entering into the determination of the propensity to invest in the model are capacity utilisation, interest rate levels, the level of taxation, a successful export drive and an improvement in the political climate for enterprise.

The South African tax-paying public in general, and its entrepreneurs in particular, perceive the current levels of personal and company taxes as too high compared to the public benefits they perceive to flow from government expenditures, and to the levels of such taxes in other middle income countries.

Such negative attitudes should be seen in conjunction with other aspects of investor uncertainty. The index of business confidence compiled by the Stellenbosch Bureau for Economic Research has shown a huge decline in recent years. From the start of the present recession in 1989, this index has declined by 76 per cent, and is currently below levels experienced in the midst of the foreign debt crisis of 1985.

Figure 3: Manufacturing business confidence (BER survey results)
From the mid-1980s, numerous factors have undermined investor confidence in the South African economy.

These include economic factors relating to foreign markets and foreign participation, domestic economic conditions and economic policy.

Many of the markets for South African products are shrinking and during the last ten years the prices of several key products have contracted in both real and nominal dollar terms. Perceptions arising from the debt standstill and domestic security also act as a barrier to foreign participation in the South African economy.

Much of this uncertainty obviously stems from the present unprecedented process of political and constitutional change. Businessmen and investors find it virtually impossible to quantify the risks involved in the fundamental shifts in the political framework. Investments in new ventures are accordingly postponed until there is greater clarity.

2. STRUCTURAL DEFECTS

Various market inefficiencies hamper the performance of the South African economy. The key inefficiencies are structural distortions due to inflation, the tariff structure, exchange control, adversarial industrial relations, uncompetitive price determination practices, and excessive involvement of government in the economy.

2.1 An endemic inflationary climate

The structural distortions caused by the inflation mentioned above undermined economic performance in South Africa in a variety of ways. Economic agents found it difficult to distinguish between relative and absolute price movements. This hampered planning, investment, the allocation of resources and economic growth in general. Inflation hedges such as real estate attracted a disproportionate amount of investment funds.

Inflation also distorted the distribution of income, assets and liabilities in a most unhealthy and unfair way. For instance, elderly people living off a fixed nominal income faced a severe decline in living standards through inflation, while fiscal drag redistributed real income from taxpayers to the government. In combination with the tax system, inflation undermined the magnitude of savings and artificially influenced the forms in which savings took place, creating unlevel playing fields and boosting or penalising entire industries.

2.2 Excessive government claims on scarce resources

As noted earlier, the claim on the nation's scarce resources by the general government has risen inordinately in recent years. In 1989 (the most recent year for which internationally comparative figures are available) real government consumption expenditure as a percentage of GDP was 5.8 percentage points higher than the average for countries in the middle income group, and even 0.8 percentage points higher than the average for high income countries. This excessive claim on resources was also reflected in government's employment of available high level manpower. In 1991, the general government employed no less than 42.2 per cent of this category of manpower. (This figure is, however, influenced
by the fact that government employs 91.7 per cent of the teaching profession and 59.0 per cent of the medical profession.)

The functional distribution of general government expenditure changed considerably in recent years - away from defence in favour of social services (which in recent years already constituted about 40 per cent of the total). Daunting problems of re-allocation and reduction arises if, as intended, total expenditure on social services is to be kept at around 14 per cent of GDP (as they were in 1990/91) while total general government expenditure as a percentage of GDP has to decline considerably from its currently excessive levels of more than 30 per cent.

2.3  **Distortive and excessive protection**

International experience over the past decade and more has shown that countries with strongly export-orientated economies perform significantly better than those which rely on import replacement and high protection. Growth in world trade exceeds growth in wood production, which indicates that countries are relying on international trade to an increasing extent to improve their own economic performance.

South Africa, in contrast, has a long tradition of import replacement, which has created an inward-looking industrial base. The potential for further inward-looking industrial development is, however, limited and this has resulted in stagnation in South African industry. Much of the country's future prosperity will, accordingly, be determined by its ability to play a bigger role in international trade in industrial goods.

The dominant policy base for industrial protection in South Africa is its system of import taxes. The tariff barrier stands at 21 per cent (weighted by import values) which rises to 27 per cent when the protective effect of the special import surcharges still in force is added. The surcharge, which was introduced in 1988 as an alternative to a further depreciation of the exchange rate, should have been removed when the heavy pressure on the reserves abated. Unfortunately, it has become a source of fiscal revenue which the fiscus finds difficult to do without, or replace, in present circumstances, while the balance of payments constraint still lurks in the background as long as the net outflow of capital continues.

Thus, while the normal tariff barrier of 21 per cent is comparable to the protective levels found in developing countries, the 27 per cent level puts South Africa amongst the highly protected countries in world trade.

Moreover, the rather ad-hoc process of granting tariff protection to individual industries over many years has given rise to a system which is apparently one of the most complex in the world. It lacks transparency, is prone to continuous change and is open to lobbying.

Apart from the surcharge mentioned above, there are particular objections to the so-called "formula duties". These complex duties were introduced to protect local firms from "disruptive" competition, but their application has often resulted in increases in the general level of protection.

A high degree of selectivity that has resulted in wide variances in nominal and effective tariff rates between products and industries, as illustrated in Table 2, has also made the system economically distortive and arbitrary. These effects manifest themselves mainly in two closely related ways. Firstly,
they raise the relative costs of producing internationally tradeable goods in South Africa (a general cost-
increasing bias), and secondly, they reduce artificially the cost competitiveness of South African goods
in export markets (a specific "anti-export bias").

**Table 2 - South Africa: Estimates of Effective Protection**

<table>
<thead>
<tr>
<th>Subsector</th>
<th>Protection on</th>
<th>Effective Protection</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>Inputs %</td>
<td>Output %</td>
</tr>
<tr>
<td>Food, beverages and tobacco</td>
<td>15.2</td>
<td>13.7</td>
</tr>
<tr>
<td>Textiles, apparel and leather</td>
<td>27.8</td>
<td>43.6</td>
</tr>
<tr>
<td>Wood and wood products</td>
<td>14.0</td>
<td>21.7</td>
</tr>
<tr>
<td>Paper and paper products</td>
<td>9.5</td>
<td>13.3</td>
</tr>
<tr>
<td>Chemicals</td>
<td>7.5</td>
<td>18.9</td>
</tr>
<tr>
<td>Non-metallic minerals</td>
<td>5.2</td>
<td>19.8</td>
</tr>
<tr>
<td>Basic metals</td>
<td>4.7</td>
<td>11.2</td>
</tr>
<tr>
<td>Metal products and equipment</td>
<td>17.1</td>
<td>18.2</td>
</tr>
<tr>
<td>Other manufacturing</td>
<td>2.8</td>
<td>10.9</td>
</tr>
<tr>
<td>MANUFACTURING</td>
<td>12.6</td>
<td>17.8</td>
</tr>
</tbody>
</table>

Source: IDC

By its nature the protective tariff system allows producers to charge higher prices in the domestic
market than they could charge on exports to world markets. Accordingly, producers become only
marginally interested in export sales and the South African export performance in manufactures improves
only when domestic demand is substantially depressed. The latter has, in fact, been the case since the
debt crisis of 1985. Unless a more efficient cost-price environment replaces the present system of
protection, any domestic-led recovery of economic activity in South Africa will almost inevitably produce
a deficit on the current account and/or a serious depreciation of the rand exchange rate. The likelihood
of such a deficit being financed from inflows of foreign capital is slight. An export-led recovery,
however, requires at the very least the removal of the present "anti-export bias" in the system of industrial
protection.

Finally, for a number of reasons, including the underpricing of the user cost of capital relative
to the cost of labour up to the late 1980s and the special supports extended to the chemical and related
industries, South Africa's international comparative advantages presently seem to emphasise capital
intensity, while the relative scarcities of capital and labour in the country indicate that the pattern of
industrial development needs a broad emphasis in the opposite direction. This requires that the training
of manpower will have to figure prominently in the long-term economic strategy. An important defect
is the neglect of the training of workers in South Africa. It has been estimated that this country spends
only 2 per cent of total GDP on training compared to about 5 per cent in other countries.
2.4 The dual exchange rate system

The existence of exchange control and the dual exchange rate system with different rates for the "commercial rand" and "financial rand" has led to serious distortions in the South African economy.

* It bottles up domestic liquidity and artificially distorts the domestic interest rate pattern and asset prices.

* Exchange control discourages an inflow of direct investment funds in a world environment characterised by the phasing out of these controls, particularly in recent years.

* The system may be injudiciously used to protect unduly and overvalue the exchange rate of the rand at times (such as in the early 1980s) when more fundamental and sensitive fiscal and monetary adjustments to the growing domestic inflation are required.

* The entire exchange rate system requires a huge administration and policing effort.

However, the present environment of political uncertainty and instability in South Africa necessitates some kind of intervention of this nature for the time being. The financial rand system is also indispensable while the debt standstill lasts.

2.5 Adversarial industrial relations

The participation of labour in the growth process in relation to the rate of new capital formation or net investment has deteriorated alarmingly in recent years. For example, between 1973 and 1979, new capital formation amounted to about R 80 billion (at 1985 prices) while about 700,000 jobs were created. Between 1985 and 1992 net investment amounted to R 26.3 billion while the number of jobs declined by 150,000. As a result, the number of people unable to find work in the formal sector of the economy rose by some 2.5 million during this period. If present trends continue those in formal work will soon become the minority of the total labour force.

Much of this situation is due to the rising labour costs per unit of output, noted above. The trend is partly due to the labour cost increasing effect of the social system (discussed below), and partly to the currently adversarial relationships in the existing system of collective bargaining about terms of employment. These industrial relations inter alia determine the perceived costs of manpower in relation to the perceived cost, of capital and eventually the relative attractiveness of capital or labour in choosing new industries and new technologies.

The cause of this defect in the system is largely laid at the door of the present centralised bargaining system as bolstered by the institution of industrial councils. Competition under this system is largely eliminated. Employers will usually pass wage increases on to consumers in the form of higher prices. In some industries the "tacit collusion" is taken one step further by employers and unions attempting to eliminate foreign competition, usually at the expense of consumers and downstream industries.

The general government's own remuneration practices are also highly centralised. Centrally determined increases in remuneration seldom take into account differences in productivity, levels of responsibility and cost of-living for different geographic areas.
The system also seems to impede the development of small and medium-sized businesses in the sense that the peculiarities of their requirements are not taken into account in industrial settlements on national or industry level. As is well-known, however, these types of businesses have a stronger than average potential for job creation.

Figure 4: Capital/labour ratio

Note: The problems identified in this field relate mainly to manpower below the ranks of highly professional skills. Demand for the latter generally shows a positive relationship with capital formation.

2.6 Non-competitive price determination

Over-recovery of input costs by producers and distributors in their output prices is a common practice in South Africa. This practice not only fuels inflationary trends, but because the scope for such practices occurs unevenly throughout the economy, it seriously distorts cost-price relationships. Restrictive practices, collusion, standardisation of professional fees and of escalation clauses in tenders and monopoly pricing are other examples. Market efficiency is also undermined by various kinds of unnecessary costs incurred by businessmen in their efforts to deal with government rules, regulations and discretionary powers, all of which require cumbersome and often complicated procedures. Entire professions, charging considerable fees, have arisen within such frameworks.

The manner in which government determines the prices of goods and services produced in the public sector, also often fails to comply with sound cost-benefit principles. These so-called "administered prices" represent a substantial proportion of total pricing in South Africa.
3. SYSTEM DEFECTS

To establish an adequate level of sustained economic growth, the restoration of market efficiency has to be supported by a rapid improvement in the capacity of, and opportunities for, the large developing sector of the country to participate beneficially in the process. This "development condition" for growth is, however, currently constrained by defects in the political, economic and social system. These relate mainly to inappropriate education and training, costly functional and physical separation of people, inadequate access to economic opportunities, unsettled community life, inadequate entrepreneurship and ineffective financial intermediation between savings and development investment.

3.1 Inappropriate education and training

The relatively high aggregate expenditure on education and training contrasts sharply with the poor performance of education according to acceptable criteria. This is due to the fact that aggregate expenditure still conceals wide racial and spatial disparities in access to, and quality and utilisation of education. This inefficient expenditure on education and training has impaired the capacity of a large proportion of the population to participate effectively in the mainstream economy. Furthermore, the very limited supply of high-level manpower serves as an important constraint on economic growth and on an improved distribution of income through the market mechanism.

The most disturbing features of the current education and training profile are the following:

* Almost 60 per cent of the economically active population is considered as functionally illiterate. The dropout rate is high, particularly among Black students. Among the latter, the percentage of Sub-A entrants in 1980 who reached Standard 10, was only about 30 per cent. (This was, nevertheless, a considerable improvement on the figure of about 10 per cent, a decade earlier!) Only 13.4 per cent of Standard 10 students studied natural sciences and 23.6 per cent mathematics. Training activities have declined, as illustrated by the 38.6 per cent decline in the number of people acquiring artisan status between 1984 and 1991;

* The administration of the education system in South Africa is characterised by fragmentation and duplication. The system for Blacks, while being upgraded, also suffers from inadequate resources, such as classrooms, teaching aids and properly trained teachers; and the culture of learning among parents and children, on the one hand, and teachers, on the other hand, has deteriorated - to the point of collapse in certain urban areas;

* On the demand side, there are clear indications of a structural decline in the demand for lesser in relation to higher skills. The ratio of semi-skilled to high-level manpower declined from 10.8 : 1 in 1981 to 6.9 : 1 in 1990. The middle-level to high-level manpower ratio showed the same tendency by declining from 5.4 : 1 in 1981 to 4 : 1 in 1990. The ratio of unskilled occupations to artisans and production workers declined from 4.9 : 1 to 3.4 : 1 in the respective years, while the ratio of semi-skilled to middle-level manpower remained constant.

3.2 The costly functional and physical separation of people

The apartheid system imposed a functional and spatial separation of people on the economy which not only limited their productive participation in the mainstream market economy, but also introduced huge excess costs of several kinds on such participation as may have been allowed. The
process of economic growth of the Republic of South Africa, was not perceived to depend more than marginally upon the presence of the "urban blacks". Accordingly, the economic waste of township social arrangements, the absence of property rights, the high cost to workers of commuter systems, etc., were overshadowed by problems of financing outlays on housing the "temporary sojourners" and the cost of other elements of administering their presence.

As the apartheid paradigm is replaced by the new paradigm of an economically integrated society, these very inefficient and costly social, physical and administrative arrangements are vividly exposed. Moreover, the continued existence of this arrangement is seriously constraining the productive participation in the mainstream economy of the 11 million urban people concerned. Specific examples are:

* Over one half of the black population residing in or around South Africa's largest industrial centres reside in circumstances that lead to a fragile social fabric susceptible to violence and crime. Moreover, these conditions inhibit the development of a stable industrial culture, associated with regular work, a propensity to seek material advance through productive employment, business enterprise, saving and profitable investment.

* Workers and their families are often confined to residential-only townships located dozens of kilometres from industrial areas. This leads to high transport costs for firms, for government (via transport subsidies) and for the labour force. Accordingly, labour costs to firms are raised substantially without any increase in the real earnings actually received by workers. Furthermore, the productivity and quality of life of the labour force is reduced by the time and energy wasted on long hours of commuting.

* The barriers to access to home-ownership inhibit abilities to save, to hedge against inflation and to gain security in both the social and the commercial sense.

* The separation of white and black living areas, and past state discrimination against black informal economic activities in cities, discouraged small-scale and informal economic activities in South Africa by separating the market linkages between suppliers and their prospective clients.

* Other barriers include extensive regulatory interventions in terms of factors such as zoning practices, health regulations, licensing and registration practices and procedures, building standards and pricing practices. Many of the laws, rules, regulations and intervention practices by government agencies are either unnecessary or unnecessarily cumbersome. These practices not only waste public resources and create barriers to access but also create excessive transaction costs for the private sector.

* Many private sector practices also effectively constrain small entrepreneurs' entry to markets and support services. Financial intermediation between formal institutions and entrepreneurs in the small enterprise sector has only recently started to occur on a sustainable basis. Most institutions in the services and distribution sectors are geared to serve the needs of larger enterprises.
3.3 Ineffective financial intermediation

The institutional system governing the flow of domestic savings and foreign investment towards domestic capital formation in South Africa is highly developed in both the public and private sectors. The intermediation is also performed with a degree of efficiency comparable to the position in many industrial countries.

From the point of view of the aims of the normative model, however, the structure of the system may not prove flexible enough to bring about the required changes in the channelling of savings in the direction of enterprises with the greatest potential contribution to real income and employment creation. In recent years, investment in assets which offered superior hedges against inflation and maximum tax avoidance attracted substantial proportions of the available savings.

The South African private banking system is, moreover, highly geared to conventional commercial finance through their loans and advances, while merchant banking concentrates mainly on business connected with the financing or restructuring of large organisations with proven track records.

These circumstances leave a gap in the institutional system with regard to the financing of innovative ventures by smaller independent businessmen, creating added output and employment but requiring higher-risk capital. This gap cannot be adequately filled merely by the existence of the Industrial Development Corporation and the Small Business Development Corporation. It needs to be filled in particular through innovation and deregulation in the private financial sector.

3.4 Inadequate entrepreneurship in the formal economy

While innovative entrepreneurship is an essential ingredient of rapid economic growth, its presence in a community is always difficult to measure. Nevertheless, there is a prevailing impression that the South African economic community, more particularly in the formal ("first world") economy, lacks a widespread spirit of industrial innovation, i.e. to enter new markets, to research and apply new technology and to seek new avenues of production. On the contrary, most young people in this community aspire to positions offering job security and social status. Many of those with greater ambitions have tended to seek careers in financial or professional services.

The reasons for this situation may be found in a wide array of institutional circumstances in the country, ranging from the attitudes of its financial institutions to the nature of its education and training and its tax system. These mostly boil down to the fact that risks of insolvency for independent unconventional ventures are normally perceived to be too high relative to the rewards of conformity within large and financially strong organisations.

4. GROWING INTERNATIONAL COMPLEXITIES

South Africa faces a world economy characterised by increasing integration, regional trade bloc formation, vigorous competition for export markets and capital, as well as declining commodity prices in relation to that of manufactured exports.
4.1 Growing global integration

Since the 1980s, world trade has grown steadily in relation to world output, while the mobility of capital has increased, due to improved communication systems and international financial deregulation. Negative foreign perceptions of any country's domestic economic, social and political developments are often costly in terms of immediate capital flight. National autonomy over traditional economic policy levers are weakened as international imperatives have an increasing influence on national economic policy decisions.

4.2 Creation of major trading blocs

Major trading blocs are being established, in North and South America, the Far East, and the expanding European Community (EC). While market efficiency is improved within the borders of such trading blocs, due to a free flow of resources, goods and services, protective barriers are usually created against outsiders. South Africa is not party to any trading bloc except for the Southern African Customs Union (SACU). An important aim must be to re-establish closer links with the EC.

South African industries may have some competitive advantage in trade with African countries, as reflected by the increase in manufactured exports to this region in the past few years. Furthermore, there are also many gains to be had from implementing and managing infrastructure projects, technology transfer and the tourism industry. The active exploitation of these markets by South African businesses, especially small and medium enterprises, could have significant benefits.

4.3 Intensifying international competition

Competition in world export markets is not based only on price. Industrialising countries in the Far East outperform their counterparts in trade and economic growth by means of aggressive export-oriented policies. These policies, supplemented by policies aimed at a stable domestic macro-economic environment, support continuous improvements in their international competitiveness and penetration of export markets. The mature industrialised countries often adopt a defensive attitude to protect their domestic industries and employment, usually through non-tariff measures. The implication for South Africa is that its export drive will face tough price and quality competition in every world market.

During the 1990s, South Africa will also be forced to compete for foreign capital with countries offering reasonable socio-political stability and acceptable returns to foreign investors, e.g. Latin America, Eastern Europe and East Asia. Foreign capital inflows, particularly direct investment, will not materialise without a consistent set of economic policies providing for a promising long-term investment climate.

4.4 Deteriorating terms of trade

The South African economy relies heavily on commodity and resource-intensive exports and technology and skill-intensive imports. The deterioration in the terms of trade since the mid-1970s has depressed the growth potential of the economy. An over-supply of commodities worldwide is expected to maintain downward pressure on the terms of trade.
Figure 5: Terms of trade

Index: 1985=100. Gold excluded
A SUGGESTED BASIC STRATEGY

The normative economic model upon which the proposed strategy is based, essentially aims for:

* a specific rate of increase in the amount of investment in relation to GDP over the next five years,

* a specific rate of increase in the productivity of investment in terms of both more output and more employment for a given amount of investment, and

* the re-establishment of a stable financial environment.

These policy aims imply that the private sector and market forces should be responsible for a much larger proportion of total fixed investment. Investment in private manufacturing in particular, is expected to increase from 3.5 per cent of GDP in 1992 to 5.3 per cent of GDP in 1997. In absolute size, this represents an increase of about 80 per cent (in real terms) between the year 1992 and the year 1997.

The basic ideas are graphically presented in figure 6.

Highlighted in the graphic presentation is the need for greater productivity of investment. Thus, as against the present average capital/output ratio of 3.1 : 1 the model requires that over the next five years no more than 1.7 units of additional capital should in the aggregate be required to produce an additional unit of output.

Similarly, as against the present ratio of labour employed to the fixed capital stock, the model requires that over the next five years 38 per cent more workers should be employed per unit of additional capital employed.
Figure 6: An outline of the basic strategy

**Market responses**

### More investment

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<th>1992</th>
<th>1997</th>
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<tbody>
<tr>
<td>Investment/GDP</td>
<td>15.9%</td>
<td>23.1%</td>
</tr>
<tr>
<td>Public sector investment/GDP</td>
<td>4.5%</td>
<td>7.8%</td>
</tr>
<tr>
<td>Private sector investment/GDP</td>
<td>11.4%</td>
<td>15.3%</td>
</tr>
<tr>
<td>Private manufacturing investment/GDP</td>
<td>3.5%</td>
<td>5.3%</td>
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### Greater productivity

<table>
<thead>
<tr>
<th></th>
<th>1992</th>
<th>1997</th>
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<tbody>
<tr>
<td>Lower capital/output ratio</td>
<td>3.1%</td>
<td>1.7%</td>
</tr>
<tr>
<td>Labour/capital ratio index</td>
<td>100</td>
<td>138</td>
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<tr>
<td>Improved multifactor productivity</td>
<td>-3/4%</td>
<td>1 1/4%</td>
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**Constraints**

- Financial discipline
- Tax relief
- Less government
- Industrial reform
- Improved market structure
- Socio-economic reconstruction
- Urban reconstruction
- A safety net

**Performance of the economy**

<table>
<thead>
<tr>
<th>GROWTH</th>
<th>1992</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP</td>
<td>2</td>
<td>4 1/2</td>
</tr>
<tr>
<td>Employment</td>
<td>3</td>
<td>3</td>
</tr>
</tbody>
</table>

(1) Preliminary estimates
(2) Incremental ratio 1992-1997
Correspondence between constraints and strategies

A crucially important matter for critical evaluation is, of course, the effectiveness of the suggested strategies, identified below, to achieve the stated objectives or to remove the constraints preventing the market-economy to achieve such objectives. This is a matter for detailed economic analysis which has not been attempted in this memorandum. Nevertheless, a broad correspondence between the several strategies and the several constraining realities discussed above, is suggested in figure 7. Economic analysts, of course, realise that "in economics everything depends upon everything else".

There is obviously a presumption in the model that the strategies envisaged would, as a total package, succeed. The theory behind the presumption is important. This is that market orientated economic systems do better than centrally planned ones, and that participants in market systems do better when their freedom of decision is not directly curtailed, but at most indirectly guided. By the same token, however, removing the unnecessary shackles and introducing the necessary incentives cannot with absolute certainty guarantee the outcome. That depends crucially on the responses of the participants in the economy.

Figure 7: Correspondence between constraints and strategies

<table>
<thead>
<tr>
<th>Constraints</th>
<th>Strategies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Functional imbalances</td>
<td>1 - Financial discipline</td>
</tr>
<tr>
<td></td>
<td>2 - Tax relief</td>
</tr>
<tr>
<td>Structural defects</td>
<td>3 - Less government</td>
</tr>
<tr>
<td></td>
<td>4 - Industrial reform</td>
</tr>
<tr>
<td></td>
<td>5 - Improved market structure</td>
</tr>
<tr>
<td>System defects</td>
<td>6 - Socio-economic reconstruction</td>
</tr>
<tr>
<td></td>
<td>7 - Urban reconstruction</td>
</tr>
<tr>
<td></td>
<td>8 - A safety net</td>
</tr>
</tbody>
</table>

1. **FINANCIAL DISCIPLINE**

Macro-economic discipline primarily entails fiscal discipline, in the sense that government should live within the limits which taxpayers can afford and which can be sustained, monetary discipline and a stable financial environment of low inflation. The attainment of such a state of affairs is crucial to the success of the strategy.
1.1 Fiscal policy

Central to the fiscal reform package is the elimination of dissaving by the general government; in other words, the balancing of current revenue and current expenditure. Government is to borrow only in order to finance capital expenditure, and not to fund current expenditure.

Table 3: Fiscal discipline

<table>
<thead>
<tr>
<th></th>
<th>1992</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>General government dissaving percentage of GDP</td>
<td>4.8</td>
<td>0</td>
</tr>
</tbody>
</table>

Elimination of dissaving by the government fits into the programme framework in the sense that it will:

* free resources, which are at present being borrowed for current government expenditure, for productive investment;

* prevent the government debt from rising to levels where the growth in such debt, and the interest on it, becomes unsustainable;

* reduce the inflationary impact of fiscal policy, thereby contributing to lower inflation and a stable financial environment;

* indirectly lead to a stronger balance of payments position.

In accordance with the medium-term nature of the proposed reform programme, government dissaving should be phased out and eliminated by 1997. A firm but gradual process is proposed to avoid the considerable disruptions and abrupt shifts in demand and supply which may be expected if dissaving were to be eliminated immediately.

Discipline in government salaries and wages would be a necessary component in eliminating government dissaving and attaining macro-economic stability. Such discipline, given the number of government employees, would also filter through to private sector salaries and wages. Government’s salary and wage policies should however be sufficiently flexible and market-related to counteract outflows of crucial skills from the service.

Government use of central bank credit in order to finance its expenditure is ruled out, given the highly inflationary effects of such action. Use of credit from the private banking sector should be restricted to bridging temporary shortfalls in exchequer issues and receipts.
1.2 Monetary policy

Achieving and entrenching a stable financial environment of low inflation is of special significance to the programme of restructuring. In view of the considerable lags in monetary policy, from the stage when a policy instrument is applied until its effects have filtered through to the economy and inflation, the recommended style of monetary policy is orientated towards the medium- to long-term. The ongoing independence of the Reserve Bank is necessary for it to follow a monetary policy which serves the longer-term needs of the country, without undue weight being given to the short-term considerations which may often be the focal point of the government of the day.

The Reserve Bank’s mission, to protect the internal and external value of the rand, compels it to combat inflation. The Bank does this mainly by controlling and lowering the rate of growth in the money supply. The Bank discourages the undue creation of money through its discount window by quoting rediscount rates for accommodation which may generally be expected to remain positive in real terms. As money supply growth is kept under control, inflation may be expected to continue its decline. This would create further scope for lowering nominal interest rates without unduly risking a rebounding of money supply growth and inflation.

Table 4: Monetary discipline

<table>
<thead>
<tr>
<th></th>
<th>1992</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disciplined money, supply growth,</td>
<td>7 - 10</td>
<td>6 - 9</td>
</tr>
<tr>
<td>contributing to lower inflation,</td>
<td>16.2 - 9.6</td>
<td>3 - 6</td>
</tr>
<tr>
<td>&amp; to lower nominal interest rates</td>
<td>20% → 17%*</td>
<td>7 - 10*</td>
</tr>
</tbody>
</table>

* Prime rate

Given a policy of domestic financial stability and relatively slow money supply growth, the effective exchange rate may also be expected to reflect the elimination of the gap in inflation rates between South Africa and its leading trading partners.

2. TAX RELIEF

A key element in the proposed strategy is the lowering of the overall tax burden and a realignment of the tax structure. Both personal and company rates of taxation in South Africa are high in relation to other middle income countries, and even industrial countries. Lower tax rates would release more funds to be used in the private sector for more productive investment, and would also more directly reward greater productivity and efficiency.

The model envisages a reduction in **company tax rates** from 48 to 40 per cent. The overall revenue from company taxation is, however, not expected to decline in accordance with the nominal rate reduction. Many tax expenditures, allowances and special exemptions, (which reduced the effective rate of company taxation to levels far below the nominal rate) have been eliminated, which may narrow the gap between these two rates in future. Furthermore, in a growing economy total taxable profits will increase and raise more government revenue in a healthy and sustainable way.
<table>
<thead>
<tr>
<th>Table 5: Proposed tax adjustments</th>
<th>1992</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lower direct corporate taxation rates</td>
<td>48</td>
<td>40</td>
</tr>
<tr>
<td>Lower ceiling of individuals' marginal rate</td>
<td>43</td>
<td>50</td>
</tr>
<tr>
<td>Change in the tax structure (% direct)</td>
<td>55</td>
<td>50</td>
</tr>
<tr>
<td>Reduce the &quot;balanced budget&quot; tax burden (tax/GDP)</td>
<td>30.7</td>
<td>24.4</td>
</tr>
</tbody>
</table>

**Individual taxation** is also to be restructured, with the ceiling of the marginal tax rate to be lowered from 43 to 40 per cent. Fair taxation of fringe benefits has already been phased in, addressing the gap between individuals' "nominal" and "effective" rate of taxation. Due attention to the elimination of fiscal drag is also proposed. Fiscal drag results from inflation when fixed income tax brackets are used to tax higher nominal income. The effect of fiscal drag is the reduction of real personal disposable income and therefore personal saving. Fiscal drag can be addressed through a reduction in the number of tax brackets, the continuous adjustment of the tax brackets to eliminate inflationary effects, and the proposed lowering of the maximum marginal rate to 40 per cent. These steps should lower the direct personal tax to GDP ratio to its 1984 level of 7.9 per cent. However, the most effective means to eliminate fiscal drag is to eliminate inflation.

**A shift from direct to indirect taxation** is a further important proposal. Direct company and personal taxes should be reduced, whereas indirect taxes like value added and excise duties should be increased. However, import duties - another form of indirect tax - should be lowered. This shift should aim to reduce the share of direct tax in total tax revenue from 55 per cent in 1992 to 50 per cent in 1997. This would contribute to higher productivity, as indirect taxes are neutral to the factors of production and in fact discourage consumption in favour of savings. They also do not tax effort to work harder, or increase the cost of labour relative to capital. A shift from direct to indirect taxation can create higher savings which will expand the scope for investment.

The average tax burden (tax/GDP) increased from 21 per cent in the period 1979 to 1985 to 25 per cent during 1985 to 1991. This was not only the result of higher public expenditure, but also a result of the weaker economic performance which eroded the tax base. It furthermore had a negative influence on saving and the investment climate, not only directly but also through inflationary pressures. It is therefore essential to reduce not only the direct tax burden but also the **total tax burden**. This implies that the additional income derived from indirect tax increases should be lower than the amounts forfeited through direct tax cuts.

Given the constraint, imposed in the interest of fiscal sustainability, that government should not borrow in order to finance current expenditure, total tax revenue in 1992 should have amounted to some 30.7 per cent of GDP in order to equate current revenue and current expenditure of the general government. (Tax revenue in fact fell substantially below this level due to both cyclical and structural forces.) In terms of the proposed programme. The "revenue account balanced budget tax burden" is
to decline to 24.4 per cent of GDP by 1997. In that year, the general government’s current expenditure and revenue are to balance.

Given the need for a reduction in direct personal and company tax rates, it becomes vital that the public sector’s recurrent expenditures be curtailed, with due consideration to the need for better socioeconomic services for the less privileged. A well-structured and managed reduction in the growth of public spending during the next few years could widen the scope for higher economic growth, boost investor confidence and eventually broaden the direct tax base.

3. GOOD GOVERNANCE

Beyond the fundamental issue of restoring a social climate of peace and order, the next important qualitative improvement needed is the restoration of public trust in good governance. In the economic arena the style of government participation and control is to be thoroughly reviewed to conform maximally to the principles of accountability, transparency and consistency. These well-known principles will guide the implementation of the programmes of government action elaborated in the following sections.

The agenda for reform includes a commitment by government to intervene less in the behaviour of the market mechanism, i.e. to “let the markets work”, and to act positively and effectively in those fields where markets cannot work. The latter refers mainly to programmes for providing social, physical and information infrastructure, such as education, training, health, transport networks and the underpinning of rural and urban settlement and small entrepreneurs, as discussed later.

This approach implies a dismantling of most of the government’s market participatory and regulatory machinery, which may result in considerable savings for the public sector and the formal and informal private sector, and a reduced bureaucracy. Figure 8 depicts the extent of the structural change in employment envisaged in the model.

Figure 8 - Indices of employment
Regarding social expenditure, it must be reiterated that in comparison with international norms, South African expenditure on these services substantially exceeds the averages for both developing and developed countries. The problem is rather the effectiveness of these outlays in terms of the benefits to the communities involved. Without any further increases in outlays on revenue account, the performance of these programmes can be considerably improved by appropriate rationalisation. This will be undertaken with regard to both the efficiency of each service in its own context and the optimal distribution of resources among the services involved in terms of relevant development criteria.

The normative model does envisage a significant increase in total capital expenditure in the public sector over the next five years, namely from 4.5 per cent of GDP in 1992 to 7.8 per cent of GDP in 1997. Within these limits, capital outlays by general government may well rise from its present 1.7 per cent share of GDP to between 2.3 and 3.0 per cent of GDP in 1997.

A major obstacle in this respect is the weaknesses in the public sector financial system that supports development. The system is plagued by a lack of coordination and inefficiencies and, in many instances, its constituent parts are hampered in the delivery of development support by financial, institutional and legitimacy problems. Various aspects of the fiscal and financial system in support of development should be reviewed, e.g. the developmental roles of and relationships between the public sector, private sector and civil society; the relationships between different levels of government and the relationship between development and public finance. At the same time, there exists a wide array of "non-governmental organisations" whose functional capacity could be improved to play a greater role in the effective investment of resources becoming available in future.

Considering the state of the business cycle, and a possible lag in the revival of private investment, scope might arise within the limits envisaged for some acceleration in time of public investment. However, the eventuality that private investment does not pick up sufficiently to avoid an unnecessary prolongation of the recession, should be discounted at this stage. Such scope as, nevertheless, might arise should be used for projects with maximum employment effects.

4. SMARTER INDUSTRIES

4.1 The importance of industrial development

The South African economy can only achieve the envisaged GDP growth performance by becoming fully competitive in internationally tradeable goods and services in categories where its terms of trade is not structurally declining. The country's private manufacturing industries are expected to play a rapidly increasing role. As mentioned earlier, the projections in the normative model imply an increase of about 80 per cent by 1997 in the annual level of private manufacturing investment over that realised in 1992.

Such an investment thrust would have to be justified by confidence in the international competitive advantages of the industries involved. According to the normative model of every R 100 in additional manufacturing production between 1992 and 2000, R 23 should be exported, compared with a current average export level of R 10 out of every R 100.

Apart from the need for South African industry to become internationally competitive, a growing export propensity will be required to pay for the expected rapid rise in imports of intermediate inputs and capital goods following the envisaged growth in domestic capital formation. There may be a chance
that a revival of economic growth will attract foreign investment, thus easing the pressure on the balance of payments, but unless this growth is export-led foreign investors are unlikely to be greatly interested.

4.2 The approach

The daunting problems facing a successful breakthrough in this respect have already been described in this memorandum. They were basically 1) the current lack of stability, efficiency and growth in the domestic economy; 2) the fact that the pattern of international comparative advantages in the current composition of South African industry seems to be diametrically opposed to the relative availability of labour and capital in the country; and 3) the fact that the very large ratio of unskilled to skilled labour poses a serious problem in its own right.

The strategy required to bring about the desired structural adjustment, accordingly, has to be based on a reform programme of the classic kind to remove the domestic inflation and inefficiency through fiscal and monetary discipline (as proposed above), and through the rationalisation of industrial protection removing its inflation and anti-export bias, as proposed below. This strategy has to be maintained until the economy is purged of the distortions of the past decades.

However, the large discrepancy between the current composition of industry and the need for employment, calls for great caution. The downward adjustment of the general level of protection (as envisaged below) may fall heavily on the relatively highly protected labour-intensive industries. Yet in the longer-run much of the growth strategy depends upon the future improved productivity and growth of these industries. It would accordingly be wrong to allow these industries to collapse under the strain of the general adjustment before the stage in the structural adjustment is reached when these industries should naturally turn out to be among the relatively more promising ones.

The facts of the current situation, accordingly, also call for temporary adjustment assistance on a selective basis during the transition. However, it should be emphasized that no selective discretion applied by the government agencies concerned should take forms which contradict the basic principles of the general structural adjustment programme.

The extent to which selective assistance to particular industries will be needed, depends largely on the tempo at which policies such as the phasing out of exchange control, the lowering of tariff protection, cooperation in wage bargaining, price competition and fiscal and monetary discipline in general are realised. Progress in these areas would reduce and possibly even eliminate the need for selective assistance to industries with a proven competitive advantage, such as in agriculture, mining and minerals beneficiation. The instruments to be used in such a selective approach should be applied over a broadly defined spectrum of more advanced industries, probably mostly category 3 and 4 products of the GEIS, and should meet the criteria of investment, employment and efficiency in their impact on development.

4.3 Elimination of the anti-export bias in materials procurement

Exporters suffering from and "anti-export bias" should be able to access intermediate inputs at the best available world prices. This would be an important step in eliminating the anti-export bias and in supporting the competitiveness of more labour-intensive and small to medium sized export firms. The following options may be exercised in this regard:
* the establishment of "Export Processing Zones" or "Free Enterprise Zones";

* upgrading of the drawback and rebate of duty system for imported materials used in export processing, on an automatic basis or as closely automatic as possible; and

* strengthening and expanding the informal arrangement whereby suppliers offer material inputs at world-related prices to manufacturers for their export business. (The supply of material inputs at world prices will be strengthened when the projects, being established with the help of Section 37E tax concession, eventually come on stream.)

4.4 Export Subsidies

Export subsidies are an imperfect and at best a partial solution to the elimination of the anti-export bias. Nevertheless exports, especially those of the so-called fully manufactured products (category 4 of GEIS), will remain dependant on them for as long as the protective system serves as a constraint on their competitiveness, or if and when movements in the real effective exchange rate displays an anti-export bias. However, the efficiency of export subsidies can be improved in conjunction with some other steps, particularly the rationalisation of the protective system, to be explained below. Delays in concluding the Uruguay Round of Trade negotiations may extend the legality of export subsidies up to the late 1990s.

4.5 Improvement of competitiveness in tradeables (including services)

Selective incentives to establish new industries and to revitalise and modernise existing ones are similar in nature and comprise of:

* lower company tax rates and the provision of finance by development agencies such as the Industrial Development Corporation and the Small Business Development Corporation. These incentives should be available for modernisation of production facilities, expansion of existing industries or the establishment of new industries and for working capital to introduce multi-shifts, and to take advantage of development opportunities;

* fiscal support for training and re-training schemes to improve the international competitiveness of the country’s human resources; and

* fiscal support for applied technological improvements.

These measures will not be limited to the enlargement of the export capacity but will also extend to certain industries with a potential competitive advantage in general and seriously affected by the rationalization of the protective system. Task Groups for this purpose have, for example, been established for Textiles and Clothing, Motor Vehicle Manufacturing and the Electronics Industry. Others may follow in due course.

4.6 Assistance with entry into world markets

Market entry into export markets of goods and services is assisted through the Export Marketing Assistance Scheme (EMA).
South Africa's market entry on a multilateral basis is safeguarded by compliance with its obligations as a member of the General Agreement on Tariffs and Trade. According to the Uruguay Round of trade negotiations South Africa is required to reduce its tariff protection. Standard practice is that the reduction in tariffs can be phased-in over a period of five years in five equal annual instalments. It is possible to negotiate a longer phasing in period.

Successful conclusion of the Uruguay Round of trade negotiations will result in the establishment of the Multilateral Trade Organisation (MTO) which will consist of three separate divisions: the General Agreement on Tariffs and Trade (GATT). The agreement on Trade Related Investment Measures (TRIMS), and the General Agreement on Trade in Services (GATS).

Membership of the MTO will require unconditional compliance to all of the agreements. The implication is that member countries will have less leeway for discretionary actions than before. For South Africa this would mean closer compliance with multi-lateral agreements than in the past. A category affected may be those incentives discriminating openly in favour of exports.

However, negotiation of a reclassification of South Africa's status in the GATT (MTO) from "developed" to a "developing country" may benefit market entry, especially with regard to the emerging trading blocs around the world. This may also allow for extended grace periods for subsidies and other discriminatory incentives.

4.7 Removal of import surcharges

The much criticised import surcharges imposed in 1988 have already been reduced and government is willing to repeal them as soon as its fiscal situation allows it. To the extent that import surcharges serve as a protective measure, their repeal would imply a reduction of the overall protective barrier from 27 per cent to 21 per cent, a reduction in costs and a major clean-up of the protective system.

4.8 Replacement of formula duties with suitable measures to counter disruptive competition

The repeal of the formula duty system is equally important. Formula duties serve to safeguard producers against dumping and disruptive competition but also normal competition from low cost producing countries, and they give rise to abnormally high protective rates for specific products and industries. Formula duties are to be replaced by anti-dumping measures against disruptive competition. This will bring South Africa's practices more in line with those found in other countries. It will also place South Africa in a better position to comply with the multilateral requirements of GATT.

Over the years highly protected industries have become reliant on the protection offered by formula duties. Progress with the rationalisation of the protective system is critically dependent on practical and suitable anti-dumping measures, which are effective in handling disruptive competition. The required systems have to be introduced urgently.

Elimination of formula duties could reduce the overall protective level by three percentage points. The combined effect of the repeal of import surcharges and the elimination of formula duties could be a reduction of the protective barrier from 27 per cent to 18 per cent.
4.9 Further rationalisation of the protective system

The third step in further rationalising the protective system would be:

* the completion of the tarification of the limited number of outstanding quantitative import restrictions,
* a review of the system of duty rebates, and most importantly,
* the standardisation and stabilisation of ad valorem duties.

The aim of the standardisation and stabilisation of the protective system is to reduce the number of tariff headings, eliminate the variations in nominal and effective rates and thus remove the selectivity and discretion that have been imbedded in the existing system. These steps should result in a neutral and transparent system.

A possible approach could be to reduce the maximum ad valorem rates on consumer goods to 30 per cent and on all other goods to 15 per cent. This would bring down the protective barrier to an average of 14 per cent. However, more research has to be undertaken to find suitable approaches, especially in the rationalisation of tariff rates below these maxima, to ensure neutrality in the effective protective rates between industries. Rationalisation of the protective system is urgent because of its implications for improved resource allocation, the rationalisation of subsidies and other export support measures and the neutralising of the anti-export bias.

5. EFFICIENT MARKET STRUCTURE

Apart from the positive impact the aforementioned measures are expected to have on efficiency in the South African market system, optimal market responses to the challenges of changing circumstances depend heavily on improvements in market structure. The particular defects identified in respect of both goods and factor markets, have to be addressed.

5.1 Effective competition in the product markets

Suggested steps to improve effective competition amongst suppliers in the market for goods and non-factor services, include:

* It has been proposed that direct government involvement in decisions about findings and recommendations by the Competitions Board be terminated, and replaced by an independent judicial system. The main institutions in such a system would be a Tribunal and a Special Court of Appeal in competition matters.

* Certain forms of anti-competitive behaviour, such as price-fixing, market sharing, resale price maintenance and collusive tendering should be outlawed in the Act itself and not by Government Notice, as is the case at present.

* Substantial administrative fines for anti-competitive behaviour.
Outlawing interlocking directorates between competing firms, or making it compulsory to disclose such positions to the public.

Streamlining appeal and other procedures.

The compulsory notification of all proposed acquisitions.

A much more critical view ought to be taken of acquisitions, restrictive practices, statutory entitlements and government concessions that create monopolies.

Clear rules and guidelines for government decisions about allegations of unfair competition with the private sector by parastatals and, if so, what the appropriate remedial action should be.

Reconsideration of the role of agricultural marketing boards.

5.2 Effective competition in the labour markets

If the aims of the model are to be met, net investment of about R 51 billion (at 1985 prices) over the next five years to 1997 will be accompanied by the creation of about 1,300,000 job opportunities in the formal sector. Such a performance is possible, but depends heavily on the well-targeted and accelerated development of human capacity, discussed elsewhere, and requires considerable improvement in the currently adversarial relationships in the existing system of collective bargaining about terms of employment. These industrial relations inter alia determine the perceived costs of manpower in relation to the perceived costs of capital and eventually the relative attractions of capital or labour in choosing new industries and new technologies.

Thus, to achieve the rate of employment targeted, real wage increases would have to be contained to 0.75 per cent per annum. Larger increases would lead to lower growth in output and employment and would jeopardise a central goal of the programme, namely to absorb the full increase in the labour force in gainful employment. Average real wage increases above 0.75 per cent per annum would only be justified if productivity increases were to exceed the 0.9 per cent per annum targeted in the programme.

The achievement of the great social objectives envisaged in the strategy depends crucially upon the way in which the several stakeholders in the process of determining wages and other working conditions apply their respective economic powers and meet their respective and mutual responsibilities.

The two major dimensions in the matter must be clearly acknowledged. On the one hand, wages and working conditions are of vital importance to the standard of living of the vast majority of people participating in the market economy. On the other hand, the cost of labour per unit of output relative to the price of outputs and costs of alternative resources, such as capital or imports (of the output concerned), is of vital importance to the revival of the viability of South African industry and trade.

The currently adversarial relationships in industrial relations must come to an end. The complementarity, rather than the conflict, in the interests of workers in an industry and the interests of the community at large should govern these relationships in the crucial period of economic restructuring ahead.
It is, accordingly, suggested that the reconstituted Manpower Commission in its forthcoming reconsideration of the legislation on industrial relations, seeks appropriate ways and means of introducing much greater flexibility in the determination of wage rates relative to productivity in particular industries and regions, and to the circumstances of employment in small businesses.

It is also necessary that the issue of training and retraining of labour by employers be thoroughly addressed.

### 5.3 The phasing out of exchange control

It is the intention of the government to phase out exchange control in due course. To ensure that the exchange rate is not exposed to volatile pressures due to non-economic influences on the capital account of the balance of payments, the authorities will ensure that each reform step is taken from a position of strength. This implies that:

* The gold and other foreign exchange reserves will first have to be built up to adequate levels.

* Domestic financial stability, including low inflation, will have to be attained and consolidated.

* The Interim Debt Arrangements will have to be replaced by normal arrangements.

* The flexibility of the South African foreign exchange market will have to be developed further, by allowing and expanding controlled wider ownership of foreign exchange in the hands of accredited domestic financial institutions and corporations.

Given the fluidity of the balance of payments and of South Africa’s foreign debt and gold and foreign exchange reserve position, it follows that no fixed dates can be set for the steps culminating in the final abolition of exchange control. Similarly, no specific order of reforms can be outlined, but periodic adjustments will have to be decided upon in the light of developments. However, progress has already been made with building up the net foreign reserves and reducing the rate of inflation.

### 5.4 Effective financial intermediation

A significant improvement in the processes of financial intermediation will follow from the adoption of the correct macro-economic policies, as outlined above. The removal of inflation, which in combination with the tax system distorts the allocation of funds, is a critical element in improving the efficiency of the financial system. Systems have also been put in place by the regulatory authorities to improve risk management practises in banking and other financial institutions. These systems are continually being reviewed.

Deregulation, innovation and competition in the private financial markets may be expected to contribute to greater efficiency and access by smaller businesses and poorer households in a variety of ways, as outlined below in paragraph 5.5.
5.5 **Support for small and medium enterprise and recognition of the worth of the informal sector**

The limited capacity of the formal economy to absorb the growing labour force necessitates additional strategies for job creation beyond mainstream growth incentives and macro-economic discipline. Strategies should be aimed at increasing the number of independent small and medium sized enterprises, expanding their share in GDP and improving the efficiency with which they do business.

Appropriate policies will differ somewhat between the informal and the small business sectors, Continued deregulation of this "business environment" is a key to improved efficiency of resource use, greater flexibility, lower costs and thus higher incomes.

With regard to the informal sector, in particular, attention should be given to their lack of secure space and shelter for operating sites and of essential utilities (power and water) and their means of obtaining relevant market information.

Additional strategies for the formal small and medium enterprise sector should be introduced:

* The private financial sector should explore possibilities whereby they can manage their risk in this market, in co-operation with development finance institutions. These might well include:
  - The development by private financial institutions of sound screening practices for the evaluation of applications for funding from small- and medium-sized enterprises.
  - Special incentives to encourage the involvement of private financial institutions in equity financing of small businesses.
  - The development of mechanisms to allow the softening or delay of the repayment of the initial instalments on loans.
  - The development of community banking mechanisms in which the pooled funds of the savers in a community are lent to borrowers in that same community, creating a spirit of self-help and identification with the developments achieved.

* An important role may be played in this regard by several development finance institutions. Burdensome aspects of tax and manpower legislation as well as so-called minimum standards, in all spheres of business, should be addressed.

* Government should be pro-active in identifying business opportunities with small enterprises e.g. through adjustment of the size of contracts and tender procedures enabling subcontracting to these enterprises.

* Arrangements which link smaller and larger business into mutually beneficial economic relationships should be encouraged through appropriate incentives. Larger businesses have many important contributions to make via financing, training, mentorship, spinning off corporate components which are potentially viable as small businesses, and subcontracting.
Skills training programmes available to small enterprises are insufficient and sometimes inaccessible to the users. The Department of Trade and Industry together with other role players should initiate a comprehensive business training programme.

6. PEOPLE PARTICIPATION

The strategy should ensure that growth does not falter due to a lack of inputs of high-level manpower and industrial skills while at the same time ensuring that the process of growth is of a high quality in terms of its social attributes. At the same time, human development is obviously an end in itself, encompassing, as it does, elements such as better education, higher standards of health and nutrition, more home ownership, less poverty and equality of opportunity.

The particulars of the various elements of a strategy for greater emphasis on developing the human capacity of the South African economy, are currently under review by government and in a number of discussion forums (such as the "National Economic Forum" and regional and local forums), where organisations concerned with civil society and development finance are also involved.

The main areas in which major improvements will have to be brought about, may be categorised as 1) rationalising education and training, 2) changing certain emphases in health services, 3) urban reconstruction, 4) rural reconstruction, and 5) reviewing the fiscal and financial aspects of these and related processes.

Apart from the fact that many of the issues concerned are still under review, it is impossible to do justice in a brief memorandum to the detailed and complex nature of many of these matters. However, a general overview of what is involved under each of the categories may be presented.

6.1 Rationalising education and training

Without raising the present relative claims by education and training on budgetary resources, its positive impact on the economy and society generally can be greatly improved. A critical improvement, for example, is the provision of free and compulsory education for at least the basic education phase (say nine years) for all South Africans. This is to take place within a unified education system that will ensure numeracy, literacy and other life skills. Another is the upgrading of training programmes emphasising entrepreneurial development, managerial capacities, youth pre-employment training and a national framework for standardising certification of competencies. Another critical issue is the restructuring of responsibilities and commitments of all stakeholders in education and training (e.g. of regional authorities, parents, pupils, teachers, private enterprise).

6.2 Health services

The critical issues in this category, from the point of view of their impact on economic performance, are duplication of functions and disparities in the allocation of resources between income groups, geographic areas, and types of health care service. A significant improvement is possible through a modest shift of resources from curative to preventive care and towards areas of greatest poverty. This, however, requires ready access to secondary and tertiary services. In this regard improved linkages between public and private sector care should make a valuable contribution. Improved availability of housing, sanitation and water, would likewise greatly support formal preventive care programmes.
6.3 Urban reconstruction

With more than 60 per cent of the country’s population and more than 80 per cent of its GDP concentrated in urban areas, the realisation of national economic policy objectives are highly dependent on improving the productivity of South Africa’s cities. Prudent macro-economic management establishes the necessary broad economic environment for urban economic activities, but it is not a sufficient condition for improving productivity at the urban level. The depressed urban property market, a vastly inefficient urban labour market, a constrained informal and small business sector, unsustainable and inefficient transport subsidies, and backlogs in basic urban services are all costs associated with the spatial distortions and unsustainable management and financing structures of urban areas. Reconstructing urban development to address the problems noted in paragraph 2 of the constraining realities, could significantly improve growth and equity at the national level. The reconstruction would depend on an effective strategy of managing the administration and the financing of the urban settlement process of at least 11 million out of the 18 million people finding themselves in urban areas. Reconstructing urban development is, thus, at once a most daunting and a most exciting element of the economic renaissance of this country.

What is at least required in this area is to properly plan the transformation of the country’s urban arrangements from the now abandoned system of functional and spatial separation, to the new paradigm of an economically integrated urban community. On the demand side, the cost of housing is largely a matter for the private sector, including the individual owner, the employer and private financial institutions. These resources should become available from domestic savings, largely in the same manner as has been the case with private residential investment throughout the country’s history. There is, however, widespread agreement that the basic needs, in this regard, of the very low-income groups will have to be met partially by a well-designed subsidy scheme from public funds.

On the supply side, urban land and housing policies would require rationalisation of current land use and zoning regulations to allow residential areas to be closer to centres of employment and economic activity. Under consideration is the densification and concentration of settlements which will take advantage of economies of agglomeration. This kind of land use planning has to tie in closely with other dimensions of urban planning such as transport systems, electrification, location of schools, hospitals, recreation areas and business areas. Expenditure on social and economic infrastructure will also lay claims on public funds. However, this expenditure should in addition to public outlays, be partly financed by development finance institutions, where outlays are largely recoverable, partly by public utilities such as Escom, and partly by the private sector where the debt structure would command appropriate servicing schedules.

Significant and immediate employment gains could result from considering employment-intensive methods in the design, provision and maintenance of socio-economic infrastructure. Furthermore, huge economic gains could be reaped immediately by creating a conducive business environment for informal and small business activities in black residential areas and along transport corridors linking these areas with the traditional areas of employment. Marginal investment and support by the public and private sectors would include: improvement of transport links with manufacturing and commercial centres near black residential areas; establishment of low-cost market places along transport corridors and within residential areas, including low-cost SBDC-type “hives”, accompanied by facilities that provide technical and managerial training programmes for emerging entrepreneurs; and revising zoning regulations to
allow for mixed land use, which will encourage small-scale manufacturing and commercial activities in residential areas.

The administrative and financial responsibilities and accountability for the public component of this process will devolve partly upon reconstituted local authorities, partly upon regional authorities and partly upon public corporations and development institutions operating on national, regional and local level. A very important and specific task of mutual coordination and cooperation among these several levels of management has to be undertaken. Furthermore, increased cooperation between public institutions and elements of civil society, such as NGOs, is important to combine the functional capacity of public institutions and the legitimacy enjoyed by e.g. the NGOs in the rendering of goods and services.

6.4 Reconstructing rural development

There is much that can be done to improve the ability of these areas to at least sustain their current population at more acceptable standards of living. Institutional improvements include security and exchangeability of land tenure, security in residence and employment, and fair working conditions. Infrastructural improvements to rural quality of life include access to health, educational services, consumer goods markets and the infrastructure supporting community life.

Economic programmes will focus on enhancing agricultural production by small farmers enjoying secure land tenure. More emphasis will also be given to "agribusinesses", i.e. commercial and industrial ventures serving agriculture in one way or another. Farming should increasingly be governed by price signals determined in competitive markets related to local and world commodity prices. Further deregulation of and increased competition in markets for commodities and farming inputs are important for economic efficiency. In view of limited public sector resource limits, "commercial farming" must rely increasingly on the private sector for farmer support services, while such services provided by or through government should continue to facilitate "emerging farmers" to achieve commercialisation.

7. A SAFETY NET

7.1 Transitional safety net

In the long run, all South Africans, and particularly the poor, would benefit from the economic restructuring through more rapid employment-creating growth, rises in real wages and continued government spending on social and economic services. Furthermore, the economic restructuring package itself has been designed to minimise social costs during transition. However, some people will still suffer job losses caused by changes in the expenditure pattern. A transitional safety net should be in place early during the proposed economic restructuring programme to preserve and reapply the skills and experience of people becoming thus unemployed, as far as possible.

This safety net includes a package of measures such as unemployment insurance, special training programmes, provision of information regarding job and training opportunities, support measures for small entrepreneurs and public work schemes. Public work schemes, per se, should be labour intensive and investment oriented, building up physical and human capital, should be targeted towards the unemployed/poor and should be relatively inexpensive to implement. Investment projects could be partly funded by the public sector capital account, particularly where planned fiscal outlays on capital projects can assume characteristics of public work schemes, and partly through foreign loans and aid.
7.2 On-going safety net

Fiscal provision for those on-going welfare and poverty programmes, which are well targeted and associated with endemic poverty, should not be adversely influenced by the envisaged restructuring and reduction of government recurrent expenditure. Current safety-net measures such as old-age pensions, disability grants, and drought and other emergency welfare funds should, however, be rationalised to cover poor and vulnerable groups more comprehensively and efficiently, within fiscal constraints. Welfare measures should be selective and targeted at specific categories of vulnerable and poor groups in society, eg. nutritional and medical support targeted at unemployed or poor mothers and their small children. Furthermore, the level and nature of welfare measures should not be such that they undermine participation in more development-oriented safety net measures or even gainful participation in the economy - particularly in rural areas. The rationalisation of education and health care services, mentioned earlier, would also benefit the poor.

8. THE BOTTOM LINE

8.1 The fiscal package

Table 6: The fiscal package

<table>
<thead>
<tr>
<th>Percentages of GDP</th>
<th>1992</th>
<th>1997</th>
</tr>
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<tbody>
<tr>
<td>A reduction in the &quot;balanced budget&quot; tax burden</td>
<td>30.7</td>
<td>24.4</td>
</tr>
<tr>
<td>Given the required elimination of government dissaving</td>
<td>4.8</td>
<td>0.0</td>
</tr>
<tr>
<td>Given the stickiness of interest on the public debt</td>
<td>5.2</td>
<td>5.7</td>
</tr>
<tr>
<td>A necessary reduction in government consumption and transfers</td>
<td>26.8</td>
<td>20.1</td>
</tr>
<tr>
<td>An increase in public sector investment</td>
<td>4.5</td>
<td>7.8</td>
</tr>
</tbody>
</table>

Accordingly, the reduction in government consumption and transfers from 26.8 per cent of GDP in 1992 to 20.1 per cent of GDP in 1997, forms an integral part of the strategy. This means that these outlays have to come down in absolute real terms by about 3 per cent between 1992 and 1997. By contrast, public sector fixed investment, which includes investment by the public corporations, is to rise substantially.

8.2 Managing the balance of payments

A major upset on the balance of payments, consisting of continued sharp declines in the net gold and other foreign exchange reserves and an eventual sharp depreciation of the exchange rate, would jeopardise the reform programme. Such an outcome would imply a resurgence of inflation and would necessitate a period of harsh monetary and fiscal policies, and possibly a reversal of certain trade reform measures, in order to restore equilibrium. However, the proposed programme provides for structural improvements which would lead to a healthier balance of payments and less susceptibility to such upsets.
The trade reform measures mentioned above are intended to improve the degree of openness and efficiency of the economy, implying increased imports as well as exports. Although imports, and the potential threat of imports, will increase, export opportunities will similarly be expanded by the commensurate reduction in the anti-export bias of the economy. Furthermore, the trade reform programme will be implemented in a gradual way, spread out over a period of several years and allowing a gradual redeployment of resources into areas of comparative advantage. As the surcharge is abolished and tariffs are gradually reduced, the rise in imports and concomitant increase in the demand for foreign exchange may be expected to lead to a lower nominal exchange rate. Within the environment of financial stability, this would imply little net movement in import prices, but somewhat higher prices for exports. In this way, the economy's anti-export bias will be reduced. The sectors expected to expand under these circumstances include primary production and manufacturing, and could, on average, be relatively more labour intensive and display a lower capital/output ratio than the present economy-wide averages.

Fixed investment, especially in manufacturing, has a relatively high import content. The considerable increase in fixed investment expenditure which is crucial to the programme may therefore be expected to add further imports to the increase which may be expected purely on account of trade reform. In contrast with earlier episodes during which imports rose rapidly when the economy moved into an upswing, imports of durable consumer goods may henceforth be less responsive, since proper control over the money supply and credit conditions will be maintained.

Nevertheless - and in spite of strong measures which will have to be taken in order to eliminate government dissaving and to improve saving by the domestic private sector - a financing gap will still remain, to be filled by foreign finance. This may especially be the case towards the middle of the five-year restructuring programme. Since the proposed economic reforms will clearly enhance the competitiveness and health of the economy, a gradual improvement in international perceptions of the risk-return profile of the South African economy may be expected. Taking South Africa's low level of international indebtedness into consideration, a reversal of the capital outflows of the past eight years is foreseen in the programme. It could lead to an average capital inflow amounting to 0.7 per cent of the gross domestic product over the programme period, with possibly much higher inflows in the middle years when investment would already have risen substantially but government dissaving would not have been eliminated.

In practical terms it is foreseen that the imports of capital goods would be financed mainly through suppliers' and other foreign credit. This would be encouraged by the South African authorities and its agencies involved in industrial and trade development, as is already the case under the E schemes. It would, of course, also imply that artificially low domestic interest rates would have to be avoided in order to encourage foreign rather than domestic financing. Non-inflationary fiscal policies would similarly have to be pursued in order to maintain foreign financier confidence in the ability of South Africa to meet its obligations. Access to the credit facilities of international organisations such as the IMF would also improve South Africa's international credit rating. The improvement that is primarily needed, however, is a perception that South Africa's economy is healthy, that its economic policies are sound and that it is politically stable.

Once the restructuring programme shows positive results, an increase in foreign equity (rather than loan) investment may also be expected.
8.3 Balancing total sources and uses

In summary, the proposed strategy addresses the macro-economic imbalances plaguing the South African economy primarily through supply-side measures. A gradual but firm policy style is to be followed, in which government dissaving is eliminated, freeing funds for more productive and employment-creating investment. Various instruments, including the lowering of nominal tax rates and deregulation, are to be used in order to encourage a strong expansion of private sector investment, while public sector investment is also to increase. The projected sources and uses of investment funds are summarised in the accompanying table.

Adequate savings, flowing through to productive investment, stimulating growth and employment, is therefore the sequence critical to the model. The projected allocation of fixed investment by broad institutional grouping is outlined in the accompanying graph. Future investment is to favour the lower capital/output ratio groupings.

The narrow macro-economic parameters within which investment and saving are to take place, are illustrated by the critical interim period that is envisaged by 1995. With higher investment and growth attained by that time, its sustainability would be critically dependent on a substantial capital inflow through the balance of payments, as well as a halving of the relative magnitude of government dissaving compared with such dissaving in 1992.

Table 7: Balance of total sources and uses

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<tr>
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<tbody>
<tr>
<td></td>
<td>%</td>
<td></td>
<td>%</td>
</tr>
<tr>
<td>Uses of investment funds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fixed investment</td>
<td>15.9</td>
<td>23.8</td>
<td>23.1</td>
</tr>
<tr>
<td>Inventory investment</td>
<td>-0.8</td>
<td>1.8</td>
<td>2.5</td>
</tr>
<tr>
<td>Total investment</td>
<td>15.1</td>
<td>25.6</td>
<td>25.6</td>
</tr>
<tr>
<td>Sources of investment funds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Provision for depreciation</td>
<td>15.3</td>
<td>15.6</td>
<td>15.3</td>
</tr>
<tr>
<td>Domestic savings</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- Personal</td>
<td>1.8</td>
<td>1.6</td>
<td>2.0</td>
</tr>
<tr>
<td>- Corporate</td>
<td>4.0</td>
<td>8.1</td>
<td>9.3</td>
</tr>
<tr>
<td>- Government</td>
<td>-4.8</td>
<td>-2.5</td>
<td>0.0</td>
</tr>
<tr>
<td>Capital flow</td>
<td>-1.0</td>
<td>2.8</td>
<td>0.0</td>
</tr>
<tr>
<td>Change in reserves (increase -)</td>
<td>-0.2</td>
<td>0.0</td>
<td>-1.0</td>
</tr>
<tr>
<td>Total sources/financing</td>
<td>15.1</td>
<td>25.6</td>
<td>25.6</td>
</tr>
</tbody>
</table>

Memo: GDP at 1985 prices R130bn R145bn R159bn
Figure 9 - Projected shifts in the structure of fixed investment

Capital/output ratios in 1991

Real gross fixed investment at 1985 prices

* Including public corporations
It must furthermore be stressed that, in the proposed programme, the assumptions have generally been made in such a way that the need for a sudden rather than gradual elimination of government dissaving is suppressed. For instance, the model allows for a capital inflow during the critical interim period; if this does not materialise for some reason, the gap would have to be filled by higher domestic savings. Similarly, even higher unattainably high-investment and savings may be needed to obtain adequate growth in employment and output if higher inflation, higher real wages or other shocks were to distort the paths foreseen in the model.

The above table illustrates the key macro-economic imbalances and their correction. Its relationship with micro-economic efficiency and the many other elements of the action programme should be borne in mind. Lower taxation and less government regulation and intervention would not only lead to higher private sector savings and investment, as shown in the table, but also to more productive and less distorted patterns of investment, employment and growth. Restoring macro-economic equilibrium is a necessary condition for sustainable growth and prosperity. However, efficiency, productivity, human qualities and various other issues that arise primarily on the micro-economic level are crucial in order to lift the South African economy into an orbit of prosperity.

9. NEXT STEPS

The normative model, and the suggested strategy based on it, thus establishes that a high rate of economic growth and gainful employment is within reach if private investment increases from its present level of 11.4 per cent of GDP to 15.3 per cent, and if the productivity of such investment in terms of value added and employment opportunities improves greatly over the averages recorded in recent years. It demands a return to financial stability and the elimination of dissaving by the government.

These are necessary conditions for placing South Africa back on a course of sustained growth. But they are of course not presented as sufficient conditions. Success depends upon the way in which the people of South Africa in their various institutional positions make their decisions and use their powers to take the kind of initiatives that will, in fact, result in the kind of growth process envisaged.

For this to happen, a great deal remains to be discussed, researched and negotiated. While private enterprise in a more competitive and unshackled economy is expected to take the lead in the pro-active processes of investment, employment and production, government agencies on all levels, trade unions and civic organisations generally have vital responsibilities.

Some of the commitments required of the fiscal and monetary authorities have been defined very clearly in the model, and have to be met if the social objectives are to be reached. But many of the principles, practices and relationships with regard to the future dispensation of political, fiscal and administrative responsibility in government still have to be thought through. This is an urgent task.

Finally, constructive co-operation within the so-called "golden triangle" of Labour, Enterprise and Government, is a further necessary condition for the return to prosperity along the road indicated in the model.
ANNEX B

CONFERENCE: BLUEPRINT FOR PROSPERITY
8 OCTOBER 1992

(The speech itself will deal succinctly with the topics discussed herein)

DR. STEF NAUDÉ

DEPARTMENT OF TRADE
AND INDUSTRY

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I. ECONOMIC RESTRUCTURING AND GROWTH

1. Introduction

Historically crucial processes already in place are moulding the Political and economic future of our country. The interaction of politics and the economy is evidenced with consistent regularity. The ability to harm the economy through reckless political action or statement is as obvious as the fact that economic growth is quite essential for an acceptable political transformation. Indeed, the responsibility of those who can directly influence these processes is a heavy one.

There is also no time to be lost. Anyone who understands the emerging success stories in Central and South America, and in Asia, and the implications of developments in greater Europe, must be seriously concerned by the harsh realities of our sub-Saharan Continent. That will include us, unless we bring about the economic success within our reach.

Michael Porter has shown that national prosperity is created, not inherited. It does not grow out of a country’s natural endowments, its labour pool, its interest rates or its currency’s value as classical economics insist. As a nation we have to prosper in a world of increasingly global competition, and the basis of competition has shifted more and more to the creation and assimilation of knowledge. We cannot isolate ourselves. This nation’s competitiveness inevitably depends on the capacity of our industry to innovate and upgrade. South African companies will only gain advantage against the world’s best competitors because of pressure and challenge. They will benefit from having strong domestic rivals, aggressive home-based suppliers and demanding local customers. There are no comfortable shortcuts to this arduous route. Porter reminds us that differences in national values, culture, economic structures, institutions and histories all contribute to competitive success. No nation can be competitive in every or even most industries. Ultimately, notions succeed in particular industries because their home environment is the most forward-looking, dynamic and challenging.

2. Some of our problems

The economy is now lingering in its longest postwar recession. From a policy point of view, it would have been much easier to revive economic growth if the poor performance of the economy was of a mere cyclical nature - as applies in the case of the major Industrial countries. South Africa’s economic problems are of a more fundamental nature, however. They are further complicated by the state of transition in which the country is involved.

South Africa, despite its modern sector, is largely a Third World country. As such it is grappling with the problems being faced by most of these countries, such as a high rate of population growth, rising unemployment, declining standards of living, inadequate literacy rates, a process of rapid urbanisation and increasing demands for socioeconomic upliftment programmes.

The basic challenge facing all of us, is whether we are going to allow matters to continue on the existing course or whether we are prepared to join forces to rebuild the economy from its present state of structural stagnation.

The answer to our economic problems is not to adopt reflationary fiscal and monetary policies, but to restructure the entire economy. We are fortunate in this respect that we do not have to start from scratch. South Africa has a low foreign debt ratio. A great deal of price stability has already
been established and the prospects for a further decline in the rate of inflation look promising. The balance of payments is in a fairly sound position and the effective exchange rate of the rand has been stabilised.

However, various crucial areas still need to be tackled. For this purpose the support of trade unions, the private sector and even extra-parliamentary groups is essential.

3. Economic restructuring

The Government is currently engaged in compiling a programme for the restructuring of the South African economy and the aim is to release it for discussion and comment about the middle of November this year. This programme does not constitute a blueprint for the future development of South Africa. It will serve as a discussion document to facilitate the formulation of future policies. It will quantify the resources available for economic development, identify the constraints that inhibit more rapid economic growth and indicate the outcome of alternative policy options. The debate of the last two or three years about alternative economic policy options has been extremely useful to identify the various problems South Africa is facing, but this exchange of views will become much more meaningful if the claims for success based on these policies could be subjected to a quantified appraisal. A test of this nature will certainly help to restrain a great deal of the loose talk and idle promises that have marked the economic debate thus far.

The main features of a policy of restructuring the South African economy are rather universal. This is so because they form the main cornerstones on which economic growth is based - such as productive fixed investment, higher multi-factor productivity, enhanced domestic and international competition, export-oriented growth, price stability, deregulation and discipline on the growth of public sector expenditure.

The outcome of any policy to revive future sustainable economic growth depends on the success with which we are able to address these matters. Some aspects, like public sector expenditure and deregulation, fall under the purview of the Government. The Government is also responsible for maintaining law and order and for determining economic policy. However, the private sector and labour are ultimately the major players that have to realise the growth potential of the country.

Policies to restructure a country's economy do not guarantee success. Political, social and economic stability are essential prerequisites to facilitate this objective, but the crucial question is whether the people of the new South Africa can transform their wants and needs into higher economic growth. Do they possess or can they acquire a culture to pursue economic growth?

Any populist policy of satisfying needs via redistribution not accompanied by higher economic growth, is doomed to failure. The sooner we realise and embrace this truth, the easier it will be to work together to tackle the economic challenges that lie ahead.

4. Requisites for sustained economic growth

A growth rate of 4 per cent per annum for which we should be aiming, will be sufficient to ensure a per capita increase in living standards of slightly more than one per cent per annum. It will do that, unless labour costs per unit produced continue to increase at the rates that have been recorded during recent years. It will also enable the formal sector of the economy to absorb the annual entrants
to the labour market, but it will provide little scope for reducing unemployment and the backlogs existing in respect of socioeconomic services. Clearly, therefore, our aim should be to perform better than this growth target.

To realise this objective implies (even if we assume a more optimistic capital-output ratio) that we will have to increase gross fixed investment from its current level comprising about 18 per cent of the gross domestic product to about 25 to 26 per cent. Can we do this? How do we finance such a rising level of investment?

Do we merely have to extrapolate past trends in respect of the employment creating capacity related to economic growth, the capital-output ratio, the capital-labour ratio, labour productivity, etc? Or is there reason to believe that we can arrest or even reverse these trends? Our success in improving the performance of these relationships will determine the success of a policy for restructuring the economy in our quest to promote higher sustainable economic growth.

A lower capital-output ratio implies a higher level of fixed investment to realise a certain rate of economic growth. Where do we find the capital to finance a higher level of fixed capital formation? Our first aim should be to increase domestic saving, eg by phasing out dissaving by the public sector, and to use the available savings as productively as possible. We should, secondly, try to stem the net outflow of foreign capital with the longer term aim of reversing this process.

There are clearly no easy options or quick fixes for the economic challenges facing South Africa. We will simply have to scale down many unrealistic expectations and be prepared to make short-term sacrifices to reap the long-term benefits of higher sustainable economic growth.

South Africa has a particularly open economy, which means that the economy is not only susceptible to extraneous foreign developments, but more importantly that its products should be cost- and quality-wise competitive. We are already in the process of devoting an increasing share of our budgetary resources to education and training, which will help to raise labour/capital productivity and to promote vertical labour mobility. South Africa is a labour surplus country and its policies should hence be directed towards using more labour intensive production techniques. It costs, in terms of 1985-prices, an outlay of about R 54,000 in the private sector to create employment for one additional worker. The total labour force increases currently by almost 400,000 per annum and it will consequently need an investment approaching R 19 billion, expressed in 1985-prices, to employ 350,000 of these annual new entrants to the labour market in the private sector. Total gross private fixed investment in 1991, measured in terms of 1985-prices, amounted to only R 16 billion, which comprises replacement investment as well, which serves to indicate the magnitude of the challenge which we are facing.

South Africa is well served with infrastructural services, such as electricity, roads, rail transport, harbours and communication networks, which are essential to accommodate economic growth. In fact, we currently have a surplus capacity in most of these areas and therefore do not need to invest a meaningful share of our scarce capital resources in structures of this nature. We have great backlogs in housing for the lower income families, which we will need to tackle in terms of a long-term housing strategy, but the often held populist view that a housing kick-start would make a major contribution towards reviving economic growth has lost its credibility.
5. **Industrial growth crucial**

South Africa’s future economic development depends largely on industrial growth, which will also have to be much more export-oriented in order to increase the import capacity of the economy.

The gold mine sector has become a declining industry, measured in terms of employment, generator of income, earner of foreign exchange and as a source of tax revenue, during the past decade. This decline has imposed a process of painful adjustment on the economy that is still in progress.

Likewise agriculture, plagued by droughts, a deterioration in the terms of trade and suffering from a high rate of increase in input costs, has become the soft underbelly of the economy and has recently needed substantial government assistance in order to maintain its productive capacity.

Favourable weather conditions may help to improve future agricultural production, but the fact remains that South Africa’s long-term growth prospects rely heavily on industrial development. In this respect a mixture of highly capitalised, labour intensive, small, medium and large sized enterprises can all make a meaningful contribution. South Africa, on account of its natural resources, enjoys certain comparative cost advantages for industrial development and it is imperative that we should not allow these development opportunities to go begging on account of misdirected policies.
II. SOME IMPORTANT ELEMENTS OF INDUSTRIAL AND TRADE POLICY

1. Introduction

Two simple realities must be emphasized at the outset. The first is that far-reaching local and international developments will require particularly careful and realistic management of our industrial and trade policies in the years to come. Some of the developments directly affecting these policies are the rapid changes in South Africa and our region, in the three main trading blocs in the world and in the multilateral trade rules suffering from the uncertain outcome of the Uruguay Round of the GATT negotiations. The second reality is that many countries across the globe offer extremely attractive industrial investment, export and R & D incentives, or provide non-tariff protection in a variety of ways. All affect competitiveness. In a tough and increasingly competitive world we cannot in our policymaking afford the naivete of ignoring what does not suit our purist tastes.

Expansion of manufacturing industry has to be the mainstay in the build-up to real growth in gross domestic product of about 4 per cent annually by 1996. This requires that the investment ratio of manufacturing industry rises to about 8 per cent of gross domestic product in coming years, instead of just more than 4 per cent at present.

A new round of investment in manufacturing industry will also have to set the pattern for structural adjustments important in obtaining more rapid industrialisation. Reliance on import substitution and the establishment of strategic industries have drawn to a close. Consequently future wealth will have to be derived increasingly from penetration into export markets. Trade and industrial policy thus needs to focus on the improvement of competitiveness in support of export driven growth, expansion of employment and wealth.

The advent of export orientated growth is going to place South Africa’s industry more fully in the international competitive environment requiring investment conditions comparable to those found in competitor countries to facilitate investment dedicated to export. While improvement in the investment climate is essential in obtaining the desired investment ratio, the different facets determining the overall investment climate will take quite some time to come into place in a satisfactory fashion. Investment to effect specific structural adjustments in the quest for higher growth, will thus continue to rely on selective support for the time being. Even when the overall investment climate has improved satisfactorily, the need for some incentives will remain as part and parcel of the industrialisation process, as experience locally and in most countries has demonstrated. However, incentives should facilitate the proper working of market forces. Their aim should be to upgrade the different resources in the production process, ie labour, capital, technology, natural resources and entrepreneurship, for South African industry to remain in the international productivity place.

1The term structural adjustment is used in a broader and in a narrower sense.

In the broader sense it refers (as in Part 1) to policy changes of a general nature viz. the change from inward towards outward orientation in economic and industrial policy.

In the narrower sense it refers to a set of measures that a government in a market economy can use to improve the competitiveness of individual sectors or branches of industry by intervention in the process in which resources are used.
The emphasis in trade policy is to shift from import replacement towards strong export orientation. This change in direction sets the pattern for future industrial policy. Modification of protection policy is discussed in the next paragraph and the more important aspects of industrial and trade policy in the following ones.

2. Reform of tariff protection policy

(a) The need for tariff reform

South Africa has for many decades followed a policy of import replacement to promote industrial and general economic development. Import replacement was promoted and supported by selective tariff protection and quantitative import restrictions. It has been realised for some time now that this policy will not be able to generate sufficient economic growth, new employment and wealth as the import replacement opportunities have been depleted to a large extent. A change in direction towards export-led growth has become essential. Many countries that have relied on the import replacement route are now embarking on trade liberalisation and export orientated growth, as the latter had been demonstrated as the superior development route by the successes achieved by the newly industrialised countries.

With the removal of most sanctions and the promotion of International trade liberalisation by GATT, we are at the same time encouraged and indeed forced to embark on an export-driven growth path. We should, moreover, diversify towards the exportation of manufactured final products as the global trade in such products rises at a much higher rate than trade in primary products. Their prices are significantly more stable than those of commodities, introducing more stability on the balance of payments, and they also tend to be more labour intensive than many commodity exports.

The Uruguay Round of trade liberalisation of the GATT is aimed at the expansion and progressive liberalisation of world trade. If South Africa is to embark on a strategy of export-driven industrial development, we need to ensure that existing external markets remain open to our products and that entry is offered into new ones. To ensure that, we have to participate in the Uruguay Round and to accept 'the obligations of participants. One of these is a phased lowering of tariff protection. As is required from all participants in the Uruguay Round, South Africa submitted in 1990 an offer for the lowering of tariffs and the eventual binding thereof at specified levels.

Following deliberations on tariff policy since the offer was submitted, the Department of Trade and Industry is at present reviewing it to establish whether it is in fact the optimum one in terms of our present circumstances, future trade policy, and the expectations of our trading partners. The review, which may result in modification of the original offer, will be completed shortly and published thereafter.

(b) Approach

Against this background government proposes to introduce tariff reductions as part of a suitable industrial policy with the aim of:

- upgrading the international competitiveness of the manufacturing industry;
- obtaining a higher rate of growth in manufacturing industry, exports, employment and wealth;
obtaining better value for money by the local consumer through competition, improved product quality and customer service;
- lowering inflation and inflationary expectations; and
- arriving at a more simplified, stable and uniform tariff involving less manpower in its administration.

Trade liberalisation is associated with significant risks if not managed carefully. South African industry was largely built-up behind protective walls. Therefore, industrial growth, the balance of payments and employment may suffer if the evolvement towards better international competitiveness is not managed carefully. Broad acceptance and success with improvement of competitiveness and tariff reform will thus be fostered by discussion in the Economic Forum. On the sectoral level deliberations between Government, business and trade unions involved in that particular industry will take place on matters such as the management and the phasing of tariff reductions, incentives, the best ways whereby competitiveness can be improved, and ways of increasing the industry’s share in world trade. For this purpose a Task Group was launched recently for the Textile and Clothing industries. Another will be launched for the Motor Industry (Phase VII) within days. In both instances a long term strategy based on viability and competitiveness is aimed at.

High duties in many instances arise from the use of formula duties for protection against low but normally priced goods, dumping and disruptive competition. It has been decided to do away with formula duties and legislation has been accepted allowing for more conventional methods to act against dumping and disruptive competition. The new procedures are now being implemented as the first step in tariff reform.

The pace and magnitude of tariff reform should be dictated by the progress that is going to be made with the improvement of the competitiveness of manufacturing industry. Progress with improvement of competitiveness, on its part, depends on the ability to afford incentives on the supply side for modernisation of production facilities, training and re-training of labour, development of technology and the advances that need to be made in improving the investment climate.

Studies that were done since the release of the IDC’s proposals on the modification of the tariff protection policy, concur with its findings and recommendations that trade liberalisation should be accompanied by supply-side measures on the macro and sectoral level. Tariff reductions on their own are considered insufficient in shifting resources meaningfully into either export dedicated development or in investment to improve the competitiveness of existing production processes.

In view of the tight fiscal situation, it is difficult, for instance, to lower significantly the corporate tax rate and to scrap the import surcharges in an effort to improve the investment climate. Assistance for improvement of competitiveness should be available for those industries where significantly lower tariffs were offered in the Uruguay Round of trade negotiations. These industries are mostly highly protected and often labour intensive.

The Department of Trade and Industry is responsible for the implementation of tariff reform. It is assisted by the Board on Tariffs and Trade, which is responsible for specific tasks relating to tariffs as such and the IDC, for technical investigations into tariff reform and improvement of competitiveness. The Department is also responsible for liaison with the Department of Manpower and other government
departments and institutions relevant to tariff reform and improvement of competitiveness, as well as with the GATT and the BLNS countries.

(MORE INFORMATION ON INDUSTRIES, POLICIES AND PROCEDURES INVOLVED IN TARIFF REFORM APPEAR IN THE ANNEXURES TO THIS REPORT.)

3. **Investment climate**

At present investment suffers from some basic disadvantages vis-à-vis foreign competitors. These need to be rectified by consistent application of prudent fiscal, monetary and other policies in support of internationally competitive investment in real economic activity. Investment can be expected to improve according to success achieved on the following:

**Inflation**

Lowering of inflation to rates comparable to those of our major trading partners, thereby removing the disadvantages associated with and need for higher nominal interest rates domestically, and offering the advantages of better price stability in investment decisions.

**Lowering of corporate tax rate**

Lowering of the corporate tax rate in compensation for the removal of tax expending over the past couple of years.

**Improvement of savings**

Rehabilitation of savings in the economy to finance investment with the emphasis on rehabilitation of saving by Government. Fostering of foreign investment even by considering investment guarantees.

**Exchange rate**

Maintaining stability in the real exchange rate. Export driven industrialisation and trade liberalisation are frustrated by overvaluation and it is facilitated substantially by a lower external value of the currency. The latter simultaneously reduces the need for and level of selective export subsidies. Depreciation in many countries served to reduce tariffs. Major changes in policy by the monetary authorities, eg review of exchange control which may result in changes in the exchange rate, should in future be harmonised with trade and industrial policy.

**Import surcharges**

Doing away with import surcharges as an impediment to investment.

**Labour**

Stabilisation of labour costs and improvements in real labour earnings to be derived from rising productivity brought about by training, re-training and investment in internationally competitive production technology. Stabilisation of labour relations inter alia, through consensus on important structural adjustments between Government, business and labour.
4. Incentives

The investment climate will only improve to a desired extent in time. As a consequence selective support measures need to play a more prominent role than otherwise, in effecting desired structural adjustments and improvement of competitiveness. Supportive measures can be divided into two broad groups according to their aims, ie for improving the competitiveness of protected industries and for lending support to export, respectively.

(a) Improvement of competitiveness of protected industries

The Industrial Development Corporation intends to offer loans at preferential interest rates to industries requiring upgrading of their competitiveness by investing in modern plant and equipment in view of changes in tariff policy.

Success in improving international competitiveness of industry, especially that of the more labour intensive ones, depends on a productive labour force. Upgrading of labour resources by training and re-training of employees will require progressively more support depending on success being achieved in expanding the industrial labour force. This conforms to the validity of experience that consistent upgrading of resources is the better way to pursue lasting competitiveness, in contrast to export subsidies and high protection, which essentially only attempt to cancel out cost disadvantages vis-a-vis international competition. The Departments of Trade and Industry and of Manpower will have to act on needs for training and re-training as it arises from deliberations between Government, business and trade unions in improving the competitiveness of specific industries.

(b) Exports

(i) Tax

Export assistance has been reduced substantially in recent years with the termination of the exporters allowance under section 11 bis of the Income Tax Act and the substitution of GEIS for the Category A and B assistance. The electricity subsidy for mineral beneficiation is to be phased out at the end of 1992.

In 1991 provision was made in terms of section 37E of the Income Tax Act to support, on a temporary basis, a new round of investment in processing industries by adjusting the conditions for depreciation of fixed assets. The provision aims to enable companies to take advantage of South Africa’s competitive advantage in natural resources and energy costs. Substantial investment is planned in the metallurgical, chemical and some other industries dedicated to export. Progress with corporate tax reform will determine the need for extending the life of 37E, especially that part of the provision allowing for negotiable tax certificates to improve the cash position of companies during construction. The 37E provision is presently scheduled to terminate by September 1993.

(ii) Preferential interest rates

The Industrial Development Corporation offers loans at concessionary interest rates to small and medium sized firms, (ie firms with less than R 100 million in assets) for installation of export capacity, introduction of multi-shifts in existing plants to improve capital productivity and for the infrastructure and accommodation required to cater for the predicted growth in tourism.
Possibilities for more downstream manufacture for export, especially as a result of internationally competitive supply of materials by existing and envisaged metallurgical and other processing industries, are being investigated. Downstream manufacture is invariably more labour intensive than the processing stage. Preferential interest rates as a support measure will be considered in conjunction with the available incentives, to exploit opportunities offering potential comparative advantage.

(iii) Export subsidies

GEIS introduced a reduction of export subsidies in that a large proportion of exports already competitive in international markets, which previously enjoyed Category A & B assistance, were excluded from GEIS benefits. Assistance was furthermore selectively categorised according to stage of fabrication with the subsidy margin higher the more advanced the stage of fabrication.

Export is openly subsidised by GEIS in contravention of the GATT and consideration will need to be given to phasing out the scheme if the Final Act of the Uruguay Round is implemented as it reads at present. The effectiveness of the scheme is also questioned on its ability to stimulate investment since industrialists fear that the subsidies may not last for very long. For this reason assurances were given that GEIS will continue at least up to 1995. The scheme is sometimes also criticised due to the large amount spent on subsidising export sales while spending on the input side for the upgrading of resources may be more economical and may eventually result in more lasting competitive benefits.

Despite these shortcomings, many exporters strongly rely on GEIS and the export drive, especially in respect of fully manufactured goods, will suffer, if alternatives with substantial impact is not put in place on the occasion of its disappearance.

In revising GEIS due consideration needs to be given to supply side measures that can help in upgrading competitiveness by investment in state-of-the-art production facilities, improved training and re-training and technology development. It may well be possible to blend a revision of GEIS into the consultation process between Government, business and unions, for those industries due for tariff reform. A switch to supply side assistance has the added advantage in that it also benefits the local consumer.

(c) Innovation

International trade is dominated by technology intensive products while trade in primary products is becoming less important. It is difficult for a manufacturer to compete with existing products in established markets. Existing products are usually protected by patents. Manufacturing under licence can serve the local market but licensing agreements usually preclude exports and contain other restrictive clauses.

Product innovation or product differentiation is generally regarded as the key to achieving market share in international markets. The market-creating effect of product innovation is of vital importance and not so much the level of technology, ie high or low technology.

Technological advances in product and process development, together with investment in modern plant and persistent upgrading of human resources is the mainstay in pursuing competitive industrialisation. South Africa can boast an excellent science and technology infrastructure with well
established research institutions. Circumstances should be created that will enhance the propensity of the private sector to make more use of the research infrastructure.

The stimulatory measures that could be introduced by Government are:

- threshold assistance to stimulate research and development and innovation by the private sector;
- application of the buying power of the State to promote product development; and
- technology programmes to prepare South African industry for future growth markets.

5. Export marketing and international economic relations

The ability to enter into new markets and the opening-up of new markets are of vital importance in restructuring manufacturing industry towards international competitiveness. Export marketing incentives and the broadening of trade relations in the post-sanctions era are pursued to broaden the scope of internationalisation of South African products.

(a) Export Marketing Assistance

The export marketing assistance scheme to ease entry into new markets is in force for traded goods and ways and means for its extension to invisible exports are being investigated by the Department of Trade and Industry.

(b) Development of New Markets

The disintegration of international communism during 1989 and the political initiatives of the Government since early 1990 have led to the dismantling of international sanctions against the RSA and has started the process of normalising our foreign trade and trade relations with countries with which the RSA had been trading traditionally as well as the so-called new market countries.

Since the RSA does not dispose of sufficient financial and manpower resources to establish trade representation and to conclude trade agreements with all countries, it became necessary to determine geographical priorities. The considerations according to which these priorities were determined also served as a basis for advice to the export community.

For the purpose of establishing priorities three broad categories were defined:

- the preservation and strengthening of trade relations with the RSA’s traditional trading partners;
- the resumption of previous trade relations; and
- the establishment of new trade relations.

As far as the first group is concerned many efforts have already been made in placing the RSA’s trade with the European Community, the USA and Canada, the Far-East, South America and Israel,
on a sound basis. Efforts have also been made for an institutionalised dialogue with the EC while the institutionalisation of the RSA’s trade relations with Japan in terms of a trade agreement is being considered. A trade agreement will also shortly be concluded with Israel.

As far as the resumption of trade relations with countries such as Sweden and Australia are concerned not much progress has been made. Both these countries still maintain sanctions against South Africa. In the case of Angola the situation has been largely normalised and interesting opportunities are available to the RSA in the reconstruction of Angola’s economic infrastructure.

Significant progress has been made with the establishment of new markets. The process in this regard started mainly in Central- and Eastern Europe and our trade and trade relations with countries such as Poland, Hungary, Czechoslovakia, Romania, Bulgaria and Russia are today largely normalised. Trade agreements have been concluded with the first four countries while agreements with Bulgaria and Russia are presently being negotiated. Trade with Finland and the Baltic States has also to a large degree been normalised.

After the successes in Europe, the emphasis has shifted to the Far East. Good progress has already been made and countries such as the People’s Republic of China, South Korea, the Philippines, Thailand and Singapore, have lifted their sanctions against the RSA. The attitude of Malaysia, Indonesia and India is also softening.

Interesting breakthroughs have also been made in the Middle East and Africa. Although the Arab League have not yet lifted sanctions, the United Arab Emirates re now openly allowing South African products and our relations with Bahrain and Oman are swiftly being normalised. Egypt still maintains sanctions but the climate has already improved significantly. In Africa relations have been normalised with Mauritius and Morocco.

South Africa’s trade and trade relations over the last three years have, therefore, largely been normalised and globalized. Although sanctions have not disappeared completely as yet, the problems they created for the RSA in general and the South African export community in particular, are not insurmountable.

(c) Reclassification of status to “developing”

Trade agreements with individual countries as well as with trading blocs such as the EC will play an important role in our increasingly outward orientation. The conditions under which such agreements are entered into are determined, among others, by a country’s economic development status. In this regard the GATT places an obligation on developed countries to grant trade preferences to developing countries. The latter hereby obtain access to the developed countries’ markets under more favourable conditions than provided for under the GATT’s most favoured nations treatment.

At present, South Africa is classified as a developed country within the GATT. However, for economic reasons South Africa is in no position to grant preferential treatment to developing countries. In fact, South Africa needs rather to receive preferential treatment from its developed trading partners such as the EC and the USA. For this reason, a reclassification of South Africa’s economic status has become essential.
There is no legal definition in the GATT of a developing country. If South Africa were to announce that it wishes to redesignate itself, this would probably be accepted internationally. However, such a declaration of intent would not make South Africa automatically eligible for preferential treatment. South Africa will have to enter into negotiations with each of its developed trading partners with a view to entering into preferential trade agreements. The successful conclusion of such agreements will, however, depend entirely on the willingness of the developed trading partners to recognise South Africa’s status as a developing country.

Since all preferential trade agreements, on their successful conclusion, are prima facie contrary to the GATT rules, they will have to be reported to the GATT. Any member of GATT which is of the opinion that its trading interests would be damaged by the preferential agreements, could then formally challenge them.

In terms of existing criteria South Africa should experience little difficulty with a reclassification of its economic status. These criteria include, among others, aspects such as population growth, life expectancy, infant mortality rate and literacy. South Africa also has many trading characteristics of a developing country, especially its heavy dependence on the export of primary commodities. Its seven principal exports account for 60 per cent of total exports while the figure for developed countries ranges between 30 and 35 per cent.

While sanctions and other restrictive measures are rapidly vanishing, South Africa will have to face new challenges. New trading blocs are being formed in the Americas and elsewhere whilst in Europe a single market is already a reality. Reclassification as a developing country could assist South Africa in its efforts to obtain access to those markets on a preferential basis. This would assist economic growth and release South Africa from its obligation to grant similar concessions to its developing trading partners.

(d) The Region: Southern African Customs Union

The most important benefit for South Africa from the SACU is the considerable expansion of the local market which it provides through the free flow of goods in the area (Botswana, Lesotho, Namibia and Swaziland). It presents two major problems, effectively crippling it as a suitable vehicle for expanded regional cooperation. The first is that on the present formula the massive and rapidly growing payments to our partners are becoming unaffordably high to us. The distribution formula of the common income pool has the effect that the BLNS countries receive a minimum payment equal to 17 per cent of the value of their total imports, including their imports from South Africa which of course make no contribution to the pool. In the 1991/1992 financial year an amount of R 2,500 million was paid to these countries. This year their cumulative share has grown to R 3,055 million. Ultimately South Africa retained 43 per cent of the pool to which it contributes more than 90 per cent. The second problem is that diverging industrial policies regarding protection levels, as well as differences in levels of industrial development, will increasingly strain the relations within the SACU.

Much attention is given in various quarters to the development of an appropriate model for regional cooperation in Southern Africa - a matter which is not made easier by the extreme differences in industrial development. Apart from obvious reasons, such a development will have significance for relations with other blocs, particularly the European community.
6. Freeing of Markets

The thrust of trade and industrial policy is to improve competitiveness of industry allowing for the freeing of markets by reducing import protection and supporting penetration into international markets. The policies and supportive measures as described in this chapter are to be supplemented by steps to deregulate trade and industry and by increased dissemination of trade and market information. The merits of Export Processing Zones is presently being evaluated by the Department of Trade and Industry as a means to strengthen export production and employment.

7. Small and Medium Size Business

The importance of the promotion of small and medium sized businesses in this country with its development needs and its high degree of economic power concentration and conglomeration, is fully understood. However, the implementation and financing of this promotion are highly fragmented.

About fourteen government departments are involved in the formulation of policy on small business development of which the Departments of Trade and Industry, Manpower, Finance and Regional and Land Affairs are the more important. On the financing side, thirteen development agencies are involved comprising of the IDC, SBDC, SADB and the different homeland development corporations. About ten institutions are involved in advisory services rendered to small businesses.


Each of the departments, and many but not all of the development agencies, are financed by central government to fund the respective small business development efforts that they pursue. The Department of Trade and Industry’s budget for 1992/1993 provides for R 19 million of which R 5.3 million is for advisory services and R 4.2 million for rent subsidies advanced to small industries. The budget of the Department of Trade and Industry also provides for rebates on the tariffs charged by private consultants for the services that they render to small business. It also provides for a credit guarantee fund. The IDC contributed R 13 million p.a. to the funding of the SBDC over the past five years.

The amount budgeted for the development corporations of the self-governing states amounts to R240 million for 1992/1993. These funds flow through the Department of Regional and Land Affairs but the governments of the self-governing states are responsible for the allocations to their respective development corporations.

Development agencies therefore advance about R 700 million annually to small business development. Government’s annual contribution to these funds is R 280 million.

A substantial portion of the funds involved in the Regional Industrial Development Programme (RIDP) is for small industries. This is in addition to the funds mentioned above. As can be seen from
the next paragraph, R 100 million p.a. is budgeted for under the RIDP in new financing on a five year cycle. The amount will thus build up to R 500 million in the fifth year. The overflow in commitments under the previous RIDP is about R 700 million p.a. The Department of Regional and Land Affairs administers the RIDP.

It is the intention of the Department of Trade and Industry further to facilitate small and medium business development. Clearly, however, some rationalisation in the structure and funding of this promotion has become essential.

8. Regional Development

The Regional Industrial Development Programme (RIDP) was changed on 1 May 1991.

The previous Regional industrial Development Programme (RIDP) aimed at off-setting regional comparative disadvantages, in an attempt to induce a more equal distribution of economic activity country-wide. The programme, which encompassed the RSA and the TBVC-States, offered incentives at select development points to attract investment in industry to the lesser-developed regions. The incentive package therefore provided for a multitude of incentives differentiated according to regional and development aspects. Despite the good economic performance of concessionaires, the programme by its very nature, was extremely difficult to administer, complicated and financially open-ended. The programme was also discredited in many quarters as manifestation of the apartheid era.

The new RIDP, introduced with effect from 1 May 1991, have the following objectives:

- the development of an integrated Southern African economy;
- the promotion of regional development as an objective in its own right, but in such a way as to contribute to improving the performance of the Southern African economy as a whole, with particular emphasis on the development of the less developed areas;
- a market-oriented approach to regional development;
- a free flow of production factors; a balanced multi-sectoral development approach supported by regional development strategies based on comparative locational advantages; and
- a market-oriented profit/output-based incentive scheme.

The incentive package for the RIDP was changed from a locational disadvantage basis to a performance based package.

The incentive package comprises of:

- a tax-free establishment grant in cash, based on investment up to a maximum of R 15 million, payable for a period of two years, subject to a minimum threshold requirement of 35 per cent operational equity to qualify for concessions; a tax-free cash allowance based on the undertaking’s profits, payable for three years, not to exceed the equivalent establishment grant in any year; and
- the reimbursement of relocation costs of approved foreign industries up to a maximum of R 1 million per project.

The differences in assistance according to geographic region has been simplified to the following three levels:

(i) PWV complex and Durban core area: no incentives.
(ii) Cape Peninsula and Durban/ Pinetown/Pietermaritzburg and larger Durban Functional Region (excluding the Durban core area) and the decentralisation areas around the PWV: 60 per cent of the calculated establishment grand during the first two years and 100 per cent during the last three years’ based profits.
(iii) All other areas: 100 per cent of incentives.

The incentives will apply on a tiered basis for a period of five years. An amount of R 100 million has been budgeted for 1991/92, R 200 million for 1992/93 until a level of R 500 million is reached, corresponding to the five year cycle of the incentives. Outstanding commitments under the previous RIDP resulted in an amount of R 696 million being budgeted for 1992/93 and R 548 million for 1993/94. It is expected that the requirements will reduce drastically in 1997 and 1998 when commitments under the previous programme draws to a close.